AUTHENTICATED
U.S. GOVERNMENT
INFORMATION
GPO

# FEDERAL REGISTER

Vol. 78 Wednesday,
No. 118 June 19, 2013

Part II

## Securities and Exchange Commission

17 CFR Parts 210, 230, 239, *et al.*
Money Market Fund Reform; Amendments to Form PF; Proposed Rule

## SECURITIES AND EXCHANGE COMMISSION

### 17 CFR Parts 210, 230, 239, 270, 274 and 279

**[Release No. 33–9408, IA–3616; IC–30551; File No. S7–03–13]**

**RIN 3235–AK61**

## Money Market Fund Reform; Amendments to Form PF

**AGENCY:** Securities and Exchange Commission.

**ACTION:** Proposed rule.

**SUMMARY:** The Securities and Exchange Commission (''Commission'' or ''SEC'') is proposing two alternatives for amending rules that govern money market mutual funds (or ''money market funds'') under the Investment Company Act of 1940. The two alternatives are designed to address money market funds' susceptibility to heavy redemptions, improve their ability to manage and mitigate potential contagion from such redemptions, and increase the transparency of their risks, while preserving, as much as possible, the benefits of money market funds. The first alternative proposal would require money market funds to sell and redeem shares based on the current market-based value of the securities in their underlying portfolios, rounded to the fourth decimal place (*e.g.,* $1.0000), *i.e.,* transact at a ''floating'' net asset value per share (''NAV''). The second alternative proposal would require money market funds to impose a liquidity fee (unless the fund's board determines that it is not in the best interest of the fund) if a fund's liquidity levels fell below a specified threshold and would permit the funds to suspend redemptions temporarily, *i.e.,* to ''gate'' the fund under the same circumstances. Under this proposal, we could adopt either alternative by itself or a combination of the two alternatives. The SEC also is proposing additional amendments that are designed to make money market funds more resilient by increasing the diversification of their portfolios, enhancing their stress testing, and increasing transparency by requiring money market funds to provide additional information to the SEC and to investors. The proposal also includes amendments requiring investment advisers to certain unregistered liquidity funds, which can resemble money market funds, to provide additional information about those funds to the SEC.

**DATES:** Comments should be received on or before September 17, 2013.

**ADDRESSES:** Comments may be submitted by any of the following methods:

### Electronic Comments

- Use the Commission's Internet comment form (*http://www.sec.gov/rules/proposed.shtml*); or
- Send an email to *rule-comments@sec.gov*. Please include File Number S7–03–13 on the subject line; or
- Use the Federal eRulemaking Portal (*http://www.regulations.gov*). Follow the instructions for submitting comments.

### Paper Comments

- Send paper comments in triplicate to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, 100 F Street NE., Washington, DC 20549–1090.

All submissions should refer to File Number S7–03–13. This file number should be included on the subject line if email is used. To help us process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet Web site (*http://www.sec.gov/rules/proposed.shtml*). Comments are also available for Web site viewing and printing in the Commission's Public Reference Room, 100 F Street NE., Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. All comments received will be posted without change; we do not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly.

**FOR FURTHER INFORMATION CONTACT:** Adam Bolter, Senior Counsel; Brian McLaughlin Johnson, Senior Counsel; Kay-Mario Vobis, Senior Counsel; Amanda Hollander Wagner, Senior Counsel; Thoreau A. Bartmann, Branch Chief; or Sarah G. ten Siethoff, Senior Special Counsel, Investment Company Rulemaking Office, at (202) 551–6792, Division of Investment Management, Securities and Exchange Commission, 100 F Street NE., Washington, DC 20549–8549.

**SUPPLEMENTARY INFORMATION:** The Commission is proposing for public comment amendments to rules 419 [17 CFR 230.419] and 482 [17 CFR 230.482] under the Securities Act of 1933 [15 U.S.C. 77a—z–3] (''Securities Act''), rules 2a–7 [17 CFR 270.2a–7], 12d3–1 [17 CFR 270.12d3–1], 18f–3 [17 CFR 270.18f–3], 22e–3 [17 CFR 270.22e–3], 30b1–7 [17 CFR 270.30b1–7], 31a–1 [17 CFR 270.31a–1], and new rule 30b1–8 [17 CFR 270.30b1–8] under the Investment Company Act of 1940 [15 U.S.C. 80a] (''Investment Company Act'' or ''Act''), Form N–1A under the Investment Company Act and the Securities Act, Form N–MFP under the Investment Company Act, and section 3 of Form PF under the Investment Advisers Act [15 U.S.C. 80b], and new Form N–CR under the Investment Company Act.[1]

### Table of Contents

I. Introduction
II. Background
A. Role of Money Market Funds
B. Economics of Money Market Funds
1. Incentives Created by Money Market Funds' Valuation and Pricing Methods
2. Incentives Created by Money Market Funds' Liquidity Needs
3. Incentives Created by Imperfect Transparency, Including Sponsor Support
4. Incentives Created by Money Market Funds Investors' Desire To Avoid Loss
5. Effects on Other Money Market Funds, Investors, and the Short-Term Financing Markets
C. The 2007–2008 Financial Crisis
D. Examination of Money Market Fund Regulation Since the Financial Crisis
1. The 2010 Amendments
2. The Eurozone Debt Crisis and U.S. Debt Ceiling Impasse of 2011
3. Our Continuing Consideration of the Need for Additional Reforms
III. Discussion
A. Floating Net Asset Value
1. Certain Considerations Relating to the Floating NAV Proposal
2. Money Market Fund Pricing
3. Exemption to the Floating NAV Requirement for Government Money Market Funds
4. Exemption to the Floating NAV Requirement for Retail Money Market Funds
5. Effect on Other Money Market Fund Exemptions
6. Tax and Accounting Implications of Floating NAV Money Market Funds
7. Operational Implications of Floating NAV Money Market Funds
8. Disclosure Regarding Floating NAV
9. Transition
B. Standby Liquidity Fees and Gates
1. Analysis of Certain Effects of Liquidity Fees and Gates
2. Terms of the Liquidity Fees and Gates
3. Exemptions To Permit Liquidity Fees and Gates
4. Amendments to Rule 22e–3
5. Exemptions From the Liquidity Fees and Gates Requirement
6. Operational Considerations Relating to Liquidity Fees and Gates
7. Tax Implications of Liquidity Fees
8. Disclosure Regarding Liquidity Fees and Gates

[1] Unless otherwise noted, all references to statutory sections are to the Investment Company Act, and all references to rules under the Investment Company Act, including rule 2a–7, will be to Title 17, Part 270 of the Code of Federal Regulations [17 CFR 270].

9. Alternative Redemption Restrictions
C. Potential Combination of Standby Liquidity Fees and Gates and Floating Net Asset Value
1. Potential Benefits of a Combination
2. Potential Drawbacks of a Combination
3. Effect of Combination
4. Operational Issues
D. Certain Alternatives Considered
1. Alternatives in the FSOC Proposed Recommendations
2. Alternatives in the PWG Report
E. Macroeconomic Effects of the Proposals
1. Effect on Current Investment in Money Market Funds
2. Effect on Current Issuers and the Short-Term Financing Markets
F. Amendments to Disclosure Requirements
1. Financial Support Provided to Money Market Funds
2. Daily Disclosure of Daily Liquid Assets and Weekly Liquid Assets
3. Daily Web Site Disclosure of Current NAV per Share
4. Disclosure of Portfolio Holdings
5. Daily Calculation of Current NAV per Share Under the Liquidity Fees and Gates Proposal
6. Money Market Fund Confirmation Statements
G. New Form N–CR
1. Proposed Disclosure Requirements Under Both Reform Alternatives
2. Additional Proposed Disclosure Requirements Under Liquidity Fees and Gates Alternative
3. Economic Analysis
H. Amendments to Form N–MFP Reporting Requirements
1. Amendments Related to Rule 2a–7 Reforms
2. New Reporting Requirements
3. Clarifying Amendments
4. Public Availability of Information
5. Request for Comment on Frequency of Filing
6. Operational Implications
I. Amendments to Form PF Reporting Requirements
1. Overview of Proposed Amendments to Form PF
2. Utility of New Information, Including Benefits, Costs, and Economic Implications
J. Diversification
1. Treatment of Certain Affiliates for Purposes of Rule 2a–7's Five Percent Issuer Diversification Requirement
2. Asset-Backed Securities
3. The Twenty-Five Percent Basket
4. Additional Diversification Alternatives Considered
K. Issuer Transparency
L. Stress Testing
1. Stress Testing Under the Floating NAV Alternative
2. Stress Testing Under the Liquidity Fees and Gates Alternative
3. Economic Analysis
4. Combined Approach
M. Clarifying Amendments
1. Definitions of Daily Liquid Assets and Weekly Liquid Assets
2. Definition of Demand Feature
3. Short-Term Floating Rate Securities
4. Second Tier Securities
N. Proposed Compliance Date
1. Compliance Period for Amendments Related to Floating NAV
2. Compliance Period for Amendments Related to Liquidity Fees and Gates
3. Compliance Period for Other Amendments to Money Market Fund Regulation
4. Request for Comment
O. Request for Comment and Data
IV. Paperwork Reduction Act Analysis
A. Alternative 1: Floating Net Asset Value
1. Rule 2a–7
2. Rule 22e–3
3. Rule 30b1–7 and Form N–MFP
4. Rule 30b1–8 and Form N–CR
5. Rule 34b–1(a)
6. Rule 482
7. Form N–1A
8. Advisers Act Rule 204(b)–1 and Form PF
B. Alternative 2: Standby Liquidity Fees and Gates
1. Rule 2a–7
2. Rule 22e–3
3. Rule 30b1–7 and Form N–MFP
4. Rule 30b1–8 and Form N–CR
5. Rule 34b–1(a)
6. Rule 482
7. Form N–1A
8. Advisers Act Rule 204(b)–1 and Form PF
C. Request for Comments
V. Regulatory Flexibility Act Certification
VI. Statutory Authority
Text of Proposed Rules and Forms

## I. Introduction

Money market funds are a type of mutual fund registered under the Investment Company Act and regulated under rule 2a–7 under the Act.[2] Money market funds pay dividends that reflect prevailing short-term interest rates, generally are redeemable on demand, and, unlike other investment companies, seek to maintain a stable net asset value per share (''NAV''), typically $1.00.[3] This combination of principal stability, liquidity, and payment of short-term yields has made money market funds popular cash management vehicles for both retail and institutional investors. As of February 28, 2013, there were approximately 586 money market funds registered with the Commission, and these funds collectively held over $2.9 trillion of assets.[4]

Money market funds seek to maintain a stable share price by limiting their investments to short-term, high-quality debt securities that fluctuate very little in value under normal market conditions.[5] They also rely on exemptions provided in rule 2a–7 that permit them to value their portfolio securities using the ''amortized cost'' method of valuation and to use the ''penny-rounding'' method of pricing.[6] Under the amortized cost method, a money market fund's portfolio securities generally are valued at cost plus any amortization of premium or accumulation of discount, rather than at their value based on current market factors.[7] The penny rounding method of pricing permits a money market fund when pricing its shares to round the fund's net asset value to the nearest one percent (*i.e.,* the nearest penny).[8] Together, these valuation and pricing techniques create a ''rounding convention'' that permits a money market fund to sell and redeem shares at a stable share price without regard to small variations in the value of the securities that comprise its portfolio.[9]

[2] Money market funds are also sometimes called ''money market mutual funds'' or ''money funds.''

[3] *See generally* Valuation of Debt Instruments and Computation of Current Price Per Share by Certain Open-End Investment Companies (Money Market Funds), Investment Company Act Release No. 13380 (July 11, 1983) [48 FR 32555 (July 18, 1983)] (''1983 Adopting Release''). Most money market funds seek to maintain a stable net asset value per share of $1.00, but a few seek to maintain a stable net asset value per share of a different amount, *e.g.,* $10.00. For convenience, throughout this Release, the discussion will simply refer to the stable net asset value of $1.00 per share.

[4] Based on Form N–MFP data. SEC regulations require that money market funds report certain portfolio information on a monthly basis to the SEC on Form N–MFP. *See* rule 30b1–7.

[5] Throughout this Release, we generally use the term ''stable share price'' to refer to the stable share price that money market funds seek to maintain and compute for purposes of distribution, redemption and repurchases of fund shares.

[6] Money market funds use a combination of the two methods so that, under normal circumstances, they can use the penny rounding method to maintain a price of $1.00 per share without pricing to the third decimal point like other mutual funds, and the amortized cost method so that they need not strike a daily market-based NAV. *See infra* text accompanying nn.163, 177.

[7] *See* rule 2a–7(a)(2). *See also infra* note 10.

[8] *See* rule 2a–7(a)(20).

[9] When the Commission initially established its regulatory framework allowing money market funds to maintain a stable share price through use of the amortized cost method of valuation and/or the penny rounding method of pricing (so long as they abided by certain risk limiting conditions), it did so understanding the benefits that stable value money market funds provided as a cash management vehicle, particularly for smaller investors, and focusing on minimizing inappropriate dilution of assets and returns for shareholders. *See* Proceedings before the Securities and Exchange Commission in the Matter of InterCapital Liquid Asset Fund, Inc. et al., 3–5431, Dec. 28, 1978, at 1533 (Statement of Martin Lybecker, Division of Investment Management at the Securities and Exchange Commission) (stating that Commission staff had learned over the course of the hearings the strong preference of money market fund investors to have a stable share price and that with the right risk limiting conditions the Commission could limit the likelihood of a deviation from that stable value, addressing Commission concerns about dilution); 1983 Adopting Release, *supra* note 3, at nn.42–43 and accompanying text (''[T]he provisions of the rule impose obligations on the board of directors to assess the fairness of the valuation or pricing method and take appropriate steps to ensure that shareholders always receive their proportionate interest in the money market fund.''). At that time, the Commission was persuaded that deviations to an extent that would cause material dilution

Continued

Other types of mutual funds not regulated by rule 2a–7, must calculate their daily NAVs using market-based factors (with some exceptions) and do not use penny rounding.[10] We note, however, that banks and other companies also make wide use of amortized cost accounting to value certain of their assets.[11]

In exchange for the ability to rely on the exemptions provided by rule 2a–7, the rule imposes important conditions designed to limit deviations between the fund's $1.00 share price and the market value of the fund's portfolio. It requires money market funds to maintain a significant amount of liquid assets and to invest in securities that meet the rule's credit quality, maturity, and diversification requirements.[12] For example, a money market fund's portfolio securities must meet certain credit quality requirements, such as posing minimal credit risks.[13] The rule also places limits on the remaining maturity of securities in the fund's portfolio to limit the interest rate and credit spread risk to which a money market fund may be exposed. A money market fund generally may not acquire any security with a remaining maturity greater than 397 days, and the dollar-weighted average maturity of the securities owned by the fund may not exceed 60 days and the fund's dollar-weighted average life to maturity may not exceed 120 days.[14] Money market funds also must maintain sufficient liquidity to meet reasonably foreseeable redemptions, and generally must invest at least 10% of their portfolios in assets that can provide daily liquidity and invest at least 30% of their portfolios in assets that can provide weekly liquidity.[15] Finally, rule 2a–7 also requires money market funds to diversify their portfolios by generally limiting the funds to investing no more than 5% of their portfolios in any one issuer and no more than 10% of their portfolios in securities issued by, or subject to guarantees or demand features (*i.e.,* puts) from, any one institution.[16]

Rule 2a–7 also includes certain procedural requirements overseen by the fund's board of directors. These include the requirement that the fund periodically calculate the market-based value of the portfolio (''shadow price'')[17] and compare it to the fund's stable share price; if the deviation between these two values exceeds ½ of 1 percent (50 basis points), the fund's board of directors must consider what action, if any, should be initiated by the board, including whether to re-price the fund's securities above or below the fund's $1.00 share price (an event colloquially known as ''breaking the buck'').[18]

Different types of money market funds have been introduced to meet the differing needs of money market fund investors. Historically, most investors have invested in ''prime money market funds,'' which hold a variety of taxable short-term obligations issued by corporations and banks, as well as repurchase agreements and asset-backed commercial paper.[19] ''Government money market funds'' principally hold obligations of the U.S. government, including obligations of the U.S. Treasury and federal agencies and instrumentalities, as well as repurchase agreements collateralized by government securities. Some government money market funds limit themselves to holding only U.S. Treasury obligations or repurchase agreements collateralized by U.S. Treasury securities and are called ''Treasury money market funds.'' Compared to prime funds, government and Treasury money market funds generally offer greater safety of principal but historically have paid lower yields. ''Tax-exempt money market funds'' primarily hold obligations of state and local governments and their instrumentalities, and pay interest that is generally exempt from federal income tax for individual taxpayers.

In the analysis that follows, we begin by reviewing the role of money market funds and the benefits they provide investors. We then review the economics of money market funds. This includes a discussion of several features of money market funds that, when combined, can create incentives for fund shareholders to redeem shares during periods of stress, as well as the potential impact that such redemptions can have on the fund and the markets that provide short-term financing.[20] We then discuss money market funds' experience during the 2007–2008 financial crisis against this backdrop. We next analyze our 2010 reforms and their impact on the heightened redemption activity during the 2011 Eurozone sovereign debt crisis and U.S. debt ceiling impasse.

Based on these analyses as well as other publicly available analytical works, some of which are contained in the report responding to certain questions posed by Commissioners Aguilar, Paredes and Gallagher (''RSFI Study'')[21] prepared by staff from the Division of Risk, Strategy, and Financial Innovation (''RSFI''), we propose two alternative frameworks for additional regulation of money market funds. Each alternative seeks to preserve the ability of money market funds to function as an effective and efficient cash management tool for investors, but also address

generally would not occur given the risk limiting conditions of the rule. *See id.,* at nn.41–42 and accompanying text (noting that testimony from the original money market fund exemptive order hearings alleged that the risk limiting conditions, short of extraordinarily adverse conditions in the market, should ensure that a properly managed money market fund should be able to maintain a stable price per share and that rule 2a–7 is based on that representation).

[10] For a mutual fund not regulated under rule 2a–7, the Investment Company Act and applicable rules generally require that it price its securities at the current net asset value per share by valuing portfolio instruments at market value or, if market quotations are not readily available, at fair value as determined in good faith by the fund's board of directors. *See* section 2(a)(41)(B) of the Act and rules 2a–4 and 22c–1. The Commission, however, has stated that it would not object if a mutual fund board of directors determines, in good faith, that the value of debt securities with remaining maturities of 60 days or less is their amortized cost, unless the particular circumstances warrant otherwise. *See* Valuation of Debt Instruments by Money Market Funds and Certain Other Open-End Investment Companies, Investment Company Act Release No. 9786 (May 31, 1977) [42 FR 28999 (June 7, 1977)] (''1977 Valuation Release''). In this regard, the Commission has stated that the ''fair value of securities with remaining maturities of 60 days or less may not always be accurately reflected through the use of amortized cost valuation, due to an impairment of the credit worthiness of an issuer, or other factors. In such situations, it would appear to be incumbent upon the directors of a fund to recognize such factors and take them into account in determining 'fair value.' '' *Id.*

[11] *See* FASB ASC paragraph 320–10–35–1c indicating investments in debt securities classified as held-to-maturity shall be measured subsequently at amortized cost in the statement of financial position. *See also* Vincent Ryan, *FASB Exposure Draft Alarms Bank CFOs* (June 2, 2010) *available at http://www.cfo.com/article.cfm/14502294.*

[12] *See* rule 2a–7(c)(2), (3), (4), and (5).

[13] *See* rule 2a–7(a)(12), (c)(3)(ii).

[14] Rule 2a–7(c)(2).

[15] *See* rule 2a–7(c)(5). The 10% daily liquid asset requirement does not apply to tax exempt funds.

[16] *See* rule 2a–7(c)(4).

[17] *See* rule 2a–7(c)(8)(ii)(A).

[18] *See* rule 2a–7(c)(8)(ii)(A) and (B). Regardless of the extent of the deviation, rule 2a–7 imposes on the board of a money market fund a duty to take appropriate action whenever the board believes the extent of any deviation may result in material dilution or other unfair results to investors or current shareholders. Rule 2a–7(c)(8)(ii)(C). In addition, the money market fund can use the amortized cost or penny-rounding methods only as long as the board of directors believes that they fairly reflect the market-based net asset value per share. *See* rule 2a–7(c)(1).

[19] *See* Investment Company Institute, 2013 Investment Company Fact Book, at 178, Table 37 (2013), *available at http://www.ici.org/pdf/2013_factbook.pdf.*

[20] Throughout this Release, we generally refer to ''short-term financing markets'' to describe the markets for short-term financing of corporations, banks, and governments.

[21] *See* Response to Questions Posed by Commissioners Aguilar, Paredes, and Gallagher, a report by staff of the Division of Risk, Strategy, and Financial Innovation (Nov. 30, 2012), *available at http://www.sec.gov/news/studies/2012/money-market-funds-memo-2012.pdf.*

certain features in money market funds that can make them susceptible to heavy redemptions, provide them with better tools to manage and mitigate potential contagion from high levels of redemptions, and increase the transparency of their risks. We are also proposing amendments that would apply under each alternative that would result in additional changes to money market fund disclosure, diversification limits, and stress testing, among other reforms.[22]

## II. Background

### *A. Role of Money Market Funds*

The combination of principal stability, liquidity, and short-term yields offered by money market funds, which is unlike that offered by other types of mutual funds, has made money market funds popular cash management vehicles for both retail and institutional investors, as discussed above. Retail investors use money market funds for a variety of reasons, including, for example, to hold cash for short or long periods of time or to take a temporary ''defensive position'' in anticipation of declining equity markets. Institutional investors commonly use money market funds for cash management in part because, as discussed later in this Release, money market funds provide efficient diversified cash management due both to the scale of their operations and their expertise.[23]

Money market funds, due to their popularity with investors, have become an important source of financing in certain segments of the short-term financing markets, as discussed in more detail in section III.E.2 below. Money market funds' ability to maintain a stable share price contributes to their popularity. Indeed, the $1.00 stable share price has been one of the fundamental features of money market funds. As discussed in more detail in section III.A.7 below, the funds' stable share price facilitates the funds' role as a cash management vehicle, provides tax and administrative convenience to both money market funds and their shareholders, and enhances money market funds' attractiveness as an investment option.

Rule 2a–7, in addition to facilitating money market funds' maintenance of stable share prices, also benefits investors by making available an investment option that provides an efficient and diversified means for investors to participate in the short-term financing markets through a portfolio of short-term, high quality debt securities.[24] Many investors likely would find it impractical or inefficient to invest directly in the short-term financing markets, and some investors likely would not want the relatively undiversified exposure that can result from investing in those markets on a smaller scale or that could be associated with certain alternatives to money market funds, like bank deposits.[25] Although other types of mutual funds can and do invest in the short-term financing markets, investors may prefer money market funds because the risk the funds may undertake is limited under rule 2a–7 (and because of the funds' corresponding ability to maintain a stable share price).[26]

Therefore, although rule 2a–7 permits money market funds to use techniques to value and price their shares not permitted to other mutual funds (or not permitted to the same extent), the rule also imposes additional protective conditions on money market funds. These additional conditions are designed to make money market funds' use of the pricing techniques permitted by rule 2a–7 consistent with the protection of investors, and more generally, to make available an investment option for investors that seek an efficient way to obtain short-term yields. These conditions thus reflect the differences in the way money market funds operate and the ways in which investors use money market funds compared to other types of mutual funds.

We recognize, and considered when developing the reform proposals we are putting forward today, that money market funds are a popular investment product and that they provide many benefits to investors and to the short-term financing markets. Indeed, it is for these reasons that we are proposing reforms designed to make the funds more resilient, as discussed throughout this Release, while preserving, to the extent possible, the benefits of money market funds. These reform proposals may, however, make money market funds less attractive to certain investors as discussed more fully below.

### *B. Economics of Money Market Funds*

The combination of several features of money market funds can create an incentive for their shareholders to redeem shares heavily in periods of financial stress, as discussed in greater detail in the RSFI Study. We discuss these factors below, as well as the harm that can result from heavy redemptions in money market funds.

#### 1. Incentives Created by Money Market Funds' Valuation and Pricing Methods

Money market funds are unique among mutual funds in that rule 2a–7 permits them to use the amortized cost method of valuation and the penny-rounding method of pricing. As discussed above, these valuation and pricing techniques allow a money market fund to sell and redeem shares at a stable share price without regard to small variations in the value of the securities that comprise its portfolio, and thus to maintain a stable $1.00 share price under most conditions.

Although the stable $1.00 share price calculated using these methods provides a close approximation to market value under normal market conditions, differences may exist because market prices adjust to changes in interest rates, credit risk, and liquidity. We note that the vast majority of money market fund portfolio securities are not valued based on market prices obtained through secondary market trading because the secondary markets for most portfolio securities such as commercial paper, repos, and certificates of deposit are not actively traded. Accordingly, most money market fund portfolio securities are valued largely through ''mark-to-model'' or ''matrix pricing'' estimates.[27]

[22] We note that we have consulted and coordinated with the Consumer Financial Protection Bureau regarding this proposed rulemaking in accordance with section 1027(i)(2) of the Dodd-Frank Wall Street Reform and Consumer Protection Act.

[23] *See infra* notes 72–73 and accompanying text.

[24] *See, e.g.,* Comment Letter of Harvard Business School Professors Samuel Hanson, David Scharfstein, & Adi Sunderam (Jan. 8, 2013) (available in File No. FSOC–2012–0003) (''Harvard Business School FSOC Comment Letter'') (explaining that prime money market funds, by providing a way for investors to invest in the short-term financing markets indirectly, ''provides MMF investors with a diversified pool of deposit-like instruments with the convenience of a single deposit-like account,'' and that, ''[g]iven the fixed costs of managing a portfolio of such instruments, MMFs provide scale efficiencies for small-balance savers (*e.g.,* households and small and mid-sized nonfinancial corporations) along with a valuable set of transactional services (*e.g.,* check-writing and other cash-management functions).'').

[25] *Id. See also, e.g.,* Comment Letter of Investment Company Institute (Jan. 24, 2013) (available in File No. FSOC–2012–0003) (''ICI Jan. 24 FSOC Comment Letter'') (explaining that although bank deposits are an alternative to money market funds, ''corporate cash managers and other institutional investors do not view an undiversified holding in an uninsured (or underinsured) bank account as having the same risk profile as an investment in a diversified short-term money market fund subject to the risk-limiting conditions of Rule 2a–7'').

[26] *See, e.g.,* ICI Jan. 24 FSOC Comment Letter, supra note 25 (''The regulatory regime established by Rule 2a–7 has proven to be effective in protecting investors' interests and maintaining their confidence in money market funds.'').

[27] *See, e.g.,* Harvard Business School FSOC Comment Letter, *supra* note 24 (''secondary markets for commercial paper and other private money market assets such as CDs are highly illiquid.

Continued

The market value of a money market fund's portfolio securities also may experience relatively large changes if a portfolio asset defaults or its credit profile deteriorates.[28] Today differences within the tolerance defined by rule 2a–7 are reflected only in a fund's shadow price, and not the share price at which the fund satisfies purchase and redemption transactions.

Deviations that arise from changes in interest rates and credit risk are temporary as long as securities are held to maturity, because amortized cost values and market-based values converge at maturity. If, however, a portfolio asset defaults or an asset sale results in a realized capital gain or loss, deviations between the stable $1.00 share price and the shadow price become permanent. For example, if a portfolio experiences a 25 basis point loss because an issuer defaults, the fund's shadow price falls from $1.0000 to $0.9975. Even though the fund has not broken the buck, this reduction is permanent and can only be rebuilt internally in the event that the fund realizes a capital gain elsewhere in the portfolio, which generally is unlikely given the types of securities in which money market funds typically invest.[29]

If a fund's shadow price deviates far enough from its stable $1.00 share price, investors may have an economic incentive to redeem money market fund shares.[30] For example, investors may have an incentive to redeem shares when a fund's shadow price is less than $1.00.[31] If investors redeem shares when the shadow price is less than $1.00, the fund's shadow price will decline even further because portfolio losses are spread across a smaller asset base. If enough shares are redeemed, a fund can ''break the buck'' due, in part, to heavy investor redemptions and the concentration of losses across a shrinking asset base. In times of stress, this reason alone provides an incentive for investors to redeem shares ahead of other investors: early redeemers get $1.00 per share, whereas later redeemers may get less than $1.00 per share even if the fund experiences no further losses.

To illustrate the incentive for investors to redeem shares early, consider a money market fund that has one million shares outstanding and holds a portfolio worth exactly $1 million. Assume the fund's stable share price and shadow price are both $1.00. If the fund recognizes a $4,000 loss, the fund's shadow price will fall below $1.00 as follows:

$$\frac{\$996{,}000}{1{,}000{,}000\ \text{shares}} = \$0.996\,/\,\text{share}$$

If investors redeem one quarter of the fund's shares (250,000 shares), the redeeming shareholders are paid $1.00. Because redeeming shareholders are paid more than the shadow price of the fund, the redemptions further concentrate the loss among the remaining shareholders. In this case, the amount of redemptions is sufficient to cause the fund to ''break the buck.''

$$\frac{\$996{,}000 - \$250{,}000}{1{,}000{,}000\ \text{shares} - 250{,}000\ \text{shares}} = \frac{\$746{,}000}{750{,}000\ \text{shares}} = \$0.9947\,/\,\text{share}$$

This example shows that if a fund's shadow price falls below $1.00 and the fund experiences redemptions, the remaining investors have an incentive to redeem shares to potentially avoid holding shares worth even less, particularly if the fund re-prices its shares below $1.00. This incentive exists even if investors do not expect the fund to incur further portfolio losses.

As discussed in greater detail in the RSFI Study and as we saw during the 2007–2008 financial crisis as further discussed below, money market funds, although generally able to maintain stable share prices, remain subject to credit, interest rate, and liquidity risks, all of which can cause a fund's shadow price to decline below $1.00 and create an incentive for investors to redeem shares ahead of other investors.[32] Although defaults are very low probability events, the resulting losses will be most acute if the default occurs in a position that is greater than 0.5% of the fund's assets, as was the case in the Reserve Primary Fund's investment in Lehman Brothers commercial paper in September 2008.[33] As discussed further in section III.J of this Release, we note that money market funds hold significant numbers of such larger positions.[34]

2. Incentives Created by Money Market Funds' Liquidity Needs

The incentive for money market fund investors to redeem shares ahead of other investors also can be heightened

Therefore, the asset prices used to calculate the floating NAV would largely be accounting or model-based estimates, rather than prices based on secondary market transactions with sizable volumes.''); Institutional Money Market Funds Association, *The Use of Amortised Cost Accounting by Money Market Funds, available at http://www.immfa.org/assets/files/IMMFA%20The%20use%20of%20amortised%20cost%20accounting%20by%20MMF.pdf* (noting that ''investors typically hold money market instruments to maturity, and so there are relatively few prices from the secondary market or broker quotes,'' that as a result most money market funds value their assets using yield curve pricing, discounted cash flow pricing, and amortized cost valuation, and surveying several money market funds and finding that only U.S. Treasury bills are considered ''level one'' assets under the relevant accounting standards for which traded or quoted prices are generally available).

[28] The credit quality standards in rule 2a–7 are designed to minimize the likelihood of such a default or credit deterioration.

[29] It is important to understand that, in practice, a money market fund cannot use future portfolio earnings to rebuild its shadow price because Subchapter M of the Internal Revenue Code effectively forces money market funds to distribute virtually all of their earnings to investors. These restrictions can cause permanent reductions in shadow prices to persist over time, even if a fund's other portfolio securities are otherwise unimpaired.

[30] The value of this economic incentive is determined in part by the volatility of the fund's underlying assets, which is, in turn, affected by the volatility of interest rates, the likelihood of default, and the maturities of the underlying assets. Since the risk limiting conditions imposed by rule 2a–7 require funds to hold high quality assets with short maturities, the volatility of the underlying assets is very low (which implies that the corresponding value of this economic incentive is low), except when the fund is under stress.

[31] We recognize that, absent the fund breaking the buck, arbitraging fluctuations in a money market fund's shadow price would require some effort and may not be compelling in many cases given the small dollar value that could be captured. *See, e.g.,* Money Market Fund Reform, Investment Company Act Release No. 28807 (June 30, 2009) [74 FR 32688 (July 8, 2009)] (''2009 Proposing Release''), at nn.304–305 and accompanying text (discussing how to arbitrage around price changes from rising interest rates, investors would need to sell money market fund shares for $1.00 and reinvest the proceeds in equivalent short-term debt securities at then-current interest rates).

[32] *See generally* RSFI Study, *supra* note 21, at section 4.A.

[33] *See generally infra* section II.C.

[34] FSOC, in formulating possible money market reform recommendations, solicited and received comments from the public (FSOC Comment File, File No. FSOC–2012–0003, *available at http://www.regulations.gov/#!docketDetail;D=FSOC-2012-0003*), some of which have made similar observations about the concentration and size of money market fund holdings. *See, e.g.,* Harvard Business School FSOC Comment Letter, *supra* note 24 (noting that ''prime MMFs mainly invest in money-market instruments issued by large, global banks'' and providing information about the size of the holdings of ''the 50 largest non-government issuers of money market instruments held by prime MMFs as of May 2012'').

by liquidity concerns. Money market funds, by definition and like all other mutual funds, offer investors the ability to redeem shares upon demand.

A money market fund has three sources of internal liquidity to meet redemption requests: cash on hand, cash from investors purchasing shares, and cash from maturing securities. If these internal sources of liquidity are insufficient to satisfy redemption requests on any particular day, money market funds may be forced to sell portfolio securities to raise additional cash.[35] Since the secondary market for many portfolio securities is not deeply liquid (in part because most money market fund securities are held to maturity), funds may have to sell securities at a discount from their amortized cost value, or even at fire-sale prices,[36] thereby incurring additional losses that may have been avoided if the funds had sufficient liquidity.[37] This, itself, can cause a fund's portfolio to lose value. In addition, redemptions that deplete a fund's most liquid assets can have incremental adverse effects because they leave the fund with fewer liquid assets, making it more difficult to avoid selling less liquid assets, potentially at a discount, to meet further redemption requests.

3. Incentives Created by Imperfect Transparency, Including Sponsor Support

Lack of investor understanding and complete transparency concerning the risks posed by particular money market funds can exacerbate the concerns discussed above. If investors do not know a fund's shadow price and/or its underlying portfolio holdings (or if previous disclosures of this information are no longer accurate), investors may not be able to fully understand the degree of risk in the underlying portfolio.[38] In such an environment, a default of a large-scale commercial paper issuer, such as a bank holding company, could accelerate redemption activity across many funds because investors may not know which funds (if any) hold defaulted securities and initiate redemptions to avoid potential rather than actual losses in a ''flight to transparency.'' [39] Since many money market funds hold securities from the same issuer, investors may respond to a lack of transparency about specific fund holdings by redeeming assets from funds that are believed to be holding highly correlated positions.[40]

Money market funds' sponsors on a number of occasions have voluntarily chosen to provide financial support for their money market funds [41] for various reasons, including to keep a fund from re-pricing below its stable value, but also, for example, to protect the sponsors' reputations or brands. Considering that instances of sponsor support are not required to be disclosed outside of financial statements, and thus were not particularly transparent to investors, voluntary sponsor support has played a role in helping some money market funds maintain a stable value and, in turn, may have lessened investors' perception of the risk in money market funds.[42] Even those investors who were aware of sponsor support could not be assured it would be available in the future.[43] Instances of discretionary sponsor support were relatively common during the financial crisis. For example, during the period from September 16, 2008 to October 1, 2008, a number of money market fund sponsors purchased large amounts of portfolio securities from their money market funds or provided capital support to the funds (or received staff no-action assurances in order to provide

[35] Although the Act permits a money market fund to borrow money from a bank, such loans, assuming the proceeds of which are paid out to meet redemptions, create liabilities that must be reflected in the fund's shadow price, and thus will contribute to the stresses that may force the fund to ''break the buck.'' *See* section 18(f) of the Investment Company Act.

[36] Money market funds normally meet redemptions by disposing of their more liquid assets, rather than selling a pro rata slice of all their holdings, which typically include less liquid securities such as certificates of deposit, commercial paper, or term repurchase agreements (''repo''). *See* Harvard Business School FSOC Comment Letter, *supra* note 24 (''MMFs forced to liquidate commercial paper and bank certificates of deposits are likely to sell them at heavily discounted, 'fire sale' prices. This creates run risk because early investor redemptions can be met with the sale of liquid Treasury bills, which generate enough cash to fully pay early redeemers. In contrast, late redemptions force the sale of illiquid assets at discounted prices, which may not generate enough revenue to fully repay late redeemers. Thus, each investor benefits from redeeming earlier than others, setting the stage for runs.''); Jonathan Witmer, *Does the Buck Stop Here? A Comparison of Withdrawals from Money Market Mutual Funds with Floating and Constant Share Prices,* Bank of Canada Working Paper 2012–25 (Aug. 2012) (''Witmer''), *available at http://www.bankofcanada.ca/wp-content/uploads/2012/08/wp2012-25.pdf.* ''Fire sales'' refer to situations when securities deviate from their information-efficient values typically as a result of sale price pressure. For an overview of the theoretical and empirical research on asset ''fire sales,'' *see* Andrei Shleifer & Robert Vishny, *Fire Sales in Finance and Macroeconomics,* 25 Journal of Economic Perspectives, Winter 2011, at 29–48 (''*Fire Sales*'').

[37] The RSFI Study examined whether money market funds are more resilient to redemptions following the 2010 reforms and notes that, ''As expected, the results show that funds with a 30 percent [weekly liquid asset requirement] are more resilient to both portfolio losses and investor redemptions'' than those funds without a 30 percent weekly liquid asset requirement. RSFI Study, *supra* note 21, at 37.

[38] *See, e.g.,* RSFI Study, *supra* note 21, at 31 (stating that although disclosures on Form N–MFP have improved fund transparency, ''it must be remembered that funds file the form on a monthly basis with no interim updates,'' and that ''[t]he Commission also makes the information public with a 60-day lag, which may cause it to be stale''); Comment Letter of the Presidents of the 12 Federal Reserve Banks (Feb. 12, 2013) (available in File No. FSOC–2012–0003) (''Federal Reserve Bank Presidents FSOC Comment Letter'') (stating that ''[e]ven more frequent and timely disclosure may be warranted to increase the transparency of MMFs'' and noting that ''[d]uring times of stress, [. . .] uncertainty regarding portfolio composition could heighten investors' incentives to redeem in between reporting periods [of money market funds' portfolio information], as they will not be able to determine if their fund is exposed to certain stressed assets''); *see also infra* section III.H where we request comment on whether we should require money market funds to file Form N–MFP more frequently.

[39] *See* Nicola Gennaioli, Andrei Shleifer & Robert Vishny, *Neglected Risks, Financial Innovation, and Financial Fragility,* 104 J. Fin. Econ. 453 (2012) (''A small piece of news that brings to investors' minds the previously unattended risks catches them by surprise and causes them to drastically revise their valuations of new securities and to sell them. . . . When investors realize that the new securities are false substitutes for the traditional ones, they fly to safety, dumping these securities on the market and buying the truly safe ones.'').

[40] *See infra* notes 65–67 and accompanying text. Based on Form N–MFP data as of February 28, 2013, there were 27 different issuers whose securities were held by more than 100 prime money market funds.

[41] Rule 17a–9 currently allows for discretionary support of money market funds by their sponsors and other affiliates.

[42] *See, e.g.,* Comment Letter of Occupy the SEC (Feb. 15, 2013) (available in File No. FSOC–2012–0003) (''Occupy the SEC FSOC Comment Letter'') (''The current strategies for maintaining a stable NAV—rounding and discretionary fund sponsor support—both serve to conceal important market signals of mounting problems within the fund's portfolio.''). *See also* Federal Reserve Bank Presidents FSOC Comment Letter, *supra* note 38 (warning that ''[g]iven the perception of stability that discretionary support creates, this practice may attract investors that are not willing to accept the underlying risks in MMFs and who therefore are more prone to run in times of potential stress.'')

[43] *See, e.g.,* U.S. Securities and Exchange Commission, *Roundtable on Money Market Funds and Systemic Risk,* unofficial transcript (May 10, 2011), *available at http://www.sec.gov/spotlight/mmf-risk/mmf-risk-transcript-051011.htm* (''Roundtable Transcript'') (Bill Stouten, Thrivent Financial) (''I think the primary factor that makes money funds vulnerable to runs is the marketing of the stable NAV. And I think the record of money market funds and maintaining the stable NAV has largely been the result of periodic voluntary sponsor support. I think sophisticated investors that understand this and doubt the willingness or ability of the sponsor to make that support know that they need to pull their money out before a declining asset is sold.''); (Lance Pan, Capital Advisors Group) (''over the last 30 or 40 years, [investors] have relied on the perception that even though there is risk in money market funds, that risk is owned somehow implicitly by the fund sponsors. So once they perceive that they are not able to get that additional assurance, I believe that was one probable cause of the run''); *see also* Federal Reserve Bank Presidents FSOC Comment Letter, *supra* note 38 (stating that ''[t]hough [sponsor support] creates a perception of stability, it may not truly provide stability in times of stress. Indeed, events of 2008 showed that sponsor support cannot always be relied upon.''); *infra* section III.F.1.

support).[44] Commission staff provided no-action assurances to 100 money market funds in 18 different fund groups so that the fund groups could enter into such arrangements.[45] Although a number of advisers to money market funds obtained staff no-action assurances in order to provide sponsor support, several did not subsequently provide the support because it was no longer necessary.[46]

The 2007–2008 financial crisis is not the only instance in which some money market funds have come under strain, although it is unique in the amount of money market funds that requested or received sponsor support.[47] Interest rate changes, issuer defaults, and credit rating downgrades can lead to significant valuation losses for individual funds. Table 1 documents that since 1989, in addition to the 2007–2008 financial crisis, 11 events were deemed to have been sufficiently negative that some fund sponsors chose to provide support or to seek staff no-action assurances in order to provide support.[48] The table indicates that these events potentially affected 158 different money market funds. This finding is consistent with estimates provided by Moody's that at least 145 U.S. money market funds received sponsor support to maintain either price stability or share liquidity before 2007.[49] Note that although these events affected money market funds and their sponsors, there is no evidence that these events caused systemic problems, most likely because the events were isolated either to a single entity or class of security. Table 1 is consistent with the interpretation that outside a crisis period, these events did not propagate risk more broadly to the rest of the money market fund industry. However, a caveat that prevents making a strong inference about the impact of sponsor support on investor behavior from Table 1 is that sponsor support generally was not immediately disclosed, and was not required to be disclosed by the Commission, and so investors may have been unaware that their money market fund had come under stress.[50]

TABLE 1

| Year | Number of money market funds from 2013 ICI mutual fund fact book[51] | Estimated number of money market funds supported by affiliate or for which no-action assurances obtained | Event |
|---|---|---|---|
| 1989 ..... | 673 | 4 | Default of Integrated Resources commercial paper (rated A–2 by Standard & Poor's until shortly prior to default).[52] |
| 1990 ..... | 741 | 11 | Default of Mortgage & Realty Trust commercial paper (rated A–2 by Standard & Poor's until shortly prior to default).[53] |
| 1990 ..... | 741 | 10 | MNC Financial Corp. commercial paper downgraded from being a second tier security.[54] |
| 1991 ..... | 820 | 10 | Mutual Benefit Life Insurance (''MBLI'') seized by state insurance regulators, causing it to fail to honor put obligations after those holding securities with these features put the obligations en masse to MBLI.[55] |
| 1994 ..... | 963 | 40 | Rising interest rates damaged the value of certain adjustable rate securities held by money market funds.[56] |
| 1994 ..... | 963 | 43 | Orange County, California bankruptcy.[57] |
| 1997 ..... | 1,103 | 3 | Mercury Finance Corp. defaults on its commercial paper. |

[44] *See* Steffanie A. Brady et al., *The Stability of Prime Money Market Mutual Funds: Sponsor Support from 2007 to 2011,* Federal Reserve Bank of Boston Risk and Policy Analysis Unit Working Paper No. 12–3 (Aug. 13, 2012), *available at http://www.bos.frb.org/bankinfo/qau/wp/2012/qau1203.pdf.* Staff in the Federal Reserve Bank of Boston's Risk and Policy Analysis Unit examine 341 money market funds and find that 78 of the funds disclosed sponsor support on Form N–CSR between 2007 and 2011 (some multiple times). This analysis excludes Capital Support Agreements and/or Letters of Credit that were not drawn upon. Large sponsor support (in aggregate) representing over 0.5% of assets under management occurred in 31 money market funds, and the primary reasons disclosed for such support include losses on Lehman Brothers, AIG, and Morgan Stanley securities. Moody's Investors Service Special Comment, *Sponsor Support Key to Money Market Funds* (Aug. 9, 2010) (''Moody's Sponsor Support Report''), reported that 62 money market funds required sponsor support during 2007–2008.

[45] Our staff estimated that during the period from August 2007 to December 31, 2008, almost 20% of all money market funds received some support (or staff no-action assurances concerning support) from their money managers or their affiliates. We note that not all of such support required no-action assurances from Commission staff (for example, fund affiliates were able to purchase defaulted Lehman Brothers securities from fund portfolios under rule 17a–9 under the Investment Company Act without the need for any no-action assurances). *See, e.g., http://www.sec.gov/divisions/investment/im-noaction.shtml#money.*

[46] *See, e.g.,* Comment Letter of The Dreyfus Corporation (Aug. 7, 2012) (available in File No. 4–619) (stating that no-action relief to provide sponsor support ''was sought by many money funds as a precautionary measure'').

[47] *See* Moody's Sponsor Support Report, *supra* note 44.

[48] The table does not comprehensively describe every instance of sponsor support of a money market fund or request for no-action assurances to provide support, but rather summarizes some of the more notable instances of sponsor support.

[49] *See* Moody's Sponsor Support Report, *supra* note 44, noting in particular 13 funds requiring support in 1990 due to credit defaults or deterioration at MNC Financial, Mortgage & Realty Trust, and Drexel Burnham; 79 funds requiring support in 1994 due to the Orange County bankruptcy and holdings of certain floating rate securities when interest rates increased; and 25 funds requiring support in 1999 after the credit of certain General American Life Insurance securities deteriorated.

[50] Note that we are proposing changes to our rules and forms to require more comprehensive and timely disclosure of such sponsor support. *See infra* sections III.F.1 and III.G.

[51] The estimated total numbers of money market funds are from Table 38 of the Investment Company Institute's 2013 Fact Book, *available at http://www.ici.org/pdf/2013_factbook.pdf.* The numbers of money market funds are as of the end of the relevant year, and not necessarily as of the date that any particular money market fund received support (or whose sponsor received no-action assurances in order to provide support).

[52] *See* Jack Lowenstein, *Should the Rating Agencies be Downgraded?,* Euromoney (Feb. 1, 1990) (noting that Integrated Resources had been rated A–2 by Standard & Poor's until two days before default); Jonathan R. Laing, *Never Say Never—Or, How Safe Is Your Money-Market Fund?,* Barron's (Mar. 26, 1990) (''Laing''), at 6; Randall W. Forsyth, *Portfolio Analysis of Selected Fixed-Income Funds—Muni Money-Fund Risks,* Barron's (July 2, 1990) (''Forsyth''), at 33; Georgette Jasen, *SEC Is Accelerating Its Inspections of Money Funds, Wall St. J.* (Dec. 4, 1990) (''Jasen''), at C1. One $630 million money market fund held a 3.5% position in Integrated Resources when it defaulted. *See* Linda Sandler, *Cloud Cast on 'Junk' IOUs By Integrated Resources,* Wall St. J. (June 28, 1989).

[53] *See* Laing, *supra* note 52; Forsyth, *supra* note 52; Jasen, *supra* note 52.

[54] *See* Revisions to Rules Regulating Money Market Funds, Investment Company Act Release No. 19959 (Dec. 17, 1993) [58 FR 68585 (Dec. 28, 1993)] at n.12 (''1993 Proposing Release''). *See also* Leslie Eaton, *Another Close Call—An Adviser Bails Out Its Money Fund,* Barron's (Mar. 11, 1991), at 42 (noting that Mercantile Bancorp bought out $28 million of MNC Financial notes from its affiliated money market fund, which had accounted for 3% of the money market fund's assets).

TABLE 1—Continued

| Year | Number of money market funds from 2013 ICI mutual fund fact book [51] | Estimated number of money market funds supported by affiliate or for which no-action assurances obtained | Event |
|---|---|---|---|
| 1999 ..... | 1,045 | 25 | Credit rating downgrade of General American Life Insurance Co. triggered a wave of demands for repayment on its funding contracts, leading to liquidity problems and causing it to be placed under administrative supervision by state insurance regulators.[58] |
| 2001 ..... | 1,015 | 6 | Pacific Gas & Electric Co. and Southern California Edison Co. commercial paper went from being first tier securities to defaulting in a 2-week period.[59] |
| 2007 ..... | 805 | 51 | Investments in SIVs. |
| 2008 ..... | 783 | 109 | Investments in Lehman Brothers, America International Group, Inc. (''AIG'') and other financial sector debt securities. |
| 2010 ..... | 652 | 3 | British Petroleum Gulf oil spill affects price of BP debt securities held by some money market funds. |
| 2011 ..... | 632 | 3 | Investments in Eksportfinans, which was downgraded from being a first tier security to junk-bond status. |

It also is important to note that, as discussed above, fund sponsors may provide financial support for a number of different reasons. Sponsors may support funds to protect their reputations and their brands or the credit rating of the fund.[60] Support also may be used to keep a fund from breaking a buck or to increase a fund's shadow price if its sponsor believes investors avoid funds that may have low shadow prices. We note that the fact that no-action assurances were obtained or sponsor support was provided does not necessarily mean that a money market fund would have broken the buck without such support or assurances.

Finally, the government assistance provided to money market funds during 2007–2008 financial crisis, discussed in more detail below, may have contributed to investors' perceptions that the risk of loss in money market funds is low.[61] If investors perceive money market funds as having an implicit government guarantee in times of crisis, any potential instability of a money market fund's NAV could be mis-estimated. Investors will form expectations about the likelihood of a potential intervention to support money market funds, either by the U.S. government or fund sponsors. To the extent these forecasts are based on inaccurate information, investor estimates of potential losses will be biased.

4. Incentives Created by Money Market Funds Investors' Desire To Avoid Loss

In addition to the incentives described above, other characteristics of money market funds create incentives to redeem in times of stress. Investors in money market funds have varying investment goals and tolerances for risk. Many investors use money market funds for principal preservation and as a cash management tool, and, consequently, these funds can attract investors who are unable or unwilling to tolerate even small losses. These investors may seek to minimize possible losses, even at the cost of forgoing higher returns.[62] Such

[55] At the time of its seizure, MBLI debt was rated in the highest short-term rating category by Standard & Poor's. *See* 1993 Proposing Release, *supra* note 54, at n.28 and accompanying text. The money market fund sponsors either repurchased the MBLI-backed instruments from the funds at their amortized cost or obtained a replacement guarantor in order to prevent shareholder losses. *Id.*

[56] *See* Money Market Fund Prospectuses, Investment Company Act Release No. 21216 (July 19, 1995) [60 FR 38454, (July 26, 1995)], at n.17; Investment Company Institute, Report of the Money Market Working Group (Mar. 17, 2009), *available at http://www.ici.org/pdf/ppr_09_mmwg.pdf* (''ICI 2009 Report''), at 177; Leslie Wayne, *Investors Lose Money in 'Safe' Fund,* N.Y. Times, Sept. 28, 1994; Leslie Eaton, *New Caution About Money Market Funds,* N.Y. Times, Sept. 29, 1994.

[57] *See* ICI 2009 Report, *supra* note 56, at 178; Tom Petruno, *Orange County in Bankruptcy: Investors Weigh Their Options: Muni Bond Values Slump but Few Trade at Fire-Sale Prices,* L.A. Times, Dec. 8, 1994.

[58] *See* Sandra Ward, *Money Good? How some fund managers sacrificed safety for yield,* Barron's (Aug. 23, 1999), at F3.

[59] *See* Aaron Lucchetti & Theo Francis, *Parents Take on Funds' Risks Tied to Utilities,* Wall St. J. (Feb. 28, 2001), at C1; Lewis Braham, *Commentary: Money Market Funds Enter the Danger Zone, Businessweek* (Apr. 8, 2001).

[60] *See, e.g.,* Marcin Kacperczyk & Philipp Schnabl, *How Safe are Money Market Funds?,* 128 Q. J. Econ. (forthcoming Aug. 2013) (''Kacperczyk & Schnabl'') (''. . . fund sponsors with more non-money market fund business expect to incur large costs if their money market funds fail. Such costs are typically reputational in nature, in that an individual fund's default generates negative spillovers to the fund's sponsor['s] other business. In practice, these costs could be outflows from other mutual funds managed by the same sponsor or a loss of business in the sponsor's commercial banking, investment banking, or insurance operations.''); Patrick E. McCabe, *The Cross Section of Money Market Fund Risks and Financial Crises,* Federal Reserve Board Finance and Economic Discussion Series Paper No. 2010–51 (2010) (''Cross Section'') (''Nothing required these sponsors to provide support, but because allowing a fund to break the buck would have been destructive to a sponsor's reputation and franchise, sponsors backstopped their funds voluntarily.''); *Value Line Posts Loss for 1st Period, Cites Charge of $7.5 Million, Wall St. J.* (Sept. 18, 1989) (''In discussing the charge in its fiscal 1989 annual report [for buying out defaulted commercial paper from its money market fund], Value Line said it purchased the fund's holdings in order to protect its reputation and the continuing income from its investment advisory and money management business.''); Comment Letter of James J. Angel (Feb. 6, 2013) (available in File No. FSOC–2012–0003) (''Angel FSOC Comment Letter'') (''Sponsors have a strong commercial incentive to stand behind their funds. Breaking the buck means the immediate and catastrophic end of the sponsor's entire asset management business.'').

[61] *See, e.g,* Marcin Kacperczyk & Philipp Schnabl, *Money Market Funds: How to Avoid Breaking the Buck, in* Regulating Wall St: The Dodd-Frank Act and the New Architecture of Global Finance (Viral V. Acharya, et al., eds., 2011), at 313 (''Given that money market funds provide both payment services to investors and refinancing to financial intermediaries, there is a strong case for the government to support money market funds during a financial crisis by guaranteeing the value of money market fund investments. As a result of such support, money market funds have an ex ante incentive to take on excessive risk, similarly to other financial institutions with explicit or implicit government guarantees . . . after the [government] guarantees were provided in September 2008 [to money market funds], most investors will expect similar guarantees during future financial crises. . . .''). *But see* Comment Letter of Fidelity (Apr. 26, 2012) (available in File No. 4–619) (''Fidelity April 2012 PWG Comment Letter'') (citing a survey of Fidelity's retail customers in which 75% of responding customers did not believe that money market funds are guaranteed by the government and 25% either believed that they were guaranteed or were not sure whether they were guaranteed). We note that investor belief that money market funds are not guaranteed by the government does not necessarily mean that investors do not believe that the government will support money market funds if there is another run on money market funds.

[62] *See, e.g.,* Comment Letter of Investment Company Institute (Apr. 19, 2012) (available in File

Continued

investors may be very loss averse for many reasons, including general risk tolerance, legal or investment restrictions, or short-term cash needs.[63] These overarching considerations may create incentives for money market investors to redeem and would be expected to persist, even if valuation and pricing incentives were addressed.

The desire to avoid loss may cause investors to redeem from money market funds in times of stress in a ''flight to quality.'' For example, as discussed in the RSFI Study, one explanation for the heavy redemptions from prime money market funds and purchases in government money market fund shares during the financial crisis may be a flight to quality, given that most of the assets held by government money market funds have a lower default risk than the assets of prime money market funds.[64]

5. Effects on Other Money Market Funds, Investors, and the Short-Term Financing Markets

The analysis above generally describes how potential losses may create shareholder incentives to redeem at a specific money market fund. We now discuss how stress at one money market fund can be positively correlated across funds in at least two ways. Some market observers have noted that if a money market fund suffers a loss on one of its portfolio securities—whether because of a deterioration in credit quality, for example, or because the fund sold the security at a discount to its amortized-cost value—other money market funds holding the same security may have to reflect the resultant discounts in their shadow prices.[65] Any resulting decline in the shadow prices of other funds could, in turn, lead to a contagion effect that could spread even further.[66] For example, a number of commenters have observed that many money market fund holdings tend to be highly correlated, making it more likely that multiple money market funds will experience contemporaneous decreases in share prices.[67]

As discussed above, in times of stress if investors do not wish to be exposed to a distressed issuer (or correlated issuers) but do not know which money market funds own these distressed securities at any given time, investors may redeem from any money market funds that could own the security (*e.g.,* redeeming from all prime funds).[68] A fund that did not own the security and was not otherwise under stress could nonetheless experience heavy redemptions which, as discussed above, could themselves ultimately cause the fund to experience losses if it does not have adequate liquidity.

As was experienced during the financial crisis, the potential for liquidity-induced contagion may have negative effects on investors and the markets for short-term financing of corporations, banks, and governments. This is in large part because of the significance of money market funds' role in such short-term financing markets.[69] Indeed, money market funds had experienced steady growth before the financial crisis, driven in part by growth in the size of institutional cash pools,[70] which grew from under $100 billion in 1990 to almost $4 trillion just before the 2008 financial crisis.[71] Money market funds' suitability for cash management operations also has made them popular among corporate treasurers, municipalities, and other institutional investors, some of whom rely on money market funds for their cash management operations because the funds provide diversified cash management more efficiently due both to the scale of their operations and their expertise.[72] For example, according to

No. 4–619) (''ICI Apr 2012 PWG Comment Letter'') (enclosing a survey commissioned by the Investment Company Institute and conducted by Treasury Strategies, Inc. finding, among other things. that 94% of respondents rated safety of principal as an ''extremely important'' factor in their money market fund investment decision and 64% ranked safety of principal as the ''primary driver'' of their money market fund investment).

[63] *See, e.g.,* Comment Letter of County Commissioners Assoc. of Ohio (Dec. 21, 2012) (available in File No. FSOC–2012–0003) (''County governments in Ohio operate under legal constraints or other policies that limit them from investing in instruments without a stable value.'').

[64] One study documented that investors redirected assets from prime money market funds into government money market funds during September 2008. *See* Russ Wermers et al., *Runs on Money Market Funds* (Jan. 2, 2013), *available at http://www.rhsmith.umd.edu/cfp/pdfs_docs/papers/WermersMoneyFundRuns.pdf* (''Wermers Study''). Another study found that redemption activity in money market funds during the financial crisis was higher for riskier money market funds. *See* Cross Section, *supra* note 60.

[65] *See generally* Douglas W. Diamond & Raghuram G. Rajan, *Fear of Fire Sales, Illiquidity Seeking, and Credit Freezes,* 126 Q. J. Econ. 557 (May 2011); *Fire Sales, supra* note 36; Markus Brunnermeier et al., *The Fundamental Principles of Financial Regulation, in* Geneva Reports on the World Economy 11 (2009).

[66] For example, *supra* Table 1, which identifies certain instances in which money market fund sponsors supported their funds or sought staff no-action assurances to do so, tends to show that correlated holdings across funds resulted in multiple funds experiencing losses that appeared to motivate sponsors to provide support or seek staff no-action assurances in order to provide support.

[67] *See, e.g.,* Comment Letter of Better Markets, Inc. (Feb. 15, 2013) (available in File No. FSOC–2012–0003) (''Better Markets FSOC Comment Letter'') (agreeing with FSOC's analysis and stating that ''MMFs tend to have similar exposures due to limits on the nature of permitted investments. As a result, losses creating instability and a crisis of confidence in one MMF are likely to affect other MMFs at the same time.''); Comment Letter of Robert Comment (Dec. 31. 2012) (available in File No. FSOC–2012–0003) (''Robert Comment FSOC Comment Letter'') (discussing correlation in money market funds' portfolios and stating, among other things, that ''now that bank-issued money market instruments have come to comprise half the holdings of the typical prime fund, the SEC should acknowledge correlated credit risk by requiring that prime funds practice sector diversification (in addition to issuer diversification)''); Occupy the SEC FSOC Comment Letter, *supra* note 42 (discussing concentration of risk across money market funds).

[68] *See, e.g.,* Wermers Study, *supra* note 64 (based on an empirical analysis of data from the 2008 run on money market funds, finding that, during 2008, ''[f]unds that cater to institutional investors, which are the most sophisticated and informed investors, were hardest hit,'' and that ''investor flows from money market funds seem to have been driven both by strategic externalities . . . and information.'').

[69] *See infra* Panels A, B, and C in section III.E for statistics on the types and percentages of outstanding short-term debt obligations held by money market funds.

[70] *See* Zoltan Pozsar, *Institutional Cash Pools and the Triffin Dilemma of the U.S. Banking System,* IMF Working Paper 11/190 (Aug. 2011) (''Pozsar''); Gary Gorton & Andrew Metrick, *Securitized Banking and the Run on Repo,* 104 J. Fin. Econ. 425 (2012) (''Gorton & Metrick''); Jeremy C. Stein, *Monetary Policy as Financial Stability Regulation,* 127 Q. J. Econ. 57 (2012); Nicola Gennaioli, Andrei Shleifer & Robert W. Vishny, *A Model of Shadow Banking, J. Fin.* (forthcoming 2013). The Pozsar paper defines institutional cash pools as ''large, centrally managed, short-term cash balances of global non-financial corporations and institutional investors such as asset managers, securities lenders and pension funds.'' Pozsar, at 4.

[71] *See* Pozsar, *supra* note 70, at 5–6. These institutional cash pools can come from corporations, bank trust departments, securities lending operations of brokerage firms, state and local governments, hedge funds, and other private funds. The rise in institutional cash pools increased demand for investments that were considered to have a relatively low risk of loss, including, in addition to money market funds, Treasury bonds, insured deposit accounts, repurchase agreements, and asset-backed commercial paper. *See* Ben S. Bernanke, Carol Bertaut, Laurie Pounder DeMarco & Steven Kamin, *International Capital Flows and the Returns to Safe Assets in the United States, 2003–2007,* Board of Governors of the Federal Reserve System International Finance Discussion Paper No. 1014 (Feb. 2011); Pozsar, *supra* note 70; Gorton & Metrick, *supra* note 70; Daniel M. Covitz, Nellie Liang & Gustavo A. Suarez, *The Evolution of a Financial Crisis: Collapse of the Asset-Backed Commercial Paper Market, J. Fin.* (forthcoming 2013) (''Covitz''). The incentive among these cash pools to search for alternate ''safe'' investments was only heightened by factors such as limits on deposit insurance coverage and historical bans on banks paying interest on institutional demand deposit accounts, which limited the utility of deposit accounts for large pools of cash. *See* Pozsar, *supra* note 70; Gary Gorton & Andrew Metrick, *Regulating the Shadow Banking System,* Brookings Papers on Economic Activity (Fall 2010), at 262–263 (''Gorton Shadow Banking'').

[72] *See, e.g.,* Roundtable Transcript, *supra* note 43 (Travis Barker, Institutional Money Market Funds Association) (''[money market funds are] there to provide institutional investors with greater diversification than they could otherwise achieve''); (Lance Pan, Capital Advisors Group) (noting diversification benefits of money market funds and investors' need for a substitute to bank products to mitigate counterparty risk); (Kathryn L. Hewitt,

one survey, approximately 19% of organizations' short-term investments were allocated to money market funds (and, according to this observer, this figure is down from almost 40% in 2008 due in part to the reallocation of cash investments to bank deposits following temporary unlimited Federal Deposit Insurance Corporation deposit insurance for non-interest bearing bank transaction accounts, which recently expired).[73]

Money market funds' size and significance in the short-term markets, together with their features that can create an incentive to redeem as discussed above, have led to concerns that money market funds may contribute to systemic risk. Heavy redemptions from money market funds during periods of financial stress can remove liquidity from the financial system, potentially disrupting the secondary market. Issuers may have difficulty obtaining capital in the short-term markets during these periods because money market funds are focused on meeting redemption requests through internal liquidity generated either from maturing securities or cash from subscriptions, and thus may be purchasing fewer short-term debt obligations.[74] To the extent that multiple money market funds experience heavy redemptions, the negative effects on the short-term markets can be magnified. Money market funds' experience during the 2007–2008 financial crisis illustrates the impact of heavy redemptions, as we discuss in more detail below.

Heavy redemptions in money market funds may disproportionately affect slow-moving shareholders because, as discussed further below, redemption data from the 2007–2008 financial crisis show that some institutional investors are likely to redeem from distressed money market funds more quickly than other investors and to redeem a greater percentage of their prime fund holdings.[75] Slower-to-redeem shareholders may be harmed because, as discussed above, redemptions at a money market fund can concentrate existing losses in the fund or create new losses if the fund must sell assets at a discount. In both cases, redemptions leave the fund's portfolio more likely to lose value, to the detriment of slower-to-redeem investors.[76] Retail investors—who tend to be slower moving—also could be harmed if market stress begins at an institutional money market fund and spreads to other funds, including funds composed solely or primarily of retail investors.[77]

### *C. The 2007–2008 Financial Crisis*

There are many possible explanations for the redemptions from money market funds during the 2007–2008 financial crisis.[78] Regardless of the cause (or causes), money market funds' experience in the 2007–2008 financial crisis demonstrates the harm that can result from such rapid heavy redemptions in money market funds.[79] As explained in the RSFI study, on September 16, 2008, the day after Lehman Brothers Holdings Inc. announced its bankruptcy, The Reserve Fund announced that as of that afternoon, its Primary Fund—which held a $785 million (or 1.2% of the fund's assets) position in Lehman Brothers commercial paper—would ''break the buck'' and price its securities at $0.97 per share.[80] At the same time, there was turbulence in the market for financial sector securities as a result of the bankruptcy of Lehman Brothers and the near failure of American International Group (''AIG''), whose commercial paper was held by many prime money market funds. In addition to Lehman Brothers and AIG, there were other stresses in the market as well, as discussed in greater detail in the RSFI Study.[81]

Redemptions in the Primary Fund were followed by redemptions from other Reserve money market funds.[82] Prime institutional money market funds more generally began experiencing heavy redemptions.[83] During the week of September 15, 2008, investors withdrew approximately $300 billion

Government Finance Officers Association) (''Most of us don't have the time, the energy, or the resources at our fingertips to analyze the credit quality of every security ourselves. So we're in essence, by going into a pooled fund, hiring that expertise for us . . . it gives us diversification, it gives us immediate cash management needs where we can move money into and out of it, and it satisfies much of our operating cash investment opportunities.''); (Brian Reid, Investment Company Institute) (''there's a very clear stated demand out there on the part of investors for a non-bank product that creates a pooled investment in short-term assets . . . banks can't satisfy this because an undiversified exposure to a single bank is considered to be far riskier. . . .''); (Carol A. DeNale, CVS Caremark) (''I think that it would be very small investment [in] deposits in banks. I don't think there's—you know, the ratings of some of the banks would make me nervous, also; [sic] they're not guaranteed. I'm not going to put a $20 million investment in some banks.'').

[73] *See* 2012 Association for Financial Professionals Liquidity Survey, at 15, *available at http://www.afponline.org/liquidity* (subscription required) (''2012 AFP Liquidity Survey''). The size of this allocation to money market funds is down substantially from prior years. For example, prior AFP Liquidity Surveys show higher allocations of organizations' short-term investments to money market funds: Almost 40% in the 2008 survey, approximately 25% in the 2009 and 2010 surveys, and almost 30% in the 2011 survey. This shift has largely reflected a re-allocation of cash investments to bank deposits, which rose from representing 25% of organizations' short-term investment allocations in the 2008 Association for Financial Professionals Liquidity Survey, *available at http://www.afponline.org/pub/pdf/2008_Liquidity_Survey.pdf* (''2008 AFP Liquidity Survey''), to 51% of organizations' short-term investment allocations in the 2012 survey. The 2012 survey notes that some of this shift has been driven by the temporary unlimited FDIC deposit insurance coverage for non-interest bearing bank transaction accounts (which expired at the end of 2012) and the above-market rate that these bank accounts are able to offer in the low interest rate environment through earnings credits. *See* 2012 AFP Liquidity Survey, this note. As of August 14, 2012, approximately 66% of money market fund assets were held in money market funds or share classes intended to be sold to institutional investors according to iMoneyNet data. All of the AFP Liquidity Surveys are available at *http://www.afponline.org*.

[74] *See supra* text preceding and accompanying n.35. Although money market funds also can build liquidity internally by retaining (rather than investing) cash from investors purchasing shares, this is not likely to be a material source of liquidity for a distressed money market fund experiencing heavy redemptions.

[75] This likely is because some institutional investors generally have more capital at stake, sophisticated tools, and professional staffs to monitor risk. *See* 2009 Proposing Release, *supra* note 31, at nn.46–48 and 178 and accompanying text.

[76] *See, e.g.,* RSFI Study, *supra* note 21, at 10 (''Investor redemptions during the 2008 financial crisis, particularly after Lehman's failure, were heaviest in institutional share classes of prime money market funds, which typically hold securities that are illiquid relative to government funds. It is possible that sophisticated investors took advantage of the opportunity to redeem shares to avoid losses, leaving less sophisticated investors (if co-mingled) to bear the losses.'').

[77] As discussed further below, retail money market funds experienced a lower level of redemptions in 2008 than institutional money market funds, although the full predictive power of this empirical evidence is tempered by the introduction of the Treasury Department's temporary guarantee program for money market funds, which may have prevented heavier shareholder redemptions among generally slower moving retail investors. *See infra* n.91.

[78] *See generally* RSFI Study, *supra* note 21, at section 3.

[79] *See generally* RSFI Study, *supra* note 21, at section 3. *See also* 2009 Proposing Release *supra* note 31, at section I.D; *infra* section II.D.2 (discussing the financial distress in 2011 caused by the Eurozone sovereign debt crisis and U.S. debt ceiling impasse and money market funds' experience during that time).

[80] *See also* 2009 Proposing Release, *supra* note 31, at n.44 and accompanying text. We note that the Reserve Primary Fund's assets have been returned to shareholders in several distributions made over a number of years. We understand that assets returned constitute approximately 99% of the fund's assets as of the close of business on September 15, 2008, including the income earned during the liquidation period. Any final distribution to former Reserve Primary Fund shareholders will not occur until the litigation surrounding the fund is complete. *See* Consolidated Class Action Complaint, *In Re* The Reserve Primary Fund Sec. & Derivative Class Action Litig., No. 08–CV–8060–PGG (S.D.N.Y. Jan. 5, 2010).

[81] *See generally* RSFI Study, *supra* note 21, at section 3.

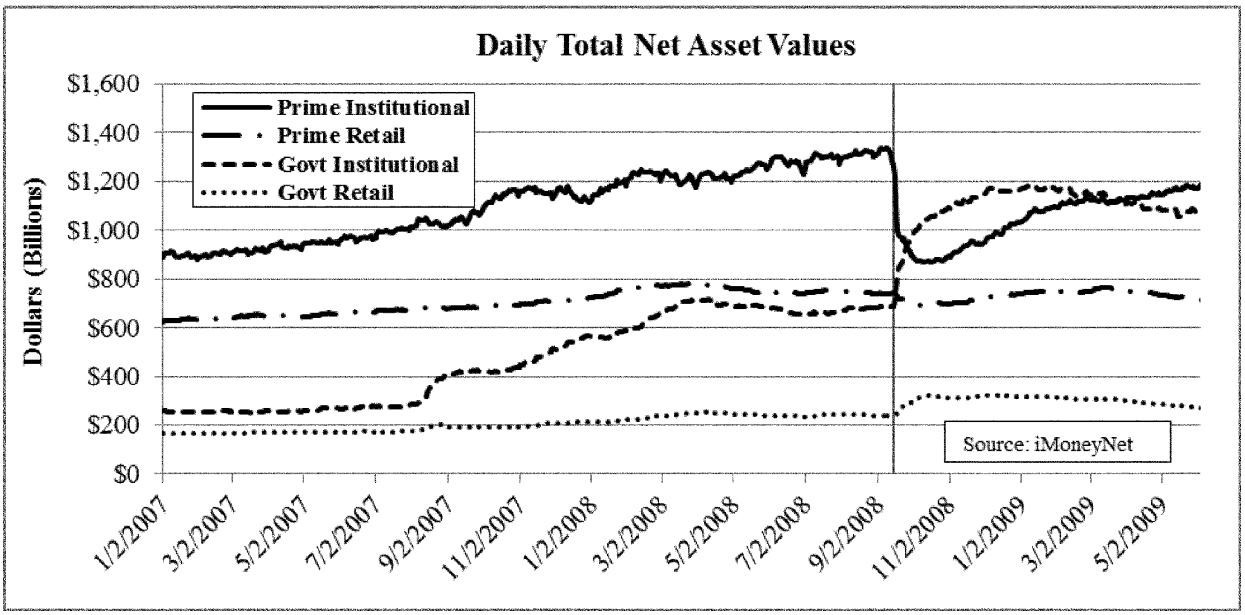
[82] *See* 2009 Proposing Release, *supra* note 31, at Section I.D.

[83] *See* RSFI Study, *supra* note 21, at section 3.

from prime money market funds or 14% of the assets in those funds.[84] During that time, fearing further redemptions, money market fund managers began to retain cash rather than invest in commercial paper, certificates of deposit, or other short-term instruments.[85] Commenters have stated that money market funds were not the only investors in the short-term financing markets that reduced or halted investment in commercial paper and other riskier short-term debt securities during the 2008 financial crisis.[86] Short-term financing markets froze, impairing access to credit, and those who were still able to access short-term credit often did so only at overnight maturities.[87]

Figure 1, below, provides context for the redemptions that occurred during the financial crisis. Specifically, it shows daily total net assets over time, where the vertical line indicates the date that Lehman Brothers filed for bankruptcy, September 15, 2008. Investor redemptions during the 2008 financial crisis, particularly after Lehman's failure, were heaviest in institutional share classes of prime money market funds, which typically hold securities that are less liquid and of lower credit quality than those typically held by government money market funds. The figure shows that institutional share classes of government money market funds, which include Treasury and government funds, experienced heavy inflows.[88] The aggregate level of retail investor redemption activity, in contrast, was not particularly high during September and October 2008, as shown in Figure 1.[89]

**Figure 1**




On September 19, 2008, the U.S. Department of the Treasury (''Treasury'') announced a temporary guarantee program (''Temporary Guarantee Program''), which would use the $50 billion Exchange Stabilization Fund to support more than $3 trillion in shares of money market funds, and the Board of Governors of the Federal Reserve System authorized the temporary extension of credit to banks to finance their purchase of high-quality asset-backed commercial paper from money market funds.[90] These programs successfully slowed redemptions in prime money market funds and provided additional liquidity to money market funds. The disruptions to the short-term markets detailed above could have continued for a longer period of time but for these programs.[91]

[84] *See* INVESTMENT COMPANY INSTITUTE, REPORT OF THE MONEY MARKET WORKING GROUP, at 62 (Mar. 17, 2009), *available at http://www.ici.org/pdf/ppr_09_mmwg.pdf* (''ICI REPORT'') (analyzing data from iMoneyNet). The latter figure describes aggregate redemptions from all prime money market funds. Some money market funds had redemptions well in excess of 14% of their assets. Based on iMoneyNet data (and excluding the Reserve Primary Fund), the maximum weekly redemptions from a money market fund during the 2008 financial crisis was over 64% of the fund's assets.

[85] *See* Philip Swagel, ''The Financial Crisis: An Inside View,'' Brookings Papers on Economic Activity, at 31 (Spring 2009) (conference draft), *available at http://www.brookings.edu/economics/bpea/~/media/Files/Programs/ES/BPEA/2009_spring_bpea_papers/2009_spring_bpea_swagel.pdf*; Christopher Condon & Bryan Keogh, *Funds' Flight from Commercial Paper Forced Fed Move,* BLOOMBERG, Oct. 7, 2008, *available at http://www.bloomberg.com/apps/news?pid=newsarchive&sid=a5hvnKFCC_pQ.*

[86] *See, e.g.,* ICI Jan. 24 FSOC Comment Letter, *supra* note 25.

[87] *See* 2009 Proposing Release, *supra* note 31, at nn.51–53 & 65–68 and accompanying text (citing to minutes of the Federal Open Market Committee, news articles, Federal Reserve Board data on commercial paper spreads over Treasury bills, and books and academic articles on the financial crisis).

[88] As discussed in section III.A.3, government money market funds historically have faced different redemption pressures in times of stress and have different risk characteristics than other money market funds because of their unique portfolio composition, which typically has lower credit default risk and greater liquidity than non-government portfolio securities typically held by money market funds.

[89] We understand that iMoneyNet differentiates retail and institutional money market funds based on factors such as minimum initial investment amount and how the fund provider self-categorizes the fund.

[90] *See* 2009 Proposing Release, *supra* note 31, at nn.55–59 and accompanying text for a fuller description of the various forms of governmental assistance provided to money market funds during this time.

[91] Treasury used the $50 billion Exchange Stabilization Fund to fund the Temporary Guarantee Program, but legislation has since been enacted prohibiting Treasury from using this fund again for guarantee programs for money market funds. *See* Emergency Economic Stabilization Act of 2008 § 131(b), 12 U.S.C. § 5236 (2008). The $50 billion Exchange Stabilization Fund was never drawn upon by money market funds under this program and the Temporary Guarantee Program expired on September 18, 2009. The Federal Reserve Board also established the Asset-Backed

*D. Examination of Money Market Fund Regulation Since the Financial Crisis*

1. The 2010 Amendments

In March 2010, we adopted a number of amendments to rule 2a–7.[92] These amendments were designed to make money market funds more resilient by reducing the interest rate, credit, and liquidity risks of fund asset portfolios. More specifically, the amendments decreased money market funds' credit risk exposure by further restricting the amount of lower quality securities that funds can hold.[93] The amendments, for the first time, also require that money market funds maintain liquidity buffers in the form of specified levels of daily and weekly liquid assets.[94] These liquidity buffers provide a source of internal liquidity and are intended to help funds withstand high redemptions during times of market illiquidity. Finally, the amendments reduce money market funds' exposure to interest rate risk by decreasing the maximum weighted average maturities of fund portfolios from 90 to 60 days.[95]

In addition to reducing the risk profile of the underlying money market fund portfolios, the reforms increased the amount of information that money market funds are required to report to the Commission and the public. Money market funds are now required to submit to the SEC monthly information on their portfolio holdings using Form N–MFP.[96] This information allows the Commission, investors, and third parties to monitor compliance with rule 2a–7 and to better understand and monitor the underlying risks of money market fund portfolios. Money market funds are now required to post portfolio information on their Web sites each month, providing investors with important information to help them make better-informed investment decisions and helping them impose market discipline on fund managers.[97]

Finally, money market funds must undergo stress tests under the direction of the board of directors on a periodic basis.[98] Under this stress testing requirement, each fund must periodically test its ability to maintain a stable NAV per share based upon 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 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. This reform was intended to provide money market fund boards and the Commission a better understanding of the risks to which the fund is exposed and give fund managers a tool to better manage those risks.[99]

2. The Eurozone Debt Crisis and U.S. Debt Ceiling Impasse of 2011

One way to evaluate the efficacy of the 2010 reforms is to examine redemption activity during the summer of 2011. Money market funds experienced substantial redemptions during this time as the Eurozone sovereign debt crisis and impasse over the U.S. debt ceiling unfolded. As a result of concerns about exposure to European financial institutions, prime money market funds began experiencing substantial redemptions.[100] Assets held by prime money market funds declined by approximately $100 billion (or 6%) during a three-week period beginning June 14, 2011.[101] Some prime money market funds had redemptions of almost 20% of their assets in each of June, July, and August 2011, and one fund lost 23% of its assets during that period after articles began to appear in the financial press that warned of *indirect* exposure of money market funds to Greece.[102] Figures 2 and 3 below show the redemptions from prime money market funds during this time, and also show that investors purchased shares of government money market funds in late June and early July in response to these concerns, but then began redeeming government money market fund shares in late July and early August, likely as a result of concerns about the U.S. debt ceiling impasse and possible ratings downgrades of government securities.[103]

Commercial Paper Money Market Mutual Fund Liquidity Facility (''AMLF''), through which credit was extended to U.S. banks and bank holding companies to finance purchases of high-quality asset-backed commercial paper (''ABCP'') from money market funds, and it may have mitigated fire sales to meet redemptions requests. *See* Burcu Duygan-Bump et al., *How Effective Were the Federal Reserve Emergency Liquidity Facilities? Evidence from the Asset-Backed Commercial Paper Money Market Mutual Fund Liquidity Facility,* 68 J. Fin. 715 (Apr. 2013) (''Our results suggest that the AMLF provided an important source of liquidity to MMMFs and the ABCP market, as it helped to stabilize MMMF asset flows and to reduce ABCP yields.''). The AMLF expired on February 1, 2010. Given the significant decline in money market investments in ABCP since 2008, reopening the AMLF would provide little benefit to money market funds today. For example, ABCP investments accounted for over 20% of Moody's-rated U.S. prime money market fund assets at the end of August 2008, but accounted for less than 10% of those assets by the end of August 2011. *See* Moody's Investors Service, *Money Market Funds: ABCP Investments Decrease,* Dec. 7, 2011, at 2. Form N–MFP data shows that as of February 28, 2013, prime money market funds held 6.9% of their assets in ABCP.

[92] Money Market Fund Reform, Investment Company Act Release No. 29132 (Feb. 23, 2010) [75 FR 10060 (Mar. 4, 2010)] (''2010 Adopting Release'').

[93] Specifically, the amendments placed tighter limits on a money market fund's ability to acquire ''second tier'' securities by (1) restricting a money market fund from investing more than 3% of its assets in second tier securities (rather than the previous limit of 5%), (2) restricting a money market fund from investing more than ½ of 1% of its assets in second tier securities issued by any single issuer (rather than the previous limit of the greater of 1% or $1 million), and (3) restricting a money market fund from buying second tier securities that mature in more than 45 days (rather than the previous limit of 397 days). *See* rule 2a–7(c)(3)(ii) and (c)(4)(i)(C). Second tier securities are eligible securities that, if rated, have received other than the highest short-term term debt rating from the requisite NRSROs or, if unrated, have been determined by the fund's board of directors to be of comparable quality. *See* rule 2a–7(a)(24) (defining ''second tier security''); rule 2a–7(a)(12) (defining ''eligible security''); rule 2a–7(a)(23) (defining ''requisite NRSROs'').

[94] The requirements are that, for all taxable money market funds, at least 10% of assets must be in cash, U.S. Treasury securities, or securities that convert into cash (*e.g.,* mature) within one day and, for all money market funds, at least 30% of assets must be in cash, U.S. Treasury securities, certain other Government securities with remaining maturities of 60 days or less, or securities that convert into cash within one week. *See* rule 2a–7(c)(5)(ii) and (iii).

[95] The 2010 amendments also introduced a weighted average life requirement of 120 days, which limits the money market fund's ability to invest in longer-term floating rate securities. *See* rule 2a–7(c)(2)(ii) and (iii).

[96] *See* rule 30b1–7.

[97] *See* rule 2a–7(c)(12).

[98] *See* rule 2a–7(c)(10)(v).

[99] *See* 2009 Proposing Release, *supra* note 31, at section II.C.3.

[100] *See* RSFI Study, *supra* note 21, at 32.

[101] *Id.*

[102] *Id.*

[103] *See also id.* at 33.

**Figure 2**

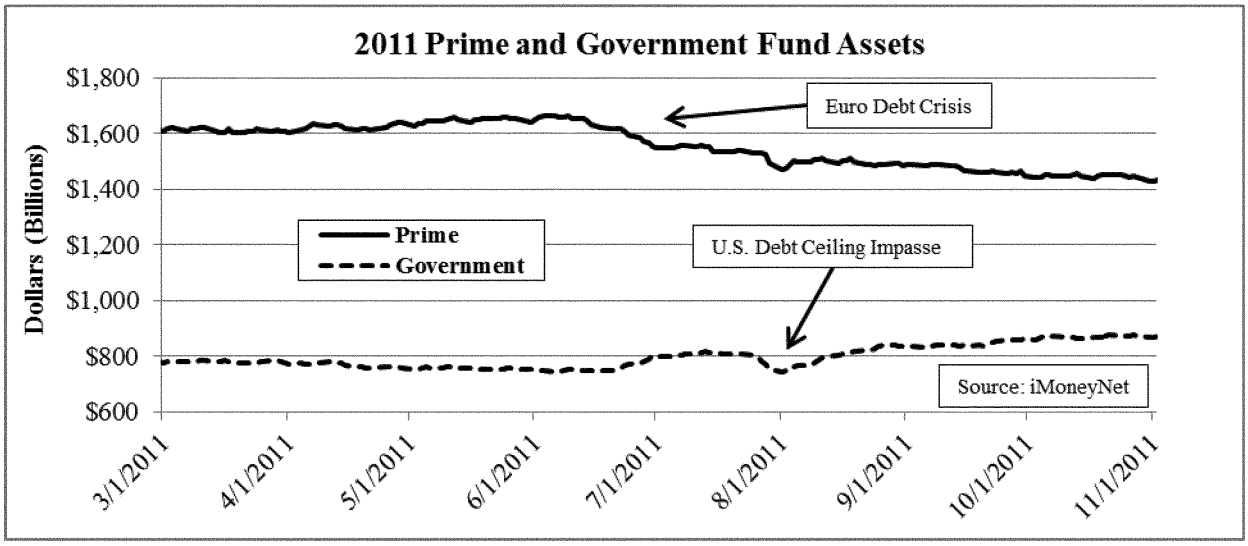
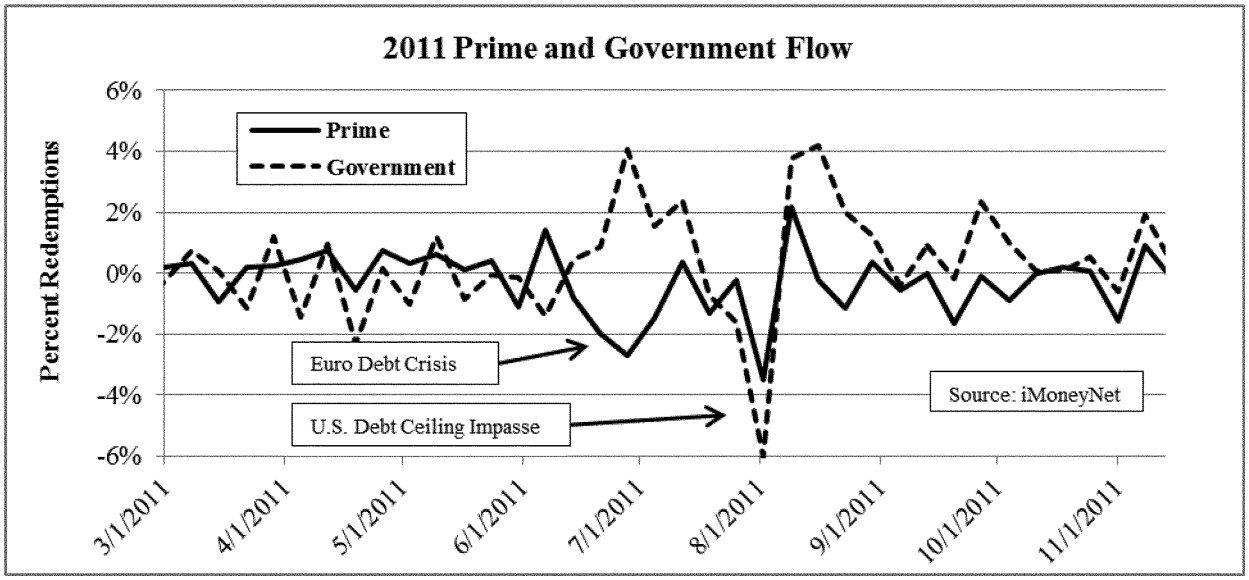



**Figure 3**




While it is difficult to isolate the effects of the 2010 amendments, these events highlight the potential increased resilience of money market funds after the reforms were adopted. Most significantly, no money market fund had to re-price below its stable $1.00 share price. As discussed in greater detail in the RSFI Study, unlike September 2008, money market funds did not experience significant capital losses that summer, and the funds' shadow prices did not deviate significantly from the funds' stable share prices; also unlike in 2008, money market funds in the summer of 2011 had sufficient liquidity to satisfy investors' redemption requests, which were made over a longer period than in 2008, suggesting that the 2010 amendments acted as intended to enhance the resiliency of money market funds.[104] The redemptions in the summer of 2011 also did not take place against the backdrop of a broader financial crisis, and therefore may have reflected more targeted concerns by investors (concern about exposure to the Eurozone and U.S. government securities as the debt ceiling impasse unfolded). Money market funds' experience in 2008, in contrast, may have reflected a broader range of concerns as reflected in the RSFI Study, which discusses a number of possible explanations for redemptions during the financial crisis.[105]

Although money market funds' experiences differed in 2008 and the summer of 2011, the heavy redemptions money market funds experienced in the

[104] *Id.* at 33–34.

[105] *Id.* at 7–13.

summer of 2011 appear to have negatively affected the markets for short-term financing. Academics researching these issues have found, as detailed in the RSFI Study, that ''creditworthy issuers may encounter financing difficulties because of risk taking by the funds from which they raise financing''; ''local branches of foreign banks reduced lending to U.S. entities in 2011''; and that ''European banks that were more reliant on money funds experienced bigger declines in dollar lending.'' [106] Thus, while such redemptions often exemplify rational risk management by money market fund investors, they can also have certain contagion effects on the short-term financing markets.

3. Our Continuing Consideration of the Need for Additional Reforms

When we proposed and adopted the 2010 amendments, we acknowledged that money market funds' experience during the 2007–2008 financial crisis raised questions of whether more fundamental changes to money market funds might be warranted.[107] We solicited and received input from a number of different sources analyzing whether or not additional reforms may be necessary, and we began to solicit and evaluate potential options for additional regulation of money market funds to address these vulnerabilities. In the 2009 Proposing Release we requested comment on certain options, including whether money market funds should be required to move to the ''floating net asset value'' used by all other mutual funds or satisfy certain redemptions in-kind.[108] We received over 100 comments on this aspect of the 2009 Proposing Release.[109] In adopting the 2010 amendments, we noted that we would continue to explore more significant regulatory changes in light of the comments we received.[110] At the time, we stated that we had not had the opportunity to fully explore possible alternatives and analyze the potential costs, benefits, and consequences of those alternatives.

Our subsequent consideration of money market funds has been informed by the work of the President's Working Group on Financial Markets, which published a report on money market fund reform options in 2010 (the ''PWG Report'').[111] We solicited comment on the features of money market funds that make them susceptible to heavy redemptions and potential options for reform both through our request for comment on the PWG Report and by hosting a May 2011 roundtable on Money Market Funds and Systemic Risk (the ''2011 Roundtable'').[112]

The potential financial stability risks associated with money market funds also have attracted the attention of the Financial Stability Oversight Council (''FSOC''), which has been tasked with monitoring and responding to threats to the U.S. financial system and which superseded the PWG.[113] On November 13, 2012, FSOC proposed to recommend that we implement one or a combination of three reforms designed to address risks to financial companies and markets that money market funds may pose.[114] The first option would require money market funds to use floating NAVs.[115] The second option would require money market funds to have a NAV buffer with a tailored amount of assets of up to 1% (raised through various means) to absorb day-to-day fluctuations in the value of the funds' portfolio securities and allow the funds to maintain a stable NAV.[116] The NAV buffer would be paired with a requirement that 3% of a shareholder's highest account value in excess of $100,000 during the previous 30 days—a ''minimum balance at risk'' (''MBR'')—be made available for redemption on a delayed basis. These requirements would not apply to certain money market funds that invest primarily in U.S. Treasury obligations and repurchase agreements collateralized with U.S. Treasury securities. The third option would require money market funds to have a risk-based NAV buffer of 3%. This 3% NAV buffer potentially could be combined with other measures aimed at enhancing the effectiveness of the buffer and potentially increasing the resiliency of money market funds, and

[106] *See id.* at 34–35 (''It is important to note, however, investor redemptions has a direct effect on short-term funding liquidity in the U.S. commercial paper market. Chernenko and Sunderam (2012) report that 'creditworthy issuers may encounter financing difficulties because of risk taking by the funds from which they raise financing.' Similarly, Correa, Sapriza, and Zlate (2012) finds U.S. branches of foreign banks reduced lending to U.S. entities in 2011, while Ivashina, Scharfstein, and Stein (2012) document European banks that were more reliant on money funds experienced bigger declines in dollar lending.'') (internal citations omitted); Sergey Chernenko & Adi Sunderam, *Frictions in Shadow Banking: Evidence from the Lending Behavior of Money Market Funds,* Fisher College of Business Working Paper No. 2012–4 (Sept. 2012); Ricardo Correa et al., *Liquidity Shocks, Dollar Funding Costs, and the Bank Lending Channel During the European Sovereign Crisis,* Federal Reserve Board International Finance Discussion Paper No. 2012–1059 (Nov. 2012); Victoria Ivashina et al., *Dollar Funding and the Lending Behavior of Global Banks,* National Bureau of Economic Research Working Paper No. 18528 (Nov. 2012).

[107] *See* 2009 Proposing Release, *supra* note 31, at section III; 2010 Adopting Release, *supra* note 92, at section I.

[108] *See* 2009 Proposing Release, *supra* note 31, at section III.A.

[109] Comments on the 2009 Proposing Release can be found at *http://www.sec.gov/comments/s7-11-09/s71109.shtml.*

[110] *See* 2010 Adopting Release, *supra* note 92, at section I.

[111] Report of the President's Working Group on Financial Markets, *Money Market Fund Reform Options* (Oct. 2010) (''PWG Report''), *available at http://www.treasury.gov/press-center/press-releases/Documents/10.21%20PWG%20Report%20Final.pdf.* The members of the PWG included the Secretary of the Treasury Department (as chairman of the PWG), the Chairman of the Board of Governors of the Federal Reserve System, the Chairman of the SEC, and the Chairman of the Commodity Futures Trading Commission.

[112] *See* President's Working Group Report on Money Market Fund Reform, Investment Company Act Release No. 29497 (Nov. 3, 2010) [75 FR 68636 (Nov. 8, 2010)]. *See also* Roundtable Transcript, *supra* note 43.

[113] The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the ''Dodd-Frank Act'') established the FSOC: (A) To identify risks to the financial stability of the United States that could arise from the material financial distress or failure, or ongoing activities, of large, interconnected bank holding companies or nonbank financial companies, or that could arise outside the financial services marketplace; (B) to promote market discipline, by eliminating expectations on the part of shareholders, creditors, and counterparties of such companies that the Government will shield them from losses in the event of failure; and (C) to respond to emerging threats to the stability of the United States financial system. The ten voting members of the FSOC include the Treasury Secretary (who serves as Chairman of the FSOC), the Chairmen of the Commission, the Board of Governors of the Federal Reserve System, the Commodity Futures Trading Commission, the Federal Deposit Insurance Corporation, and the National Credit Union Administration Board, the Directors of the Bureau of Consumer Financial Protection and the Federal Housing Finance Agency, the Comptroller of the Currency, and an independent insurance expert appointed by the President of the United States. *See* Dodd-Frank Act, Public Law 111–203, 124 Stat. 1376 §§ 111–112 (2010).

[114] *See* Proposed Recommendations Regarding Money Market Mutual Fund Reform, Financial Stability Oversight Council [77 FR 69455 (Nov. 19, 2012)] (the ''FSOC Proposed Recommendations''). Under section 120 of the Dodd-Frank Act, if the FSOC determines that the conduct, scope, nature, size, scale, concentration, or interconnectedness of a financial activity or practice conducted by bank holding companies or nonbank financial companies could create or increase the risk of significant liquidity, credit, or other problems spreading among bank holding companies and nonbank financial companies, the financial markets of the United States, or low-income, minority or under-served communities, the FSOC may provide for more stringent regulation of such financial activity or practice by issuing recommendations to primary financial regulators, like the Commission, to apply new or heightened standards or safeguards. FSOC has proposed to issue a recommendation to the Commission under this authority concerning money market funds. If FSOC issues a final recommendation to the Commission, the Commission, under section 120, would be required to impose the recommended standards, or similar standards that FSOC deems acceptable, or explain in writing to FSOC why the Commission has determined not to follow FSOC's recommendation.

[115] *See* FSOC Proposed Recommendations, *supra* note 114, at section V.A.

[116] *See id.* at section V.B.

thereby justifying a reduction in the level of the required NAV buffer.[117] Finally, in addition to proposing to recommend these three reform options, FSOC requested comment on other potential reforms, including standby liquidity fees and temporary restrictions on redemptions (''gates''), which would be implemented during times of market stress to reduce money market funds' vulnerability to runs.[118]

In its proposed recommendation FSOC stated that the Commission, ''by virtue of its institutional expertise and statutory authority, is best positioned to implement reforms to address the risk that [money market funds] present to the economy,'' and that if the Commission ''moves forward with meaningful structural reforms of [money market funds] before [FSOC] completes its Section 120 process, [FSOC] expects that it would not issue a final Section 120 recommendation.'' [119] We strongly agree that the Commission is best positioned to consider and implement any further reforms to money market funds, and we have considered FSOC's analysis of its proposed recommended reform options and the public comments that FSOC has received in formulating the money market reforms we are proposing today.

The RSFI Study, discussed throughout this Release, also has informed our consideration of the risks that may be posed by money market funds and our formulation of today's proposals. The RSFI Study contains, among other things, a detailed analysis of our 2010 amendments to rule 2a–7 and some of the amendments' effects to date, including changes in some of the characteristics of money market funds, the likelihood that a fund with the maximum permitted weighted average maturity (''WAM'') would ''break the buck'' before and after the 2010 reforms, money market funds' experience during the 2011 Eurozone sovereign debt crisis and the U.S. debt-ceiling impasse, and how money market funds would have performed during September 2008 had the 2010 reforms been in place at that time.[120]

In particular, the RSFI Study found that under certain assumptions the expected probability of a money market fund breaking the buck was lower with the additional liquidity required by the 2010 reforms.[121] In addition, funds in 2011 had sufficient liquidity to withstand investors' redemptions during the summer of 2011.[122] The fact that no fund experienced a credit event during that time also contributed to the evidence that funds' were able to withstand relatively heavy redemptions while maintaining a stable $1.00 share price. Finally, using actual portfolio holdings from September 2008, the RSFI Study analyzed how funds would have performed during the financial crisis had the 2010 reforms been in place at that time. While funds holding 30% weekly liquid assets are more resilient to portfolio losses, funds will ''break the buck'' with near certainty if capital losses of the fund's non-weekly liquid assets exceed 1%.[123] The RSFI Study concludes that the 2010 reforms would have been unlikely to prevent a fund from breaking the buck when faced with large credit losses like the ones experienced in 2008.[124] The inferences that can be drawn from the RSFI Study lead us to conclude that while the 2010 reforms were an important step in making money market funds better able to withstand heavy redemptions when there are no portfolio losses (as was the case in the summer of 2011), they are not sufficient to address the incentive to redeem when credit losses are expected to cause fund's portfolios to lose value or when the short-term financing markets more generally are expected to, or do, come under stress. Accordingly, we preliminarily believe that the alternative reforms proposed in this Release could lessen money market funds' susceptibility to heavy redemptions, improve their ability to manage and mitigate potential contagion from high levels of redemptions, and increase the transparency of their risks, while preserving, as much as possible, the benefits of money market funds.

## III. Discussion

We are proposing alternative amendments to rule 2a–7, and related rules and forms, that would either (i) require money market funds (other than government and retail money market funds) [125] to ''float'' their NAV per share or (ii) require that a money market fund (other than a government fund) whose weekly liquid assets fall below 15% of its total assets be required to impose a liquidity fee of 2% on all redemptions (unless the fund's board determines that the liquidity fee is not in the best interest of the fund). Under the second alternative, once the money market fund crosses this threshold, the fund's board also would have the ability to temporarily suspend redemptions (or ''gate'') the fund for a limited period of time if the board determines that doing so is in the fund's best interest.[126] We discuss each of these alternative proposals in this section, along with potential tax, accounting, operational, and economic implications. We also discuss a potential combination of our floating NAV proposal and liquidity fees and gates proposal, as well as the potential benefits, drawbacks, and operational issues associated with such a potential combination. We also discuss various alternative approaches that we have considered for money market fund reform.

In addition, we are proposing a number of other amendments that would apply under either alternative proposal to enhance the disclosure of money market fund operations and risks. Certain of our proposed disclosure requirements would vary depending on the alternative proposal adopted (if any) as they specifically relate to the floating NAV proposal or the liquidity fees and gates proposal. In addition, we are proposing additional disclosure reforms to improve the transparency of risks present in money market funds, including daily Web site disclosure of funds' daily and weekly liquid assets and market-based NAV per share and historic instances of sponsor support. We also are proposing to establish a new current event disclosure form that would require funds to make prompt public disclosure of certain events, including portfolio security defaults, sponsor support, a fall in the funds' weekly liquid assets below 15% of total

[117] *See id.* at section V.C.

[118] *See id.* at section V.D.

[119] *See id.* at section III.B.

[120] *See generally* RSFI Study, *supra* note 21, at section 4.

[121] *Id.* at 30.

[122] *Id.* at 34.

[123] *Id.* at 38, Table 5. In fact, even at capital losses of only 0.75% of the fund's non-weekly liquid assets and no investor redemptions, funds are already more likely than not (64.6%) to ''break the buck.'' *Id.*

[124] To further illustrate the point, the RSFI Study noted that the Reserve Primary Fund ''would have broken the buck even in the presence of the 2010 liquidity requirements.'' *Id.* at 37.

[125] Our proposed exemptions for government and retail money market funds (including our proposed definition for a retail money market fund) are discussed in sections III.A.3 and III.A.4, respectively. The exemptive amendments we are proposing are within the Commission's broad authority under section 6(c) of the Act. Section 6(c) authorizes the Commission to exempt by rule, conditionally or unconditionally, any person, security, or transaction (or classes of persons, securities, or transactions) from any provision of the Act ''if and to the extent that such exemption is necessary or appropriate in the public interest and consistent with the protection of investors and the purposes fairly intended by the policy and provisions'' of the Act. 15 U.S.C. 80a–6(c). For the reasons discussed throughout this Release, the Commission preliminarily believes that the proposed amendments to rules 2a–7, 12d3–1, 18f–3, and 22e–3 meet these standards.

[126] In the text of the proposed rules and forms below we refer to our floating NAV alternative as ''Alternative 1,'' and our liquidity fees and gates alternative as ''Alternative 2.''

assets, and a fall in the market-based price of the fund below $0.9975.

We are proposing to amend Form N–MFP to provide additional information relevant to assessing the risk of funds and make this information public immediately upon filing. In addition, we are proposing to require that a large liquidity fund adviser that manages a private liquidity fund provide security-level reporting on Form PF that are substantially the same as those currently required to be reported by money market funds on Form N–MFP.[127]

Our proposed amendments also would tighten the diversification requirements of rule 2a–7 by requiring consolidation of certain affiliates for purposes of the 5% issuer diversification requirement, requiring funds to presumptively treat the sponsors of asset-backed securities (''ABSs'') as guarantors subject to rule 2a–7's diversification requirements, and removing the so-called ''twenty-five percent basket.'' [128] Finally, we are proposing to amend the stress testing provision of rule 2a–7 to enhance how funds stress test their portfolios and require that money market funds stress test against the fund's level of weekly liquid assets falling below 15% of total assets.

We note finally that we are not rescinding our outstanding 2011 proposal to remove references to credit ratings from two rules and four forms under the Investment Company Act, including rule 2a–7 and Form N–MFP, under section 939A of the Dodd-Frank Act, and on which we welcome additional comments.[129] The Commission intends to address this matter at another time and, therefore, this Release is based on rule 2a–7 and Form N–MFP as amended and adopted in 2010.[130]

*A. Floating Net Asset Value*

Our first alternative proposal—a floating NAV—is designed primarily to address the incentive of money market fund shareholders to redeem shares in times of fund and market stress based on the fund's valuation and pricing methods, as discussed in section II.B.1 above. It should also improve the transparency of pricing associated with money market funds. Under this alternative, money market funds (other than government and retail money market funds [131]) would be required to ''float'' their net asset value. This proposal would amend [132] rule 2a–7 to rescind certain exemptions that have permitted money market funds to maintain a stable price by use of amortized cost valuation and penny-rounding pricing of their portfolios.[133] As a result, the money market funds subject to this reform would sell and redeem shares at prices that reflect the value using market-based factors of their portfolio securities and would not penny round their prices.[134] In other words, the daily share prices of these money market funds would ''float,'' which means that each fund's NAV would fluctuate along with changes, if any, in the value using market-based factors of the fund's underlying portfolio of securities.[135] Money market funds would only be able to use amortized cost valuation to the extent other mutual funds are able to do so—where the fund's board of directors determines, in good faith, that the fair value of debt securities with remaining maturities of 60 days or less is their amortized cost, unless the particular circumstances warrant otherwise.[136]

Under this approach, the ''risk limiting'' provisions of rule 2a–7 would continue to apply to money market funds.[137] Accordingly, mutual funds that hold themselves out as money market funds would continue to be limited to investing in short-term, high-quality, dollar-denominated instruments. We would, however, rescind rule 2a–7's provisions that relate to the maintenance of a stable value for these funds, including shadow pricing, and would adopt the other reforms discussed in this Release that are not related to the discretionary standby liquidity fees and gates alternative, as discussed in section III.B below.

We also propose to require that all money market funds, other than government and retail money market funds, price their shares using a more precise method of rounding.[138] The proposal would require that each money market fund round prices and transact in its shares at the fourth decimal place in the case of a fund with a $1.00 target share price (*i.e.,* $1.0000) or an equivalent level of precision if a fund prices its shares at a different target level (*e.g.,* a fund with a $10 target share price would price its shares at $10.000). Depending on the degree of fluctuation, this precision would increase the

[127] *See infra* section III.I.

[128] The ''twenty-five percent basket'' currently allows money market funds to only comply with the 10% guarantee concentration limit with respect to 75% of the fund's total assets. *See infra* section III.J.

[129] *See* References to Credit Ratings in Certain Investment Company Act Rules and Forms, Investment Company Act Release No. 29592 (Mar. 3, 2011) [76 FR 12896 (Mar. 9, 2011)] (proposing to also eliminate references to credit ratings from rule 5b–3 and Forms N–1A, N–2, and N–3, and establish new rule 6a–5 to replace a reference to credit ratings in section 6(a)(5) that the Dodd-Frank Act eliminated).

[130] *See* 2010 Adopting Release, *supra* note 92. We note that after enactment of the Dodd-Frank Act, our staff issued a no-action letter assuring money market funds and their managers that, in light of section 939A of the Dodd-Frank Act, the staff would not recommend enforcement action to the Commission under section 2(a)(41) of the Act and rules 2a–4 and 22c–1 thereunder if a money market fund board did not designate NRSROs and did not make related disclosures in its SAI before the Commission had completed its review of rule 2a–7 required by the Dodd-Frank Act and made any modifications to the rule. *See* SEC Staff No-Action Letter to the Investment Company Institute (Aug. 19, 2010). This staff guidance remains in effect until such time as the Commission or its staff indicate otherwise.

[131] The definitions of government and retail money market funds, as considered exempt under our proposals from certain proposed reforms, are discussed in sections III.A.3 and III.A.4. These funds would also price their portfolio securities using market-based factors, but would continue to be able to maintain a stable price per share through the use of the penny rounding method of pricing.

[132] References to rule 2a–7 as amended under our floating NAV proposal will be ''proposed (FNAV) rule''; similarly, references to rule 2a–7 as amended under our liquidity fees and gates proposal discussed in section III.B will be ''proposed (Fees & Gates) rule.''

[133] We also propose to amend rule 18f–3(c)(2)(i) to replace the phrase ''that determines net asset value using the amortized cost method permitted by § 270.2a–7'' with ''that operates in compliance with § 270.2a–7'' because money market funds would not use the amortized cost method to a greater extent than mutual funds generally under either of our core reform proposals.

[134] We have not previously proposed, but have sought comment on requiring money market funds to use a floating NAV. *See* 2009 Proposing Release, *supra* note 31, at section II.A. The floating NAV alternative on which we seek comment today is informed by the comments we received in response to the 2009 comment request, as well as relevant comments submitted in response to: (i) the PWG Report and (ii) the FSOC Proposed Recommendations.

[135] *See infra* note 27 for a discussion of how money market funds generally value their portfolio securities using market-based factors based on estimates from models rather than trading inputs.

[136] *See* 1977 Valuation Release, *supra* note 10. In this regard, the Commission has stated that the ''fair value of securities with remaining maturities of 60 days or less may not always be accurately reflected through the use of amortized cost valuation, due to an impairment of the creditworthiness of an issuer, or other factors. In such situations, it would appear to be incumbent on the directors of a fund to recognize such factors and take them into account in determining 'fair value.' '' *Id.* Accordingly, this guidance effectively limits the use of amortized cost valuation to circumstances where it is the same as valuation based on market factors. Some commenters voiced concern about allowing an exemption for money market funds with remaining maturities of 60 days or less. *See, e.g.,* Federal Reserve Bank Presidents FSOC Comment Letter, *supra* note 38. However, we believe that these commenters misunderstood Commission guidance in this area, which limits the use of amortized cost valuation for these securities to circumstances under which the amortized cost value accurately reflects the fair value, as determined using market factors. *See* 1977 Valuation Release, *supra* note 10.

[137] *See* proposed (FNAV) rule 2a–7(d) (risk-limiting conditions).

[138] *See* proposed (FNAV) rule 2a–7(c) (share price). We discuss our proposed amendment to share pricing in *infra* section III.A.2.

observed sensitivity of a fund's share price to changes in the market values of the fund's portfolio securities, and should better inform shareholders of the floating nature of the fund's value. Finally, we propose a relatively long compliance date of 2 years to provide time for money market funds converting to a floating NAV on a permanent basis to make system modifications and time for funds to respond to redemption requests. The extended compliance date would also allow shareholders time to understand the implications of any reforms, determine if a floating NAV money market fund is an appropriate investment, and if not, redeem their shares in an orderly fashion.

The financial crisis of 2007–2008 had significant impacts on investors, money market funds, and the short-term financing markets. The floating NAV alternative is designed to respond, at least in part, to the contagion effects from heavy redemptions from money market funds that were revealed during that crisis. As discussed in greater detail below, although it is not possible to state with certainty what would have happened if money market funds had operated with a floating NAV at that time, we expect that if a floating NAV had been in place, it could have mitigated some of the heavy redemptions that occurred due to the stable share price. Many factors, however, contributed to these heavy redemptions, and we recognize that a floating NAV requirement is a targeted reform that may not ameliorate all of those factors.

Under a floating NAV, investors would not have had the incentive to redeem money market fund shares to benefit from receiving the stable share price of a fund that may have experienced losses, because they would have received the actual market-based value of their shares. The transparency provided by the floating NAV alternative might also have reduced redemptions during the crisis that were a result of investor uncertainty about the value of the securities owned by money market funds because investors would have seen fluctuations in money market fund share prices that reflect market-based factors.

Of course, a floating NAV would not have prevented redemptions from money market funds that were driven by certain other investing decisions, such as a desire to own higher quality assets than those that were in the portfolios of prime money market funds, or not to be invested in securities at all, but rather to hold assets in another form such as in insured bank deposits. The floating NAV alternative is not intended to deter redemptions that constitute rational risk management by shareholders or that reflect a general incentive to avoid loss. Instead, it is designed to increase transparency, and thus investor awareness, of money market fund risks and dis-incentivize redemption activity that can result from informed investors attempting to exploit the possibility of redeeming shares at their stable share price even if the portfolio has suffered a loss.

1. Certain Considerations Relating to the Floating NAV Proposal

a. A Reduction in the Incentive To Redeem Shares

As discussed above, when a fund's shadow price is less than the fund's $1.00 share price, money market fund shareholders have an incentive to redeem shares ahead of other investors in times of fund and market stress. Given the size of institutional investors' holdings and their resources for monitoring funds, institutions have both the motivation and ability to act on this incentive. Indeed, as discussed above and in the RSFI Study, institutional investors redeemed shares more heavily than retail investors from prime money market funds in both September 2008 and June 2011.

Some market observers have suggested that the valuation and pricing techniques permitted by rule 2a–7 may exacerbate the incentive to redeem in money market funds if investors expect that the value of the fund's shares will fall below $1.00.[139] Our floating NAV proposal is designed to lower this risk by reducing investors' incentive to redeem shares in times of fund and market stress. Under our floating NAV proposal, money market funds would transact at share prices that reflect current market-based factors (not amortized cost or penny rounding) and thus investor incentives to redeem early to take advantage of transacting at a stable value are ameliorated.[140]

b. Improved Transparency

Our floating NAV proposal also is designed to increase the transparency of money market fund risk. Money market funds are investment products that have the potential for the portfolio to deviate from a stable value. Although many investors understand that money market funds are not guaranteed, survey data shows that some investors are unsure about the amount of risk in money market funds and the likelihood of government assistance if losses occur.[141] Similarly, many institutional investors use money market funds for liquidity purposes and are extremely loss averse; that is, they are unwilling to suffer any losses on money market fund investments.[142] Money market funds' stable share price, combined with the practice of fund management companies providing financial support to money market funds when necessary, may have

[139] *See, e.g.,* Roundtable Transcript, *supra* note 43. (Bill Stouten, Thrivent Financial) (''I think the primary factor that makes money funds vulnerable to runs is the marketing of the stable value.''); (Gary Gensler, U.S. Commodity Futures Trading Commission (''CFTC'')) (''But one thing comes along with the money market funds, which is the stable value, or if I can say as an old market guy, it's a 'free put.' You can put back an instrument and get 100 cents on the dollar. And it's that free put that I think causes some structural challenges.''); Comment Letter of Federal Reserve Bank of Richmond (Jan. 10, 2011) (available in File No. 4–619) (''Richmond Fed PWG Comment Letter''). *See also supra* section II.B (discussing the structural features of money market funds that can make them vulnerable to runs); Statement 309 of the Shadow Financial Regulatory Committee, *Systemic Risk and Money Market Mutual Funds* (Feb. 14, 2011) (available in File No. 4–619), (''[I]f fund valuations were marked to market immediately using the full NAV approach—as required for other types of mutual funds—this type of run [the September 2008 run on money market funds] would not have occurred, and there would not have been a strong economic incentive for money market mutual funds to liquidate positions.''); Gorton Shadow Banking, *supra* note 71, at 269–270 (explaining that money market funds' ability to transact at a stable $1.00 per share distinguishes them from other mutual funds, allows them to compete with bank demand deposits, and ''may have instilled a false sense of security in investors who took the implicit promise as equivalent to the explicit insurance offered by deposit accounts'').

[140] As discussed *supra* in Section II, we recognize that incentives other than those created by money market fund's stable share price exist for money market fund shareholders to redeem in times of stress, including avoidance of loss and the tendency of investors to engage in flights to quality, liquidity, and transparency.

[141] *See* Fidelity April 2012 PWG Comment Letter, *supra* note 61. For example, 41% of the retail customers surveyed said they either would expect the government to protect money market funds' stable values in times of crisis (10%) or were unsure about whether the government would do so (31%). 47% of the retail customers thought money market funds present comparable risks to ''bank products,'' which in context appears to refer to insured deposits, 12% thought money market funds posed less risk than bank products, while 36% of the retail customers thought money market funds posed more risk than bank products.

[142] *See, e.g.,* Roundtable Transcript, *supra* note 43 (Lance Pan, Capital Advisors Group) (''I would like to add that money fund investors do view money funds as liquidity vehicles, not as investment vehicles. What I mean by that is they will take zero loss, and they're loss averse as opposed to risk averse. So to the extent that they own that risk [*i.e.,* investors, rather than fund sponsors, may be exposed to a loss], at a certain point they started to own that risk, then the run would start to develop.''); Comment Letter of Treasury Strategies, Inc. (Jan. 10, 2011) (available in File No. 4–619) (''The added risk [in The Reserve Primary Fund resulting from its taking on more risk] produced higher yields, and as a result attracted substantial 'hot money' from highly sophisticated, institutional investors. These investors were fully knowledgeable of the risks they were taking, and assumed they would be the first to be able to sell their investments if the Reserve Fund's bet on a government bailout of Lehman Brothers failed.'').

implicitly encouraged investors to view these funds as ''risk-free'' cash.[143] However, the stability of money market fund share prices has been due, in part, to the willingness of fund sponsors to support the stable value of the fund. As discussed in section II.B.3 above, sponsor support has not always been transparent to investors, potentially causing investors to underestimate the investment risk posed by money market funds. As a result, money market fund investors, who were not accustomed to seeing their funds lose value, may have increased their redemptions of shares when values fell in recent times.[144]

Our floating NAV proposal is designed to increase the transparency of risks present in money market funds. By making gains and losses a more regular and observable occurrence in money market funds, a floating NAV could alter investor expectations by making clear that money market funds are not risk free and that the funds' share price will fluctuate based on the value of the funds' assets.[145] Investors in money market funds with floating NAVs should become more accustomed to, and tolerant of, fluctuations in money market funds' NAVs and thus may be less likely to redeem shares in times of stress. The proposal would also treat money market fund shareholders more equitably than the current system by requiring redeeming shareholders to receive the fair value of their shares.[146]

To further enhance transparency, we also are proposing to require a number of new disclosures related to fund sponsor support (*see* section III.F below). As discussed further in section III.E below, investors unwilling to bear the risk of a floating NAV would likely move to other products, such as government or retail money market funds (which we propose would be exempt from our floating NAV proposal and permitted to maintain a stable price).

We seek comment on this aspect of our proposal.

- Do commenters agree that floating a money market fund's NAV would lessen the incentive to redeem shares in times of fund and market stress that can result from use of amortized cost valuation and penny rounding pricing by money market funds today?
- What would be the effect of the other incentives to redeem that would remain under a floating NAV with basis point pricing requirement?
- Would floating a money market fund's NAV provide sufficient transparency to cause investors to estimate more accurately the investment risks of money market funds? Do commenters believe that daily disclosure of shadow prices on fund Web sites would accomplish the same goal without eliminating the stable share price at which fund investors purchase and redeem shares? Why or why not? Is daily disclosure of a fund's shadow price without transacting at that price likely to lead to higher or lower risks of large redemptions in times of stress? If the enhanced disclosure requirements proposed elsewhere in this Release were in place, what would be the incremental benefit of the enhanced transparency of a floating NAV?
- Are there other places to disclose the shadow price that would make the disclosure more effective in enhancing transparency?
- If the fluctuations in money market funds' NAVs remained relatively small even with a $1.0000 share price, would investors become accustomed only to experiencing small gains and losses, and therefore be inclined to redeem heavily if a fund experienced a loss in excess of investors' expectations?
- Would investors in a floating NAV money market fund that appears likely to suffer a loss be less inclined to redeem because the loss would be shared pro rata by all shareholders? Would a floating NAV make investors in a fund more likely to redeem at the first sign of potential stress because any loss would be immediately reflected in the floating NAV?
- Would floating NAV money market funds treat non-redeeming shareholders, and particularly slower-to-redeem shareholders, more equitably in times of stress?
- To the extent that some investors choose not to invest in money market funds due to the prospect of even a modest loss through a floating NAV, would the funds' resiliency to heightened redemptions be improved?
- Would money market fund sponsors voluntarily make cash contributions or use other available means to support their money market funds and thereby prevent their NAVs from actually floating?[147] Would larger fund sponsors or those sponsors with more access to capital have a competitive advantage over other fund sponsors?

c. Redemptions During Periods of Illiquidity

We recognize that a floating NAV may not eliminate investors' incentives to redeem fund shares, particularly when financial markets are under stress and investors are engaging in flights to quality, liquidity, or transparency.[148] As discussed above, the RSFI Study noted that the incentive for investors to redeem ahead of other investors is heightened by liquidity concerns–when liquidity levels are insufficient to meet redemption requests, funds may be forced to sell portfolio securities into illiquid secondary markets at

[143] *See also, e.g.,* Better Markets FSOC Comment Letter, *supra* note 67, at 11–12 (''a fluctuating NAV would correct the basic misconception among many investors that their investment is guaranteed'').

[144] *See, e.g.,* PWG Report, *supra* note 111, at 10 (''Investors have come to view MMF shares as extremely safe, in part because of the funds' stable NAVs and sponsors' record of supporting funds that might otherwise lose value. MMFs' history of maintaining stable value has attracted highly risk-averse investors who are prone to withdraw assets rapidly when losses appear possible.''); Comment Letter of Capital Advisers (Apr. 2, 2012) (available in File No. 4–619) (stating that institutional money market fund investors ''derive their risk-free assumptions from the fact that very few (a total of two) funds have experienced losses and in *all* other 'near miss' instances fund sponsors have provided voluntary capital or liquidity support to cover potential losses'' and that the ''Treasury Department further reinforced these assumptions when it announced the Temporary Guarantee Program for Money Market Funds on September 29, 2008'') (emphasis in original).

[145] For a more detailed discussion of a floating NAV and investors' expectations, *see* PWG Report, *supra* note 111, at 19–22; 2009 Proposing Release, *supra* note 31, at section III.A.

[146] *See, e.g.,* Comment Letter of Deutsche Investment Management Americas Inc. (Jan. 10, 2011) (available in File No. 4–619) (''Deutsche PWG Comment Letter'') (noting that a ''variable NAV fund . . . will treat all investors fairly during times of stress''; that ''large and sudden redemptions runs [are] a phenomenon exacerbated by the fact that amortized cost accounting rules can embed realized losses in the fund that are not reflected in the NAV''; and that ''[t]o avoid having to absorb these embedded losses, investors have the incentive to redeem early''); Comment Letter of TDAM USA Inc. (Sept. 8, 2009) (available in File No. S7–11–09) (agreeing that ''requiring money market funds to issue and redeem their shares at market value, or to float their NAVs, would in certain respects advance shareholder fairness'').

[147] In section III.A.5.a we discuss the economic implications of sponsor support under our floating NAV proposal. We are not proposing any changes that would prohibit fund sponsors from supporting money market funds under our floating NAV proposal. Our proposal also includes new disclosure requirements related to sponsor support. *See infra* section III.F.

[148] *See, e.g.,* PWG Report, *supra* note 111, at 20 (''To be sure, a floating NAV itself would not eliminate entirely MMFs' susceptibility to runs. Rational investors still would have an incentive to redeem as fast as possible the shares of any MMF that is at risk of depleting its liquidity buffer before that buffer is exhausted, because subsequent redemptions may force the fund to dispose of less-liquid assets and incur losses.''); 2009 Proposing Release, *supra* note 31, at 106 (''We recognize that a floating net asset value would not necessarily eliminate the incentive to redeem shares during a liquidity crisis—shareholders still would have an incentive to redeem before the portfolio quality deteriorated further from the fund selling securities into an illiquid market to meet redemption demands.''). *See also supra* notes 36–37 and accompanying text.

discounted or even fire-sale prices.[149] Because the potential cost of liquidity transformation is not reflected in market-based pricing until after the redemption has occurred, this liquidity pressure may create an additional incentive for investors to redeem shares in times of fund and market stress.[150] In addition, market-based pricing does not capture the likely increasing illiquidity of a fund's portfolio as it sells its more liquid assets first during a period of market stress to defer liquidity pressures as long as possible. As discussed in section II.D.1 above, our 2010 amendments, including new daily and weekly liquid asset requirements, strengthened the resiliency of money market funds to both portfolio losses and investor redemptions as compared with 2008. We note, however, that other financial intermediaries that engage in maturity transformation, including banks, also have liquidity mismatches to some degree.

We request comment on the incentive to redeem that exists in a liquidity crisis.

- Do commenters believe that a floating NAV is sufficient to address the incentive to redeem caused by liquidity concerns in times of market stress? Would other tools, such as redemption gates or liquidity fees, also be necessary?
- Do commenters believe that money market funds as currently structured present unique risks as compared with other mutual funds, all of which may face some degree of liquidity pressure during times of market stress? Would the floating NAV proposal suffice to address those risks?
- Did the 2010 amendments, including new daily and weekly liquid asset requirements, address sufficiently the incentive to redeem in periods of illiquidity?

d. Empirical Evidence in Other Floating NAV Cash Management Vehicles

Commenters have cited to the fact that some floating value money market funds in other jurisdictions and U.S. ultra-short bond mutual funds also suffered heavy redemptions during the 2007–2008 financial crisis.[151] These commenters suggest, therefore, that money market fund floating NAVs would likely not stop investors from redeeming shares. One qualification in considering these experiences is that many of the European floating NAV products that experienced heavy shareholder redemptions were priced and managed differently than our proposal and that U.S. ultra-short bond mutual funds are not subject to rule 2a–7's risk-limiting conditions.[152]

Europe, for example, has several different types of money market funds, all of which can take on more risk than U.S. money market funds as they are not currently subject to regulatory restrictions on their credit quality, liquidity, maturity, and diversification as stringent as those imposed under rule 2a–7, among other differences in regulation.[153] One commenter observed that the financial crisis was first felt in Europe when ''so-called '*enhanced money market funds,*' which used the 'money market' fund label in their marketing strategies while taking on more risk than traditional money market funds, [ran] into problems.'' [154] The difficulties experienced by these funds, the commenter asserted, ''created confusion for investors about the definition, classification and risk characteristics of money market funds.'' [155] In contrast, French *monétaire* funds, which are managed more conservatively than ''enhanced money market funds'' and thus resemble more closely the floating NAV money market funds contemplated by our proposal, generally did not experience heavy redemptions.[156] The experience of French *monétaire* funds would be consistent with another commenter's observation that ''one could reach the opposite conclusion that a variable NAV structure can, and in fact *has,* operated as intended during times of market stress in a manner consistent with minimizing systemic risk.'' [157]

U.S ultra-short bond funds also experienced redemptions in this period. U.S. ultra-short bond funds are not subject to rule 2a–7's risk-limiting conditions and although their NAVs float, pose more risk of loss to investors than most U.S. money market funds, including floating NAV money market funds under our proposal.[158] One reason that investors redeemed shares in ultra-short bond funds during the 2007–2008 financial crisis may have been because they did not fully understand the riskiness or liquidity of ultra-short

[149] *See* RSFI Study, *supra* note 21, at 4 (noting that most money market fund portfolio securities are held to maturity, and secondary markets in these securities are not deeply liquid).

[150] Although we recognize that managers of certain other mutual funds, and not just money market funds, generally sell the most liquid portfolio securities first to satisfy redemptions that exceed available cash, non-money market mutual funds generally are not as susceptible to heightened redemptions as are money market funds for a variety of reasons, including that non-money market mutual funds generally are not used for cash management.

[151] *See, e.g.,* Statement of the Investment Company Institute, SEC Open Meeting of the Investor Advisory Committee, May 10, 2010, at 4, *available at www.ici.org/pdf/24289.pdf* (stating that ''[u]ltra-short bond funds lost more than 60% of their assets from mid-2007 to the end of 2008, and French floating NAV dynamic money funds lost about 40% of their assets in a three-month time span from July 2007 to September 2007'' and that ''[s]hareholders in fixed-income funds [including those with floating NAVs] also tend to be more risk adverse and more likely to redeem shares quickly when fixed-income markets show any signs of distress''); Comment Letter of the European Fund and Asset Management Association (Jan. 10, 2011) (available in File No. 4–619) (''EFAMA PWG Comment Letter'') (noting that ''[i]n a matter of weeks, EUR 70 billion were redeemed from these [enhanced money market] funds, predominantly by institutional investors; around 15–20 suspended redemptions for a short period, and 4 of them were [definitively] closed.'').

[152] Many European floating NAV money market funds, not all of which suffered heavy redemptions, price their shares differently than floating NAV money market funds would under our proposal by accumulating rather than distributing dividends. The shares of accumulating dividend funds therefore generally will exceed one euro, and a loss in these funds would be a small reduction in the excess value above one euro as opposed to a drop in value below a single euro. This kind of floating NAV money market fund may not have affected shareholders' expectations of and tolerance for losses to the same extent as would our proposal. *See, e.g.,* Deutsche PWG Comment Letter, *supra* note 146 (stating that ''drawing parallels to the return or redemption experiences within [European money market funds and ultra-short bond funds] and those in the proposed variable NAV rule 2a–7 money market funds is not entirely accurate due to the differences in the duration of time and the magnitude of the redemption experiences'' and noting that (i) ''the variable NAV structure prevalent in many European money market funds is based on a system of accumulating dividends, not the use of a mark to market accounting system'' and (ii) ''one of the weaknesses addressed through the European Fund and Asset Management Association (''EFAMA'') and the Committee of European Securities Regulators (''CESR'') in the European style of money market funds was the lack of standardization in the definition of money market funds and the broad investment policies across EU member states''). *See also* Witmer, *supra* note 36.

[153] For a discussion of the regulation of European money market funds, *see infra* Table 2, notes E and H; Common Definition of European Money Market Funds (Ref. CESR/10–049).

[154] *See* EFAMA PWG Comment Letter, *supra* note 151 (emphasis in original).

[155] *Id.* (noting that ''[i]n a matter of weeks, EUR 70 billion were redeemed from these [enhanced money market] funds, predominantly by institutional investors; around 15–20 suspended redemptions for a short period, and 4 of them were [definitively] closed'').

[156] *See* Comment Letter of HSBC Global Asset Management on the European Commission's Green Paper on Shadow Banking (May 28, 2012) (''HSBC EC Letter''), *available at http://ec.europa.eu/internal_market/consultations/2012/shadow/individual-others/hsbc_en.pdf* (comparing inflows and outflows of European money market funds); EFAMA PWG Comment Letter, *supra* note 151 (describing the outflows from European enhanced money market funds).

[157] Deutsche PWG Comment Letter, *supra* note 146 (emphasis in original).

[158] *See, e.g.,* Witmer, *supra* note 36, at 23 (noting that ultra-short bond funds in the U.S. and enhanced money market funds in Europe both maintain a floating NAV structure, but are not subject to the same liquidity, credit, and maturity restrictions as money market funds).

bond funds. That some ultra-short bond funds experienced heavy redemptions during the financial crisis, therefore, does not necessarily suggest that investors in the floating NAV money market funds contemplated by our proposal also would experience redemptions in a financial crisis. Empirical analysis in this area also yields different opinions.[159]

Having pointed out these differences, we recognize that the data is consistent with certain commenters' view that other incentives may lead to heavy redemptions of floating NAV funds in times of stress.[160] We seek comment on the performance of other floating NAV investment products during the 2007–2008 financial crisis.

- Do commenters agree with the preceding discussion of what may have caused investors to heavily redeem shares in some floating value money market funds in other jurisdictions and in U.S. ultra-short bond funds during the 2007–2008 financial crisis? Are there other possible factors that we should consider?
- Do commenters agree with the distinctions we identified between money market funds under our proposed floating NAV and money market funds in other jurisdictions and U.S. ultra-short bond funds? Are there similarities or differences we have not identified?
- Do commenters believe that the risk limiting requirements of rule 2a–7 would deter heavy redemptions in money market funds with a floating NAV because of the restrictions on the underlying assets?
- Do commenters believe that money market funds attract very risk averse investors? If so, are these investors more or less likely to rapidly redeem in times of stress to avoid even small losses?

2. Money Market Fund Pricing

We are proposing that money market funds, other than government and retail money market funds, price their shares using a more precise method of valuation that would require funds to price and transact in their shares at an NAV that is calculated to the fourth decimal place for shares with a target NAV of one dollar (*e.g.,* $1.0000). Funds with a current share price other than $1.00 would be required to price their shares at an equivalent level of precision (*e.g.,* a fund with a $10 target share price would price its shares at $10.000).[161] The proposed change to money market fund pricing under our floating NAV proposal would change the rounding convention for money market funds—from penny rounding (*i.e.,* to the nearest one percent) to ''basis point'' rounding (to the nearest 1/100th of one percent).[162] ''Basis point'' rounding is a significantly more precise standard than the 1/10th of one percent currently required for most mutual funds.[163] For the reasons discussed below, we believe that our proposal provides the level of precision necessary to convey the risks of money market funds to investors.

Market-based valuation with penny rather than ''basis point'' rounding effectively provides the same rounding convention as exists in money market funds today—the underlying valuation based on market-based factors may deviate by as much as 50 basis points before the fund breaks the buck. Accordingly, it is unlikely to change investor behavior.

A $1.0000 share price, however, would reflect small fluctuations in value more than a $1.00 price, which may more effectively inform investor expectations. For example, the value of a $1.00 per share fund's portfolio securities would have to change by 50 basis points for investors to currently see a one-penny change in the NAV; under our proposal, the share price at which investors purchase and redeem shares would reflect single basis point variations.[164] We do not anticipate significant operational difficulties or overly burdensome costs arising from funds pricing shares using ''basis point'' rounding: A number of money market funds recently elected to voluntarily report daily shadow NAVs at this level of precision.[165]

''Basis point'' rounding should enhance many of the potential advantages of having a floating NAV. It should allow funds to reflect gains and losses more precisely. In addition, it should help reduce incentives for investors to redeem shares ahead of other investors when the shadow price is less than $1.0000 as investors would sell shares at a more precise and equitable price than under the current rules. At the same time, it should help reduce penalties for investors buying shares when shadow prices are less than $1.0000. ''Basis point'' rounding should therefore help stabilize funds in times of market stress by deterring redemptions from investors that would otherwise seek to take advantage of less precise pricing to redeem at a higher value than a more precise valuation would provide

[159] *See, e.g.,* Witmer, *supra* note 36 (empirically testing whether floating NAVs (as compared with constant NAVs) provide a benefit in reducing run-like behavior by examining flow and withdrawal behavior (from 2006 through 2011) of money market mutual funds in the United States and Europe and concluding that the variable NAV fund structure is less susceptible to run-like behavior relative to constant NAV money market funds). *But see* Comment Letter of Jeffrey Gordon (Feb. 28, 2013) (available in File No. FSOC–2012–0003) (''Gordon FSOC Comment Letter'').

[160] *See, e.g.,* Comment Letter of Treasury Strategies, Inc. (Alternative One: Floating Net Asset Value) (Jan. 15, 2013) (available in File No. FSOC–2012–0003).

[161] *See* proposed (FNAV) rule 2a–7(c). In its proposed recommendations the FSOC proposed that money market funds re-price their shares to $100.00, which is the mathematical equivalent of our $1.0000 proposed share price. *See* FSOC Proposed Recommendations, *supra* note 114, at 31. FSOC commenters generally opposed the $100.00 per share re-pricing, stating that the Investment Company Act does not require that a registered investment company offer its shares at a particular price. *See, e.g.,* Comment Letter of Federated Investors, Inc. (Re: Alternative One) (Jan. 25. 2013) (available in File No. FSOC–2012–0003) (''Federated Investors Alternative 1 FSOC Comment Letter''); ICI Jan. 24 FSOC Comment Letter, *supra* note 25. While our proposed pricing is mathematically the same as that proposed by the FSOC, pricing fund shares using $1.00 extended to four decimal places reduces other potential costs, including, for example, the possibility that funds would require corporate actions (*e.g.,* reverse stock splits) to re-price their shares at $100.00. Our proposed pricing does not mandate that funds establish a particular share price, but rather amends the precision by which a fund prices its shares.

[162] Money market funds are permitted to use penny rounding under rule 2a–7(c) and therefore, a money market fund priced at $1.00 per share may round its NAV to the nearest penny.

[163] Currently, money market funds priced at $1.00 may round their NAV to the nearest penny ($1.00). *See* rule 2a–7(c). Mutual funds other than money market funds must calculate the fund's NAV to the nearest 1/10th of 1% (*i.e.,* for funds with shares priced at $1.00, the funds should price their shares to the third decimal place, or $1.000). *See* 1977 Valuation Release, *supra* note 10. Many mutual funds typically price their shares at an initial NAV of $10 and round their NAV to the nearest penny. *See* rule 2a–4. Because floating NAV money market funds, under our proposal, would continue to adhere to rule 2a–7s's risk-limiting conditions and generally seek principal stability, we are proposing that money market funds with a floating NAV value their shares to the nearest 1/100th of 1%, a more precise standard than that required of most mutual funds today.

[164] We expect that floating $100.00 NAVs (which is the mathematical equivalent of our proposed $1.0000 NAV) would change by a penny or more during all but the shortest investment horizons. Commission staff compared reported shadow prices on Form N–MFP between November 2010 and March 2012 over consecutive one-, three-, and six-month periods. Staff estimated that there would have been no penny change over a one-month period in 98% of the months using a $10.00 NAV but only 69% of the months using a $100 NAV. Staff estimated that there would have been no penny change over a three-month period in 98% of the time using a $10 NAV but only 59% of the time using a $100.00 NAV. Staff estimates that there would have been no penny change over a six-month period in 96% of the time using a $10 NAV but only 43% of the time using a $100.00 NAV. No money market fund had a support agreement in place during this time period.

[165] Many large fund complexes have begun (or plan) to disclose daily money market fund market valuations (*i.e.,* shadow prices) of at least some of their money market funds, rounded to four decimal places (''basis point'' rounding), for example, BlackRock, Fidelity Investments, and J.P. Morgan. *See, e.g., Money Funds' New Openness Unlikely to Stop Regulation,* Wall St. J. (Jan. 30, 2013).

and thus dilute the value of the fund for remaining shareholders.

Our proposed amendment to require that money market funds use ''basis point'' rounding should provide shareholders with sufficient price transparency to better understand the tradeoffs between risk and return across competing funds, and become more accustomed to fluctuations in market value of a fund's portfolio securities.[166] It should allow them to appreciate that some money market funds may experience greater price volatility than others, and thus that there are variations in the risk profiles of different money market funds.

We also considered whether to require that money market funds price to three decimal places (for a fund with a target share price of $1.000), as other mutual funds do. We are concerned, however, that such ''10 basis point'' rounding may not be sufficient to ensure that investors do not underestimate the investment risks of money market funds, particularly if funds manage themselves in such a way that their NAVs remain constant or nearly constant. Fund investment managers may respond to a floating NAV with ''10 basis point'' rounding by managing their portfolios more conservatively to avoid volatility that would require them to price fund shares at something other than $1.000. It is possible that managers would be able to avoid this volatility for quite some time, even with a floating NAV.[167] Although a floating NAV with ''basis point'' rounding may discourage risk taking in funds, a floating NAV with ''10 basis point'' rounding may mask small deviations in the market-based value of the fund's portfolio securities.

We seek comment on this aspect of our proposal.

- What level of precision in calculating a fund's share price would best convey to investors that floating NAV funds are different from stable price funds? Is ''basis point'' rounding too precise? Would ''10 basis point rounding'' ($1.000 for a fund with a $1.00 target share price) provide sufficient price transparency? Or another measure?
- Would requiring funds to price their shares at $1.0000 per share effectively alter investor expectations regarding a fund's NAV gains and losses? Would this in turn make investors less likely to redeem heavily when faced with potential or actual losses?
- Would ''basis point'' rounding better reflect gains and losses? Would it help eliminate incentives for investors to redeem shares ahead of other investors when prices are less than $1.0000?
- Should we require that all money market funds price their shares at $1.0000, including those funds that currently price their shares at an initial value other than $1.00? Do commenters agree that, regardless of a fund's initial share price, under our proposal all money market funds would be required to price fund shares to an equivalent level of precision (*e.g.,* ''basis point'' rounding)?
- What would be the cost of implementing ''basis point'' rounding? Would funds require corporate actions or shareholder approval to price fund shares at $1.0000? What operational changes and related costs would be involved?

3. Exemption to the Floating NAV Requirement for Government Money Market Funds

We are proposing an exemption to the floating NAV requirement for government money market funds–money market funds that maintain at least 80% of their total assets in cash, government securities, or repurchase agreements that are collateralized fully.[168] We believe that a government money market fund that maintains 80% of its total assets in cash and government securities fits within the typical risk profile of government money market funds as understood by investors, and is the portfolio holdings test used today for determining the accuracy of a fund's name.[169] Under the proposal, government money market funds would not be subject to the basis point rounding aspect of the floating NAV requirement and instead would be permitted to use the penny rounding method of pricing fund shares to maintain a stable price.[170]

As discussed above, government money market funds face different redemption pressures and have different risk characteristics than other money market funds because of their unique portfolio composition.[171] The securities primarily held by government money market funds typically have even a lower credit default risk than commercial paper and are highly liquid in even the most stressful market scenario.[172] The primary risk that these funds bear is interest rate risk; that is, the risk that changes in interest rates result in a change in the market value of portfolio securities. Even the interest rate risk of government money market funds, however, is generally mitigated because they typically hold assets that have short maturities and hold those assets to maturity.[173]

Nonetheless, it is possible that a government money market fund could undergo such stress that it results in a significant decline in a fund's shadow price. Government money market funds may invest up to 20% of their portfolio in non-government securities, and a credit event in that 20% portion of the portfolio or a shift in interest rates could trigger a drop in the shadow price, thereby creating incentives for shareholders to redeem shares ahead of other investors.

[166] Similar to other mutual funds, our proposed pricing of money market fund shares would continue to allow shareholders to purchase and redeem fractional shares, and therefore would not affect the ability of shareholders to purchase and redeem shares with round or precise dollar amounts as they do today.

[167] *See, e.g.,* PWG Report, *supra* note 111, at 22 (''Investors' perceptions that MMFs are virtually riskless may change slowly and unpredictably if NAV fluctuations remain small and rare. MMFs with floating NAVs, at least temporarily, might even be more prone to runs if investors who continue to see shares as essentially risk-free react to small or temporary changes in the value of their shares.''); Comment Letter of Federated Investors, Inc. (May 19, 2011) (available in File No. 4–619) (stating that ''managers would employ all manners of techniques to minimize the fluctuations in their funds' NAVs'' and, therefore, ''[i]nvestors would then expect the funds to exhibit very low volatility, and would redeem their shares if the volatility exceeded their expectations'').

[168] Proposed (FNAV) rule 2a–7(c)(2).

[169] For example, some government money market funds limit themselves to holding mostly Treasury securities and Treasury repos and are referred to as ''Treasury money market funds.'' To comply with the investment company names rule, funds that hold themselves out as Treasury money market funds must hold at least 80% of their portfolio assets in U.S. Treasury securities and for Treasury repos. *See* rule 35d–1 (a materially deceptive and misleading name of a fund (for purposes of section 35(d) of the Investment Company Act (Unlawful representations and names)) includes a name suggesting that the fund focuses its investments in a particular type of investment or in investments in a particular industry or group of industries, unless, among other requirements, the fund has adopted a policy to invest, under normal circumstances, at least 80% of the value of its assets in the particular type of investments or industry suggested by the fund's name).

[170] As discussed in greater detail below, money market funds that take advantage of an exemption to the floating NAV requirement would not be able to use the amortized cost method of valuation, but would instead be required to only use the penny rounding method of pricing to facilitate a stable price per share.

[171] *See, e.g.,* Comment Letter of Charles Schwab (Jan. 17, 2013) (available in File No. FSOC–2012–0003) (''Schwab FSOC Comment Letter''); FSOC Proposed Recommendations, *supra* note 114, at 9.

[172] *See, e.g.,* RSFI Study, *supra* note 21, at 8–9; Comment Letter of Vanguard (Jan. 15, 2013) (available in File No. FSOC–2012–0003) (''Vanguard FSOC Comment Letter'').

[173] *See, e.g.,* ICI Jan. 24 FSOC Comment Letter, *supra* note 25 (''Given the short duration of [government] money market fund portfolios, any interest rate movements have a modest and temporary effect on the value of the fund's securities'').

Despite these risks, we believe that requiring government money market funds to float their NAV may be unnecessary to achieve policy goals.[174] As discussed below, shifting to a floating NAV could impose potentially significant costs on both a fund and its investors. In light of the evidence of investor behavior during previous crises, it does not appear that government money market funds are as susceptible to the risks of mass investor redemptions as other money market funds.[175] Investors have frequently noted the benefits of having a stable money market fund option, and exempting government money market funds from a floating NAV would allow us to preserve this option at a minimal risk.[176] On balance, we believe the benefits of retaining a stable share price money market fund option and the relative safety in a government money market fund's 80% bucket appropriately counterbalances the risks associated with the 20% portion of a government money market fund's portfolio that may be invested in securities other than cash, government securities, or repurchase agreements.

Under the proposal, funds taking advantage of the government fund exemption (as well as funds using the retail exemption discussed in the next section) would no longer be permitted to use the amortized cost method of valuation to facilitate a stable NAV, but would continue to be able to use the penny rounding method of pricing. While today virtually all money market funds use both amortized cost valuation and penny rounding pricing together to maintain a stable value, either method alone effectively provides the same 50 basis points of deviation from a fund's shadow price before the fund must ''break the buck'' and re-price its shares. Accordingly, today the principal benefit from money market funds being able to use amortized cost valuation *in addition to* basis point rounding is that it alleviates the burden of the money market fund having to value each portfolio security each day using market factors.[177] However, as described in section III.F.3 below, we are proposing that all money market funds be required to disclose on a daily basis their share price with portfolios valued using market factors and applying basis point rounding. As a result, money market funds—including those exempt from the floating NAV requirement—would have to value their portfolio assets using market factors instead of amortized cost each day. Accordingly, in line with this increased transparency on the valuation of money market funds' portfolios, and in light of the fact that this increased transparency renders penny rounding alone an equal method of achieving price stability in money market funds, we are proposing that the government exemption permit penny rounding pricing alone and not also amortized cost valuation for all portfolio securities.

The government money market fund exemption to the floating NAV requirement would not be limited solely to Treasury money market funds, but also would extend to money market funds that invest at least 80% of their portfolio in cash, ''government securities'' as defined in section 2(a)(16) of the Act, and repurchase agreements collateralized with government securities. Allowable securities would include securities issued by government-sponsored entities such as the Federal Home Loan Banks, government repurchase agreements, and those issued by other ''instrumentalities'' of the U.S. government.[178] It would exclude, however, securities issued by state and municipal governments, which do not generally share the same credit and liquidity traits as U.S. government securities.[179]

Today, government money market funds hold approximately $910 billion in assets, or around 40% of all money market fund assets.[180] Fund groups that wish to focus on offering stable price products could offer government and retail money market funds. We also note that our proposed retail money market fund exemption discussed in the next section would likely cover most municipal (or tax-exempt) funds, because the tax advantages that these funds offer are only enjoyed by individuals and thus most of these funds could continue to offer a stable share price.[181] Similarly, investors who prefer a stable price fund or are unable to invest in a floating NAV fund could choose to invest in government money market funds. These investors could continue to use these money market funds as a cash management tool without incurring any costs or other effects associated with floating NAV investment vehicles.

We request comment on this aspect of our proposal.

- Do commenters agree with our assumption that money market funds with at least 80% of their total assets in cash, government securities, and government repos are unlikely to suffer losses due to credit quality problems correct? Is our assumption that they are unlikely to be subject to significant shareholder redemptions during a financial crisis correct?
- Should government money market funds be exempt from the floating NAV requirement? Why or why not? Are there other risks, such as interest rate or liquidity risks, about which we should be concerned if we adopt this proposed exemption to the floating NAV requirement? If so, what are they and how should they be addressed?
- Would the costs imposed on government money market funds if we required them to price at a floating NAV be different from the costs discussed below?
- Are the proposed criteria for qualifying for the government money market funds exemption to the floating NAV requirement appropriate? Should government money market funds be required to hold more or fewer than 80% of total assets in cash, government securities, and government repos? If so, what should it be and why?
- What kinds of risks are created by exempting government money market funds from a floating NAV requirement where the funds are permitted to maintain 20% of their portfolio in securities other than cash, government securities, and government repos? Should there be additional limits or

[174] Many commenters have agreed with this position, suggesting that a floating NAV proposal should exempt government money market funds. *See, e.g.,* Comment Letter of The Dreyfus Corporation (Feb. 11, 2013) (available in File No. FSOC–2012–0003) (''Dreyfus FSOC Comment Letter''); Comment Letter of Northern Trust (Feb. 14, 2013) (available in File No. FSOC–2012–0003) (''Northern Trust FSOC Comment Letter''); ICI Jan. 24 FSOC Comment Letter, *supra* note 25.

[175] *See* RSFI Study, *supra* note 21, at 12–13 (examining the change in daily assets of different types of money market funds and highlighting abnormally large inflows into institutional and retail government funds during September 2008).

[176] *See, e.g.,* Comment Letter of Allegheny Conference on Community Development (Jan. 4, 2013) (available in File No. FSOC–2012–0003) (''Many nonprofit institutions are required, by law or by investment policy, to invest cash only in products offering a stable value''); Comment Letter of New Jersey Association of Counties (Dec. 21, 2012) (available in File No. FSOC–2012–0003) (''We thus strongly support maintaining the ability of money market funds to offer a stable $1.00 per-share value'').

[177] Rule 2a–7 currently requires a money market fund's board of directors to review the amount of deviation between the fund's market-based NAV per share and the fund's amortized cost per share ''periodically.'' Rule 2a–7(c)(8)(ii)(A)(2).

[178] Section 2(a)(16) of the Investment Company Act.

[179] *See, e.g.,* RSFI Study, *supra* note 21; Schwab FSOC Comment Letter, *supra* note 171 (''There may be slightly higher risk in municipal money market funds, but these funds tend to be more liquid than most prime funds.'').

[180] Based on iMoneyNet data.

[181] We note that there are some tax-exempt money market funds that self-classify as institutional funds to private reporting services such as iMoneyNet. We understand that these funds' shareholder base typically is comprised of omnibus accounts, with underlying individual investors.

requirements on the 20%? Would investors have incentives to redeem shares ahead of other investors if they see a material downgrade in securities held in the 20% basket? Would such an incentive create a significant risk of runs?

• Is penny rounding sufficient to allow government money market funds to maintain a stable price? Should we also permit these funds to use amortized cost valuation? If so, why? Should we permit money market funds to continue using amortized cost valuation for certain types of securities, such as government securities? Why?

• If the Commission does not adopt this exemption, how many investors in government money market funds might reallocate assets to non-government money market fund alternatives? How many assets in government money market funds might be reallocated to alternatives? To what non-government money market fund alternatives are these investors likely to reallocate their investments?

• Should we provide other exemptions to the floating NAV requirement based on the characteristics of a fund's portfolio assets, such as funds that hold heightened daily or weekly liquid assets? If so, why and what threshold should we use?

• Should money market funds that invest primarily in municipal securities be exempted from the floating NAV requirement? Why or why not? To what extent would such funds expect to qualify for the retail exemption?

4. Exemption to the Floating NAV Requirement for Retail Money Market Funds

a. Overview

We are also proposing to exempt money market funds that are limited to retail investors from our floating NAV proposal by allowing them to use the penny rounding method of pricing instead of basis point rounding.[182] Under this proposal, retail funds would still generally be required to value portfolio securities using market-based factors rather than amortized cost. As discussed in detail below, retail investors historically have behaved differently from institutional investors in a crisis, being much less likely to make large redemptions quickly in response to the first sign of market stress. Thus, prime money market funds that are limited to retail investors in general have not been subject to the same pressures as institutional or mixed funds.[183] Under the proposed exemption, we would define a retail fund as a money market fund that does not permit a shareholder to redeem more than $1 million in a single business day. We would permit retail funds to continue to maintain a stable price. As of February 28, 2013, funds that self-report as retail money market funds currently hold nearly $695 billion in assets, which is approximately 26% of all assets held in money market funds.[184]

As noted above in section II, during the 2007–2008 financial crisis, institutional prime money market funds had substantially greater redemptions than retail prime money market funds.[185] For example, approximately 4–5% of prime retail money market funds had outflows of greater than 5% on each of September 17, 18, and 19, 2008, compared to 22–30% of prime institutional money market funds.[186] Similarly, in late June 2011, institutional prime money market funds experienced heightened redemptions in response to concerns about their potential exposure to the Eurozone debt crisis, whereas retail prime money market funds generally did not experience a similar increase.[187] Studies of money market fund redemption patterns in times of market stress also have noted this difference.[188] As discussed above, institutional shareholders tend to respond more quickly than retail shareholders to potential market stresses because generally they have greater capital at risk and may be better informed about the fund through sophisticated tools to monitor and analyze the portfolio holdings of the funds in which they invest.

Given the tendency of retail investors to continue to hold money market fund shares in times of market stress, it appears to be unnecessary to impose a floating NAV requirement on retail funds to address the risk that a fund would be unable to manage heavy redemptions in times of crisis.[189] We understand that funds designed for retail investors generally do not have a concentrated shareholder base and are therefore less likely to experience large and unexpected redemptions that would put a strain on the fund's liquidity.[190] Some commenters have therefore suggested providing an exemption for retail funds to preserve the current benefits of money market funds for these investors, and as a consequence, reduce the macroeconomic effects that may be associated with a floating NAV requirement.[191] A retail exemption may also reduce the operational burdens of implementing a floating NAV, because retail funds and their intermediaries may not need to undertake the operational costs of transitioning

[182] Much like under the government fund proposal, funds that take advantage of the retail exemption would not be able to use the amortized cost method of valuation to facilitate a stable NAV for the same reasons as discussed in section III.A.3 above.

[183] *See, e.g.,* Comment Letter of United Services Automobile Association (Feb. 15. 2013) (available in File No. FSOC–2012–0003) (''USAA FSOC Comment Letter'') (''Retail MMFs do not need additional or more stringent regulation to prevent runs because retail investors are inherently (and historically) less likely to cause runs.'').

[184] Based on iMoneyNet data. Of these assets, approximately $497 billion are held by prime money market funds and another $198 billion are in government funds. Because we are proposing to exempt government funds from the floating NAV requirement, the proposed retail exemption would only be relevant to the investors holding the $497 billion in retail prime funds.

[185] *See* RSFI Study, *supra* note 21, at 8. We note that the RSFI Study used a definition of retail fund based on fund self-classification, which does not entirely correspond with the definition of retail fund that we are proposing today.

[186] Based on iMoneyNet data. iMoneyNet classifies retail and institutional money market funds according to who is eligible to purchase fund shares, minimum initial investment amount in the fund, and to whom the fund is marketed. However, as discussed *infra,* there is currently no regulatory distinction that reliably distinguishes these types of investors, and the iMoneyNet method uses a different method of classification than the method we are proposing.

[187] Based on iMoneyNet data. Retail money market funds suffered net redemptions of less than 1% between June 14, 2011 and July 5, 2011, and only 27 retail money market funds had redemptions in excess of 5% during that period (and of these funds only 7 had redemptions in excess of 10% during this period), far fewer redemptions than those incurred by institutional funds.

[188] *See, e.g.,* RSFI Study, *supra* note 21, at 8; Cross Section, *supra* note 60, at 9 (noting that institutional prime money market funds suffered net redemptions of $410 billion (or 30% of assets under management) in the four weeks beginning September 10, 2008, based on iMoneyNet data, while retail prime money market funds suffered net redemptions of $40 billion (or 5% of assets under management) during this same time period); Kacperczyk & Schnabl, *supra* note 60, at 31; Wermers Study, *supra* note 64.

[189] *See* Comment Letter of Reich & Tang (Feb. 14, 2013) (available in File No. FSOC–2012–0003) (''Reich & Tang FSOC Comment Letter'') (''As a general rule, retail investors' use of money market funds tends to be stable and countercyclical. . . . This is in direct contrast to the general behavior of institutional investors.'').

[190] *See* Comment Letter of John M. Winters (Dec. 18, 2012) (available in File No. FSOC–2012–0003) (''Winters FSOC Comment Letter'') (''Retail MMFs and institutional government MMFs do not have a liquidity problem due to the nature of the investor type or portfolio securities. . . .'').

[191] *See, e.g.,* USAA FSOC Comment Letter, *supra* note 183 (''Bifurcation would allow retail MMFs to continue to play the same vital role they do today, provide retail investors with professional investment management services, portfolio diversification and liquidity, while also acting as a key provider of financing in the broader capital markets''); Reich & Tang FSOC Comment Letter, *supra* note 189 (''A departure of this nature would diminish and endanger the benefits [of MMFs] to retail investors and cause these same individuals to seek potentially less appropriate or riskier alternatives.''). *See also infra* section III.E.

systems or managing potential tax and accounting issues associated with a floating NAV. However, other commenters have opposed a retail exemption, citing the difficulty of distinguishing retail and institutional investors, operational issues, and other concerns.[192]

In 2009, similar considerations led us to propose lower requirements for the amount of daily and weekly liquid assets that retail money market funds would need to hold compared with institutional funds.[193] We noted that retail prime money market funds experienced significantly fewer outflows when compared with institutional prime money market funds in the fall of 2008.[194] Although we have not adopted that proposal, in part because we recognize significant difficulties in distinguishing retail from institutional funds for purposes of that reform, we continue to consider whether retail and institutional money market funds should be subject to different requirements.

It is important to note that some commenters on our 2009 money market fund reforms proposal suggested that not all retail and institutional shareholders behave the same way as their peers.[195] Also, although retail shareholders during recent financial crises have not redeemed from money market funds in large numbers in response to market stress, this does not necessarily mean that in the future they will not eventually exhibit increased redemption activity if stress on one or more money market funds persists.[196] Empirical analyses of retail money market fund redemptions during the 2007–2008 financial crisis show that at least some retail investors eventually began redeeming shares.[197] The introduction of the Treasury Temporary Guarantee Program on September 19, 2008 (a few days after institutional prime money market funds experienced heavy redemptions) may have prevented shareholder redemptions from accelerating in retail money market funds. Commenters on the FSOC Proposed Recommendations also have questioned whether the behavior of retail investors during the 2008 crisis should be regarded as definitive.[198]

The evidence, however, suggests that retail investors tend to redeem shares slowly in times of fund and market stress or do not redeem shares at all. As indicated in the RSFI study, such lower redemptions may be more readily managed without adverse effects on the fund, in part because of the Commission's enhanced liquidity requirements adopted in 2010.[199] However, we recognize that by providing a retail exemption to the floating NAV, we would be leaving in place for those investors the existing incentive to redeem that can result from the use of a stable price, and some retail investors could potentially benefit from redeeming shares ahead of other retail investors in times of fund and market stress.[200]

The retail exemption would take the same form as the government exemption in allowing these money market funds to price using penny rounding instead of basis point rounding. For the reasons described in section III.A.3 above, we do not believe that allowing continued use of amortized cost valuation for all securities in these funds' portfolios is appropriate given that these funds will be required to value their securities using market factors on a daily basis due to new Web site disclosure requirements described in section III.F.3 and given that penny rounding otherwise achieves the same level of price stability.

We request comment on whether we should provide a retail money market fund exemption to the floating NAV.

- Are we correct in our understanding that retail investors are less likely to redeem money market fund shares in times of market stress than institutional investors? Or are they just slower to participate in heavy redemptions?
- Does the evidence showing that retail investors behave differently than institutional investors justify a retail exemption? Is this difference in behavior likely to continue in the future?
- Would a retail exemption reduce the operational effects of implementing the floating NAV requirement, such as systems changes and tax and accounting issues? If so, to what extent and how?
- If the Commission does not adopt an exemption to the floating NAV requirement for retail funds, how many investors in retail prime money market funds might reallocate assets to non-prime money market fund alternatives? How many assets in retail prime money market funds might be reallocated to alternatives? To what non-prime money market alternatives are retail investors likely to reallocate their investments?[201]
- Are we correct that retail investors would prefer an exemption from the floating NAV requirement? Would they instead prefer to invest in floating NAV funds? If so, why?
- Is penny rounding sufficient to allow retail money market funds to maintain a stable price? Should we also permit these funds to use amortized cost valuation? If so, why?
- Should we consider requiring retail funds that rely on an exemption from

[192] *See, e.g.,* Comment Letter of Invesco Ltd. (Feb. 15, 2013) (available in File No. FSOC–2012–0003) (''Invesco FSOC Comment Letter'') (''While we acknowledge that the disruptions experienced by MMFs during the 2008 financial crisis were largely attributable to prime MMF redemptions by large investors, we believe that efforts to characterize MMFs or their investors as either ''institutional'' or ''retail'' are misplaced and impractical due to the difficulty of establishing a litmus test that can be used consistently to identify those investors most likely to trigger a MMF run.''); Comment Letter of Federated Investors, Inc. (Feb. 15. 2013) (available in File No. FSOC–2012–0003) (''Federated Investors Feb. 15 FSOC Comment Letter'').

[193] In 2009, we proposed to define a retail money market fund as a money market fund that was not an institutional fund, and to define an institutional fund as a money market fund whose board of directors, considering a number of factors, determines that is ''intended to be offered to institutional investors.'' *See* 2009 Proposing Release, *supra* note 31, at section II.C.2.

[194] *Id.* at n.185 and accompanying text.

[195] *See, e.g.,* Comment Letter of Invesco Aim Advisors, Inc. (Sept. 4, 2009) (available in File No. S7–11–09) (''Invesco 2009 Comment Letter''); Comment Letter of Federated Investors, Inc. (Sept. 8, 2009) (available in File No. S7–11–09).

[196] *See, e.g.,* Comment Letter of HSBC Global Asset Management Ltd (Feb. 15, 2013) (available in File No. FSOC–2012–0003) (''HSBC FSOC Comment Letter'') (''Whilst the credit crisis of 2008 is an important data point to compare investor behavior, there are other data points in history that show that retail investors do ''run'' from investments (banks, other types of mutual fund) during times of market crisis.'').

[197] *See, e.g.,* Cross Section, *supra* note 60, at 25–26 (finding that net redemptions from retail prime money market funds in September 2008 indicates that higher risk money market funds did have greater net outflows but only late in the run and that outflows from retail money market funds peaked later than those from institutional funds); Wermers Study, *supra* note 64, at 3 (analysis of money market fund redemption data from the 2007–2008 financial crisis showed that ''prime institutional funds exhibited much larger persistence in outflows than retail funds, although retail investors also exhibited some run-like behavior.'').

[198] *See, e.g.,* Federated Investors Feb 15 FSOC Comment Letter, *supra* note 192 (''The oft-repeated point that some funds labeled ''institutional'' experienced higher redemptions than some funds labeled ''retail'' during the financial crisis is not sufficient. Many so-called institutional funds experienced the same or even lower levels of redemptions as so-called [retail money market] funds during the period of high redemptions during the financial crisis, and many funds included both retail and institutional investors.'').

[199] *See supra* section II.D.2 for a discussion of how these enhanced liquidity requirements were more effective in providing stability in the face of the slower pace of redemptions in institutional prime money market funds in June and July of 2011 in response to the Eurozone debt crisis compared with the very rapid heavy redemptions that occurred in September 2008. *But see* RSFI study, *supra* at note 21, at 37 (noting that The Reserve Primary Fund would have broken the buck even in the presence of the 2010 liquidity requirements).

[200] *See* Dreyfus FSOC Comment Letter, *supra* note 174 (''Thus while it can be expected that different kinds of prime money market funds may experience different levels of redemption activity, it may not be the case that different kinds of prime money market funds have different credit risk profiles.'').

[201] *See infra* section III.E.

the floating NAV requirement to be subject to the liquidity fees and gates requirement described in section III.B?

b. Operation of the Retail Fund Exemption

The operational challenges of implementing an exemption for retail investor funds are numerous and complex. Currently, many money market funds are owned by both retail and institutional investors, although many are separated into retail and institutional share classes.[202] With the retail exemption to the floating NAV requirement, funds with separate share classes for different types of investors (as well as funds that mix different types of investors together) that wish to offer a stable price would need to reorganize, offering separate money market funds to retail and institutional investors.[203] We recognize that any distinction could result in ''gaming behavior'' whereby investors having the general attributes of an institution might attempt to fit within the confines of whatever retail exemption we craft.[204]

It can be difficult to distinguish objectively between retail and institutional money market funds, given that funds generally self-report this designation, there are no clear or consistent criteria for classifying funds and there is no common regulatory or industry definition of a retail investor or a retail money market fund.[205] Many of the issues that we discuss below regarding distinguishing between types of investors were raised by our 2009 proposed money market fund reforms in which we proposed to establish different liquidity requirements for institutional and retail money market funds.[206] Many commenters then asserted that distinguishing between retail and institutional money market funds would be difficult given the extent to which shares of money market funds are held by investors through omnibus accounts and other financial intermediaries.[207]

Some commenters at the time, however, suggested possible approaches we might take.[208] We have since received more comments suggesting other methods for distinguishing between investor types.[209] The daily redemption limit method we are proposing today is an objective criterion intended to encourage self-identification of retail investors, because we understand that institutional investors generally would not be able to tolerate such redemption limits and they would accordingly self-select into institutional money market funds designed for them, while we anticipate that the limit would not constrain how most retail investors typically use money market funds. We also discuss several alternate methods we could use to make such a distinction below.

i. Daily Redemption Limit

We are proposing to define a retail money market fund as a money market fund that restricts a shareholder of record from redeeming more than $1,000,000 in any one business day.[210] We believe that this approach would be relatively simple to implement, since it would only require a retail money market fund to establish a one-time, across-the-board redemption policy,[211] and unlike other approaches discussed below, it would not depend on a fund's ability to monitor the dollar amounts invested in shareholders' accounts, shareholder concentrations, or other shareholder characteristics. A daily redemption limitation approach also should reduce the risk that a retail fund will experience heavier redemption requests than it can effectively manage in a crisis, because it will limit the total amount of redemptions a fund can experience in a single day, allowing the fund time to better predict and manage its liquidity.[212]

A redemption limitation approach to defining retail funds should also lead institutions to self-select into institutional floating money market funds, since retail money market funds with redemption limitations would typically not meet their operational needs.[213] This incentive to self-select may help mitigate (but cannot eliminate) ''gaming'' by investors with institutional characteristics who otherwise might be tempted to try and invest in stable price retail funds, compared to the other methods of distinguishing investors discussed below. Even if an institutional investor purchased shares in a stable price fund, the institutional investor would be subject to the $1 million daily redemption limit. Retail investors rarely need the ability to redeem such a significant amount on a daily basis, and if they do anticipate needing to make

[202] Several of the largest prime money market funds have both institutional and retail share classes. For example, *see* Vanguard Money Market Reserves, Vanguard Prime Money Market Fund Investor Shares (VMMXX), Registration Statement (Form N–1A) (Dec. 28, 2012); Vanguard Money Market Reserves, Vanguard Prime Money Market Fund Institutional Shares (VMRXX), Registration Statement (Form N–1A) (Dec. 28, 2012); J.P. Morgan Money Market Funds, JPMorgan Prime Money Market Fund Institutional Class Shares (JINXX), Registration Statement (Form N–1A) (July 1, 2012); J.P. Morgan Money Market Funds, JPMorgan Prime Money Market Fund Morgan Class Shares (VMVXX), Registration Statement (Form N–1A) (July 1, 2012).

[203] Alternatively, funds might choose to be treated as institutional (and not eligible for the proposed retail exemption to the floating NAV requirement).

[204] *See* Comment Letter of BlackRock, Inc. (Dec. 13, 2012) (available in File No. FSOC–2012–0003) (''BlackRock FSOC Comment Letter'') (''A two-tiered approach to MMFs based on a distinction between ''retail'' and ''institutional'' funds would be difficult to implement and may lead to gaming behavior by investors.''); HSBC FSOC Comment Letter, *supra* note 196 (''There are also practical challenges such as defining and identifying different types of investors and preventing the ''gaming'' of any regulation.'').

[205] Commenters have suggested a number of ways to distinguish retail funds from institutional funds. *See, e.g.,* Comment Letter of Fidelity Investments, Comments on Response to Questions Posed by Commissioners Aguilar, Paredes, and Gallagher, (Jan. 24, 2013), *available at http://www.sec.gov/comments/mms-response/mms-response.shtml* (''Fidelity RSFI Comment Letter''); Schwab FSOC Comment Letter, *supra* note 171. All of these methods involve some degree of subjectivity and risk of over or under inclusion.

[206] We proposed but did not adopt a requirement that a money market fund's board determine at least once each calendar year whether the fund is an institutional fund based on the nature of the record owner of the fund's shares, minimum initial investment requirements, and cash flows from purchases and redemptions. *See* 2009 Proposing Release, *supra* note 31, at nn.195–197 and accompanying text.

[207] *See* 2010 Adopting Release, *supra* note 92, at nn.220–228 and accompanying text. Many commenters also expressed concern with requiring fund boards to make such a determination. *See* 2010 Adopting Release, *supra* note 92, at n.222 and accompanying text. *See also* section III.A.4.b of this Release.

[208] For example, one commenter suggested that we treat as institutional a fund that has any class that offers same-day liquidity to shareholders. Comment Letter of Fidelity Investments (Aug. 24, 2009) (available in File No. S7–11–09) (''Fidelity 2009 Comment Letter''). We expressed concern regarding this proposal and whether institutional investors would be willing to migrate to funds that offer next-day liquidity to avoid the more restrictive requirements. *See* 2010 Adopting Release, *supra* note 92. We expressed similar concerns about others' suggestion that retail funds be distinguished based on minimum initial account sizes or maximum expense ratios. *See, e.g.,* Comment Letter of HighMark Capital Management, Inc. (Sept. 8, 2009) (available in File No. S7–11–09); Comment Letter of T. Rowe Price Associates, Inc. (Sept. 8, 2009) (available in File No. S7–11–09) (''T. Rowe Price 2009 Comment Letter'').

[209] *See, e.g.,* Fidelity RSFI Comment Letter, *supra* note 205; Schwab FSOC Comment Letter, *supra* note 171.

[210] *See* proposed (FNAV) rule 2a–7(c)(3).

[211] The proposed retail exemption would provide exemptive relief from the Investment Company Act and its rules to permit a retail money market fund to restrict daily redemptions as provided for in the proposed rule. *See* proposed (FNAV) rule 2a–7(c)(3)(iii).

[212] *See* USAA FSOC Comment Letter, *supra* note 183 (''This approach would reduce large money movement from retail MMFs in any given day, and therefore retail MMFs would be less likely to experience large scale runs resulting from a lack of liquidity.'').

[213] *See id.* (noting that if the Commission were to define a fund as retail through a daily redemption limitation approach ''[l]arge individual investors and institutions will self-select into institutional MMFs because retail MMFs will not meet their operational needs.'').

large redemptions quickly, they would be able to choose to invest in a government money market fund, a floating NAV fund, or plan to make several redemptions over time.

Applying the daily redemption limitation method to omnibus accounts may pose difficulties. In order for the fund to impose its redemption limit policies on the underlying shareholders, intermediaries with omnibus accounts would need to provide some form of transparency regarding underlying shareholders, such as account sizes of underlying shareholders (showing that each was below the $1 million redemption limit). Alternatively, the fund could arrange with the intermediary to carry out the fund's policies and impose the redemption limitation, or else impose redemption limits on the omnibus account as a whole. We discuss omnibus account issues further below.

We have selected $1,000,000 as the appropriate daily redemption threshold because we expect that such a daily limit is high enough that it should continue to make money market funds a viable and desirable cash management tool for retail investors,[214] but is low enough that it should not suit the operational needs of institutions. We recognize that typical retail investors rarely make redemptions that approach $1,000,000 in a single day. Nonetheless, retail investors' net worth and investment choices can differ significantly, and they may on occasion engage in large transactions. For example, a retail investor may make large redemption requests when closing out their account, rebalancing their investment portfolio, paying their tax bills, or making a large purchase such as the down payment on a house. In selecting the appropriate redemption limit, we sought to find a threshold that is low enough that institutions would self-select out of retail funds, but high enough that it would not impose unnecessary burdens on retail investors, even when they engage in atypical redemptions. One commenter suggested a lower redemption threshold of $250,000,[215] but we are concerned that such a threshold may be too low to meet the cash management needs of retail investors that engage in occasional large transactions. We also considered a higher threshold, such as a $5,000,000 daily redemption limit instead, but are concerned that such a higher limit might not provide sufficient limitation on heightened redemptions in times of stress.

As mentioned previously, setting an appropriate redemption threshold for retail money market funds is complicated by the fact that retail investors may, however, on occasion need to redeem relatively large amounts from a money market fund, for example, in connection with the purchase of a home, and that some institutions may have small enough cash balances that they may find that a $1,000,000 daily redemption threshold still suits their operational needs. A retail fund's prospectus and advertising materials would need to provide information to shareholders about daily redemption limitations to shareholders.[216] This should provide sufficient information to potential investors, both retail and institutional, to allow them to make informed decisions about whether investing in the fund would be appropriate. Any money market fund that takes advantage of the retail exemption would also need to effectively describe that it is intended for retail investors. Retail investors who may need to make large (*i.e.,* in excess of $1,000,000) immediate redemptions would thus know that they should not invest in a retail money market fund with daily redemption limitations, and that they should instead use an alternate cash management tool. Alternatively, since it is likely that retail investors would have advance notice of the need to redeem in excess of the fund's limits, they could manage the redemption request over a period of several days.

We request comment on our proposed method of distinguishing between retail and institutional money market funds based on a daily redemption limitation of $1,000,000.

- Would a daily redemption limit effectively distinguish retail from institutional money market funds? Are we correct in assuming that institutional investors would self-select out of retail funds with such redemption limits? Would a daily redemption limit help reduce the risk that a fund might not be able to manage heavy shareholder redemptions in times of stress? Would this method of distinguishing between retail and institutional money market funds appropriately reflect the relative risks faced by these two types of funds?
- If we classify funds as retail or institutional based on an investor's permitted daily redemptions, should we limit a retail fund investor's daily redemptions to $1,000,000, or some other dollar amount such as $250,000 or $5,000,000? Should we provide a means to increase the dollar amount limit to keep pace with inflation? If so, what method should we use?
- How large are institutional investors' typical account balances and daily redemptions? Would institutional investors be willing to break large investments into smaller pieces so they can spread them across multiple retail funds?
- Are current disclosure requirements sufficient to inform current and potential shareholders of the operations and risks of redemption limitations? Should we consider additional disclosure requirements? If so, what kinds of disclosures should be required?
- We ask commenters to provide empirical justification for any comments on a redemption limitation approach to distinguishing retail and institutional money market funds. We also request that commenters with access to shareholder redemption data provide us with detailed information about the size of individual redemptions in normal market periods but especially in September 2008 and summer 2011.
- In particular, we request that commenters submit data on the size and frequency of retail and institutional redemptions in money market funds today, including breakdowns of the typical number and dollar volume of transactions in funds intended for retail and institutional shareholders. We also request empirical data on the size and frequency of retail investors outlier redemption activity, such as when closing out their accounts or making other atypical transactions.
- Should the exemption have a weekly redemption limit as an alternative to, or in addition to, the daily redemption limit? If so, what should that limit be?

We have discussed above why we believe a daily redemption limit may effectively distinguish between retail and institutional investors and may also serve to help a retail fund manage the redemption requests it receives. In some cases, retail investors may still want to

[214] The staff understands that for at least one large fund group, significantly less than 1% of the number of redemption transactions in money market funds intended for retail investors exceed $1,000,000, and that more than 97% of retail transactions were under $25,000. Nonetheless, the fund group received redemption request exceeding $250,000 from some retail investors on a daily basis.

[215] *See* USAA FSOC Comment Letter, *supra* note 183 (suggesting that a $250,000 cap on daily redemptions is a natural dollar limit because it is consistent with rule 18f–1 (exemption for mutual funds that allows funds to commit to pay certain redemptions in cash, rather than in-kind) and the current FDIC account guarantee limit).

[216] Prospectus disclosure regarding any restrictions on redemptions is currently required by Form N–1A, and we do not believe that any amendments to the current disclosure requirements would be necessary to require additional fund disclosure regarding the daily redemption restrictions of the proposed retail exemption. *See* Item 6 and Item 11(c)(1) of Form N–1A.

redeem more than $1 million in a single day. To help accommodate such requests, but at the same time allow a retail fund to effectively manage its redemptions, a retail exemption also could include a provision permitting an investor to redeem in excess of the fund's daily redemption limit, provided the investor gives advance notice of their intent to redeem in excess of the limit. Permitting higher redemptions with advance notice may serve the interests of retail investors, while also giving a fund manager sufficient time to prepare to meet the redemption request without adverse consequences to the fund. We request comment on whether we should include a provision allowing retail funds to permit redemption requests in excess of their daily limit if the investor provides advance notice.

• Should we include a provision permitting retail investors to redeem more than the daily redemption limit if they gave advance notice? How frequently are retail investors likely to need to redeem more than the daily redemption limit, and also know that they would need to make such a redemption in advance? Would such an advance notice provision encourage ''gaming behavior,'' for example if an institution invested in a retail fund and gave notice that every Friday it would redeem a large position to make payroll? Should we be concerned with such ''gaming behavior'' provided that the fund was given sufficient notice that it could effectively manage the redemptions?

• If we were to include an advance notice provision, what should the terms be? Should a retail investor be permitted to redeem any amount provided that they gave sufficient notice? A limited amount, such as $5 or $10 million? How much advance notice would be required, 2 days, 5 days, more or less? Should the amount that an investor be permitted to redeem be tied to the amount of advance notice given? For example, should an investor be permitted to redeem $3 million in a single day if they give 3 days' notice, but $10 million in a single day if they gave 10 days' notice?

• Should an advance notice provision include requirements regarding the method of how the notice is submitted to the fund, or for fund recordkeeping of the notices it receives? Should such a provision include requirements on intermediary communications, (for example, if the notice is provided to the intermediary rather than the fund, should we require that the advance notice clock begin counting once the fund receives the notice, not when it is given to the intermediary) or should it leave such details to be worked out between the parties?

• What operational costs would be associated with providing such an advance notice provision? Would funds be able to effectively communicate to investors the terms of such an advance notice provision?

We note that most money market funds that invest in municipal securities (tax-exempt funds) are intended for retail investors, because the tax advantages of those securities are only applicable to individual investors, and accordingly, a retail exemption would likely result in most such funds seeking to qualify for the proposed exemption. Our 2010 reforms exempted tax-exempt funds from the requirement to maintain 10% daily liquid assets because, at the time, we understood that the supply of tax-exempt securities with daily demand features was extremely limited.[217] Because tax-exempt money market funds are not required to maintain 10% daily liquid assets, these funds may be less liquid than other retail money market funds, which could raise concerns that tax-exempt retail funds might not be able to manage even the lower level of redemptions expected in a retail fund. Based on information received through Form N–MFP, we now understand that many tax-exempt funds can and do maintain more than 10% of their portfolio in daily liquid assets, and thus complying with a 10% daily liquid asset requirement may be feasible for these funds.[218] We request comment on whether we should require tax-exempt funds that wish to take advantage of the proposed retail exemption to also meet the 10% daily liquid asset requirements.

• Would tax-exempt funds that rely on the proposed retail exemption be able to manage redemptions in time of stress without such a daily liquid asset requirement? What level of daily liquid assets do tax-exempt money market funds typically maintain today? Should we require tax-exempt money market funds to meet the daily liquid asset requirement if they are to rely on the proposed retail exemption to the floating NAV?

There are different ways a money market fund could comply with the exemption's daily redemption limitation if a shareholder seeks to redeem more than $1 million on any given day notwithstanding the fund's policy not to honor such requests. The fund could treat the entire order as not in ''good order'' and reject the order in its entirety. Alternatively, the fund could treat the order as a request to redeem $1 million and reject the remainder of the order (or treat it as if it were received on the next business day). Any of those approaches would allow the money market fund to meet the daily redemption limitation and neither would provide an incentive for a shareholder to submit a redemption request in excess of $1 million on any one day. A fund would also need to disclose how it handles such excessive redemption requests in its prospectus.[219] We request comment on these approaches.

• Should we specify in rule 2a–7 the way that a money market fund must comply with the exemption's daily redemption limitation? Is either of the ways we discuss above easier or less costly to implement than the other?

• Are there any other approaches, other than the ones discussed above, that funds may use to meet the daily redemption limitation? If so, what are the benefits and costs of those alternatives?

ii. Omnibus Account Issues

Today, most money market funds do not have the ability to look through omnibus accounts to determine the characteristics and redemption patterns of their underlying investors. An omnibus account may consist of holdings of thousands of small investors in retirement plans or brokerage accounts, just one or a few institutional accounts, or a mix of the two. Omnibus accounts typically aggregate all the customer orders they receive each day, net purchases and redemptions, and they often present a single buy and single sell order to the fund. Because the omnibus account holder is the shareholder of record, to qualify as a retail fund under a direct application of our daily redemptions limitation proposal, a fund would be required to restrict daily redemptions by omnibus accounts to no more than $1,000,000. Because omnibus accounts can represent hundreds or thousands of beneficial owners and their transactions, they would often have daily activity that exceeds this limit. This combined activity would result in omnibus accounts often having daily redemptions that exceed the limit even though no one beneficial owner's

[217] *See* 2010 Adopting Release, *supra* note 92, at nn.240–243 and accompanying text; rule 2a–7(c)(5)(ii).

[218] Based on a review of Form N–MFP filings, we understand that as of the end of February 2013, 51% of tax-exempt funds maintain daily liquid assets in excess of 10%, and that another 29% maintain daily liquid assets of between 5% and 10% of their portfolios. The average daily liquid assets held across all tax-exempt funds was approximately 9.9% of their total portfolios.

[219] *See* Item 6 and Item 11(c)(1) of Form N–1A.

transaction exceeds the limit.[220] Accordingly, to implement a retail exemption, our proposal needs to also address retail investors that purchase money market shares through omnibus accounts.

To address this issue, the proposed retail exemption would also permit a fund to allow a shareholder of record to redeem more than $1,000,000 in a single day, provided that the shareholder of record is an ''omnibus account holder'' [221] that similarly restricts each beneficial owner in the omnibus account to no more than $1,000,000 in daily redemptions.[222] Under the proposed exemption, a fund would not be required to impose its redemption limits on an omnibus account holder, provided that the fund has policies and procedures reasonably designed to allow the conclusion that the omnibus account holder does not permit any beneficial owner from ''directly or indirectly'' redeeming more than $1,000,000 in a single day.[223]

The restriction on ''direct or indirect'' redemptions is designed to manage issues related to ''chains of intermediaries,'' such as when an investor purchases fund shares through one intermediary, for example, an introducing broker or retirement plan, which then purchases the fund shares through a second intermediary, such as a clearing broker.[224] The proposed exemption would require that a retail fund's policies and procedures be reasonably designed to allow the conclusion that the fund's redemption limit is applied to beneficial owners all the way down any chain of intermediaries. If a fund cannot reasonably conclude that such policies are enforced by intermediaries at each step of the chain, then the fund must apply its redemption limit at the aggregate omnibus account holder level (or rely on a cooperating intermediary to apply the fund's redemption limits to any uncooperative intermediaries further down the chain). Accordingly, to redeem more than $1,000,000 daily, a fund's policies and procedures must be designed to conclude that an omnibus account holder that is the shareholder of record with the fund reasonably concludes that all beneficial owners in the omnibus account, even if invested through another intermediary, comply with the redemption limit. If the fund cannot reasonably conclude that intermediaries that have omnibus accounts with it also do not permit beneficial owners to redeem more than $1,000,000 in a single day, the fund's policies must be reasonably designed to allow the conclusion that the omnibus account holder applies the fund's redemption limit to the other intermediaries' transactions on an aggregate level.[225]

We note that the challenges of managing implementation of fund policies through omnibus accounts are not unique to a retail exemption. For example, funds frequently rely on intermediaries to assess, collect, and remit redemption fees charged pursuant to rule 22c–2 on beneficial owners that invest through omnibus accounts. Funds and intermediaries face similar issues when managing compliance with other fund policies, such as account size limits, breakpoints, rights of accumulation, and contingent deferred sales charges.[226] Service providers also offer services designed to facilitate compliance and evaluation of intermediary activities.

The proposed rule would not require retail money market funds to enter into explicit agreements or contracts with omnibus account holders at any stage in the chain, but would instead allow funds to manage these relations in whatever way that best suits their circumstances. We would expect that in some cases, funds may enter into agreements with omnibus account holders to reasonably conclude that their policies are complied with. In other cases, funds may have sufficient transparency into the activity of omnibus account holders, or use other verification methods (such as certifications), that funds could reasonably conclude that their policies are being followed without an explicit agreement. If a fund could not verify or reasonably conclude that an omnibus account holder is applying the redemption limit to underlying beneficial owner transactions, we would expect that a fund would treat that omnibus account holder like any other shareholder of record, and impose the $1,000,000 daily redemption limit on that omnibus account. Retail money market funds will need to monitor compliance and implement policies and procedures to address the implications of potential exceptions, for example, if an intermediary improperly permitted a redemption in excess of the fund's limits. Finally, the rule would also prohibit a fund from allowing an omnibus account holder to redeem more than $1,000,000 for its own account in a single day.[227] This restriction is intended to prevent an omnibus account holder from exceeding the fund's redemption limits under the exemption when trading for its own account.

As proposed, the omnibus account holder provision does not provide for any different treatment of intermediaries based on their characteristics and instead applies the redemption limits equally to all beneficial owners. However, in some circumstances such treatment may not be consistent with the intent of the exemption. For example, an intermediary with investment discretion, such as a defined-contribution pension plan that allows the plan sponsor to remove a money market fund from its offerings, could unilaterally liquidate in one day a quantity of fund shares that greatly exceeds the fund's redemption limit, even if no one beneficial owner had an account balance that exceeds the limit. Intermediaries might also pose different risks, for example, the risks associated with a sweep account might be different than the risks posed by a retirement plan. Also, certain intermediaries may not be able to offer funds with redemption restrictions to investors, even if the underlying beneficial owners are retail investors. We understand that identical treatment of intermediaries under the proposal may not precisely reflect the risks of intermediaries with different characteristics, but recognize that this is a cost of our attempt to keep the retail exemption simple to implement.

A shareholder may own fund shares through multiple accounts, either directly with a fund, or through an intermediary. In some cases, such as when one account is held directly with

[220] *See, e.g.,* Invesco FSOC Comment Letter, *supra* note 192 (''These [omnibus] accounts, due to their size, might well be regarded as 'institutional' despite the fact that the aggregate of assets belong largely to investors who would be considered 'retail' if they invested in the MMF directly.'').

[221] Omnibus account holder would be defined in the proposed rule as ''a broker, dealer, bank, or other person that holds securities issued by the fund in nominee name.'' *See* proposed (FNAV) rule 2a–7(c)(3) (ii).

[222] *See* proposed (FNAV) rule 2a–7(c)(3) (ii).

[223] *See id.*

[224] For purposes of imposing redemption limitations on beneficial owners, we would expect that funds seek to ensure as part of their policies and procedures that an intermediary would make reasonable efforts consistent with applicable regulatory requirements to aggregate multiple accounts held with it that are owned by a single beneficial owner. We would not expect that a fund would seek to ensure that an intermediary reasonably be able to identify that a single beneficial owner owns fund shares through multiple accounts if the shareholder has an account with the intermediary, and also owns shares through another intermediary that does not already share account information with the first intermediary.

[225] *See* proposed (FNAV) rule 2a–7(c)(3)(ii).

[226] Under rule 38a–1, funds are required to have policies and procedures reasonably designed to prevent violation of the federal securities laws by the fund and certain service providers.

[227] *See* proposed (FNAV) rule 2a–7(c)(3)(ii).

a fund and another account is held through an intermediary, the fund would not be able to identify that the same shareholder has multiple accounts with the fund, and may not be able to effectively restrict that shareholder from redeeming fund shares from those accounts, that in aggregate, may exceed the proposed daily redemption limit. The proposed retail exemption would not restrict such redemptions, because the shareholder with multiple accounts would not be a ''shareholder of record'' for all of the accounts.[228] In other cases, a fund may be able to identify that a shareholder holds multiple accounts with the fund, such as if a shareholder owns fund shares in an account held directly with the fund, and also owns shares through an individual retirement account (''IRA'') held with the fund. In those cases, the shareholder with multiple accounts would be the shareholder of record for both accounts, and the fund should be able to identify the shareholder as such.[229] If a fund receives redemption orders exceeding the $1,000,000 limit from a shareholder of record through multiple accounts in a single day, the fund would need to aggregate the redemption requests from all accounts held by that shareholder of record, and impose the daily redemption limit on the shareholder of record's total redemptions, not just on an account-by-account basis.[230]

We request comment on the proposed treatment of omnibus account holders under the retail exemption to the floating NAV alternative.

- Does our proposed treatment of omnibus accounts under the retail exemption appropriately address the operation of such accounts? What types of policies and procedures would funds develop to confirm that omnibus account holders are able to reasonably prevent beneficial owners that invest through the account from violating a retail money market fund's redemption limit policies and procedures?
- The proposed rule does not require funds to enter into agreements with omnibus account holders, nor does it prescribe any other mechanism for requiring a fund to verify that its redemption limits are effectively enforced. Should we require such agreements? What difficulties would arise in implementing such agreements? Instead of agreements, should we consider prescribing some other type of verification or compliance procedure to prevent a fund's limit from being breached, such as certifications from omnibus account holders?
- Should the rule require a fund to obtain periodic certifications regarding the redemptions of beneficial owners in an omnibus account? If so, should we require a specific periodicity of certifications, such as every month, or every quarter?
- Should we differentiate between intermediaries that invest through omnibus accounts? For example, should we require that an intermediary that has investment discretion over a number of beneficial owners' accounts be treated as a single beneficial owner for purposes of the daily redemption limit? Should we treat certain intermediaries differently than others, perhaps allowing higher or unlimited redemptions for investors who invest through certain types of intermediaries such as retirement plans? What operational difficulties would arise if we were to provide for such differential treatment of intermediaries?
- Can funds accurately identify multiple accounts in a fund that are owned by a single shareholder of record? If not, what costs would be incurred in building such systems? How should the redemption limit apply to accounts that are owned by multiple investors? Should we be concerned about investors opening accounts through multiple intermediaries and multiple accounts in an attempt to circumvent the daily redemption limits?

As discussed above, we understand that today many money market funds are unable to determine the characteristics or redemption patterns of their shareholders that invest through omnibus accounts. This lack of transparency can not only hinder a fund from effectively applying a retail exemption but can also lead to difficulties in managing the liquidity levels of a fund's portfolio, if a fund cannot effectively anticipate when it is likely to receive significant shareholder redemptions through examination of its shareholder base. We request comment on whether we should consider requiring additional transparency into money market fund omnibus accounts to enable funds to understand better their respective shareholder base and relevant redemption patterns.

- Should we consider any other methods of generally providing more transparency into omnibus accounts for money market funds so that funds could better manage their portfolios in light of their respective shareholder base? If so, what methods should we consider?

c. Consideration of Other Distinguishing Methods

As discussed above, as part of the retail exemption that we are proposing today, we are proposing a method of distinguishing between retail and institutional money market funds based on daily redemption limits. This is not the only method by which we could attempt to distinguish types of funds. Below we discuss several alternate methods of making such a distinction, and request comment on whether we should adopt one of these methods instead.

i. Maximum Account Balance

A different method of distinguishing retail funds would be to define a retail fund as a fund that does not permit account balances of more than a certain size. For example, we could define a fund as retail if the fund does not permit investors to maintain accounts with a balance that exceeds $250,000, $1,000,000, $5,000,000, or some other amount.[231] If an investor's account balance were to exceed the threshold dollar amount, the fund could automatically direct additional investments to shares of a government money market fund or a fund subject to the floating NAV requirement.[232] Such an approach would require a retail fund to update the disclosure in its prospectus and advertising materials to inform investors how their investments would be handled in such circumstances. Much like the redemption limitation method, omnibus accounts may pose difficulties that would need to be addressed through certifications, transparency, or some other manner.[233] A maximum account balance approach may also create operational issues in other ways, such

[228] *See id.*. An intermediary would be the shareholder of record for the omnibus accounts they hold.

[229] We note that we do not expect funds to collapse such accounts, but rather match such accounts where there is reasonably available identifying information on hand at the fund or its transfer agent that the accounts have the same record owner.

[230] Similar issues may arise if a shareholder holds an account jointly with another person, such as a spouse. A fund's policies and procedures should establish methods of managing redemptions from joint accounts.

[231] A variation on this approach might prohibit further investment in a retail fund at the end of a calendar quarter if the average account size exceeds a threshold dollar amount during the quarter.

[232] If a fund were part of a fund group that does not include an affiliated institutional fund, the fund would not allow further investments from an investor whose account balance reaches (or, if the account receives dividends or otherwise increases in value, exceeds) the threshold amount.

[233] We also expect that there may be significant differences in costs depending on how such an exemption was structured, and that it could be significantly less costly to test whether an investor investing through an omnibus account has exceeded a maximum account balance periodically rather than on a trade-by-trade basis. *See also infra* section III.A.4.d for a discussion of operational costs of the retail exemption.

as managing what happens if a buy and hold investor's account exceeded the limits due to appreciation in value. Determining the proper maximum account balance that would effectively distinguish between retail and institutional investors may also prove difficult.

Defining a retail fund based on the maximum permitted account balance would be relatively simple to explain to investors through disclosure in the fund's prospectus and advertising materials. This approach could, however, disadvantage funds that do not have an affiliated government or institutional money market fund into which investors' ''spillover'' investments in excess of the maximum amount could be directed and could encourage ''gaming behavior,'' if institutional investors were to open multiple accounts through different intermediaries with balances under the maximum amount in order to evade any maximum investment limit we might set.[234]

We request comment on the approach of distinguishing between retail and institutional money market funds based on investors' account balances:

- If we were to classify funds as retail or institutional based on an investor's account balance, what maximum account size would appropriately distinguish a retail account from an institutional account: $250,000, $1,000,000, $5,000,000, or some other dollar amount? Would this method of distinguishing between retail and institutional money market funds appropriately reflect the relative risks faced by these two types of funds? How would funds or other parties, such as intermediaries and omnibus accountholders, be able to enforce account balance limitations?
- Would shareholders with institutional characteristics be likely to open multiple retail money market fund accounts under the maximum amount, for example by going through intermediaries, to circumvent the account size requirement, and if so, would retail funds be subject to greater risk during periods of stress? What disclosure would be necessary to inform current and potential shareholders of the operations and risks of account balance limitations?
- We ask commenters to provide empirical justification for any comments on an account balance approach to distinguishing retail and institutional money market funds. We also request information on composition and distribution of individual account sizes to assist the Commission in considering this approach.

ii. Shareholder Concentration

Another approach to distinguishing retail and institutional money market funds might be to base the distinction on the fund's shareholder concentration characteristics. Under this approach, a fund would be able to qualify for a retail exemption if the fund's largest shareholders owned less than a certain percentage of the fund. This type of ''concentration'' method of distinguishing funds would be a test for identifying funds whose shareholders are more concentrated, and thus have a limited number of shareholders whose redemption choices could affect the fund more significantly during periods of stress. A heavily concentrated fund may indicate that the fund has a smaller number of large shareholders, who are likely institutions. In addition, funds whose shareholders are less concentrated, and thereby that are less subject to heavy redemption pressure from a limited number of investors, may be able to withstand stress more effectively and thus could maintain a stable price.

Commenters have suggested several methods for defining the appropriate concentration level for a fund. One test for determining if a fund is institutional might be whether the top 20 shareholders own more than 15% of the fund's assets,[235] or the top 100 shareholders own more than 25% of fund assets, or some other similar measure. Another method to test concentration might be to define a fund as institutional if any shareholder owns more than 0.1% of the fund,[236] or 1% of the fund, or some other percentage.

Distinguishing between retail and institutional money market funds based on shareholder concentration could more accurately reflect the relative risks that funds face than distinguishing retail and institutional money market funds based on the maximum balance of shareholders' accounts, since an individual shareholder's account value does not necessarily reflect the risks of concentrated heavy redemptions. However it may be less accurate at distinguishing types of investors (and at reducing the risks of heavy redemptions associated with certain types of investors) than the redemption limitation discussed above, because the redemption limitation would likely cause investors to self-select into the appropriate fund.

One benefit of the concentration method of distinguishing retail funds is that it may lessen operational issues related to omnibus accounts. If funds were required to count an intermediary with omnibus accounts as one shareholder for concentration purposes (*e.g.,* like any other shareholder), there may be no need for transparency into omnibus accounts.[237] However, if we did not require such treatment of omnibus accounts, this concentration method would raise the same issues associated with managing omnibus accounts as the other methods discussed above.

This concentration method of distinguishing retail funds would also pose a number of difficulties in implementation and operation. For example, it may be over-inclusive and a fund may be wrongly classified as an institutional money market fund if many of its large shareholders of record are intermediaries or sweep accounts,[238] even though the underlying beneficial owners may be retail investors. The method may also create difficulties for funds that have limited assets or investors (for example, new funds with only a few investors), because those small and start-up funds may have a concentrated investor base even though their investors may be primarily retail.[239] Similarly, this method may not effectively distinguish retail and institutional money market funds if the fund is so large that even institutional accounts do not trigger the concentration limits. An institutional fund that is not heavily concentrated may be subject to the same risks as a more concentrated fund, because institutional investors tend to be more sensitive to changing market conditions.

Finally, this method could create significant operational issues for funds if shareholder concentration levels were to change temporarily, or to fluctuate periodically.[240] For example, if we were to provide a retail exemption that

[234] *See* BlackRock FSOC Comment Letter, *supra* note 204; Federated Investors Feb. 15 FSOC Comment Letter, *supra* note 192.

[235] *See* Fidelity RSFI Comment Letter, *supra* note 205. This commenter suggested that the test would apply regardless of whether underlying shareholders are individuals or institutions.

[236] *See* Schwab FSOC Comment Letter, *supra* note 171.

[237] *See supra* note 235.

[238] *See, e.g.,* Dreyfus FSOC Comment Letter, *supra* note 174 (noting that sweep accounts behaved more like retail accounts rather than institutional ones during the 2008 financial crisis).

[239] *See* Invesco FSOC Comment Letter, *supra* note 192 (''Proposals to designate as ''institutional'' any account holding more than a given percentage of a MMF would provide an unfair competitive advantage to larger funds, which could continue to classify larger investors as ''retail.'').

[240] *See* Schwab FSOC Comment Letter, *supra* note 171 (discussing issues related to temporary changes in ownership percentages that may cause violations of such a concentration test).

depended on a fund's top 20 investors not owning more than 15% of the fund, this would require a fund to constantly monitor the size of its investor base and reject investments that would push the fund over the concentration limit in real time. Constant monitoring and order rejection may be costly and difficult to implement, not only for the fund but also for the affected shareholders who may have their purchase orders rejected unexpectedly by the fund. Shareholders may also have issues understanding whether a fund is institutional or retail, and because concentration may frequently change, it may be difficult to provide clear guidelines regarding whether a shareholder could or could not invest in a fund.

We request comment on the approach of distinguishing between retail and institutional money market funds based on shareholder concentration:

- If we classify funds as retail or institutional based on shareholder concentration, what thresholds should we use? Would criteria such as whether the top 20 investors make up more than 15% of the fund, or some other threshold, effectively distinguish between types of funds? Would such a concentration test pose operational difficulties? How would funds enforce such limits? How should funds treat omnibus accounts if they were to use such a test?
- Would investors who are likely to redeem shares when market-based valuations fall below the stable price per share be willing and able to spread their investment across enough funds to avoid being too large in any one of them?
- Would shareholder concentration limits result in further consolidation in the industry, as funds seek to grow in order to accommodate large investors?
- We ask commenters to provide empirical justification for any comments on a shareholder concentration approach to distinguishing retail and institutional money market funds.

iii. Shareholder Characteristics

Money market funds could also look at certain characteristics of the investors, such as whether they use a social security number or a taxpayer identification number to register their accounts or whether they demand same-day settlement, to distinguish between retail and institutional money market funds. Such a characteristics test could be used either alone, or in combination with one of the other methods discussed above to distinguish retail funds. However, this approach also has significant drawbacks. While institutional money market funds primarily offer same-day settlement and retail money market funds primarily do not, this is not always the case.[241] Likewise, social security numbers do not necessarily correlate to an individual, and taxpayer identification numbers do not necessarily correlate to a business. For instance, many businesses are operated as pass-through entities for tax purposes. In addition, funds may not be aware of whether their investors have a SSN or a TIN if the investments are held through an omnibus account.

The Commission requests comment on shareholder characteristics that could effectively distinguish between types of investors, as well as other methods of distinguishing between retail and institutional money market funds.

- What types of shareholder characteristics would effectively distinguish between types of investors? Social security numbers and/or taxpayer identification numbers? Whether the fund provides same-day settlement? Some other characteristic(s)?
- Besides the approaches discussed above, are there other ways we could effectively distinguish retail from institutional money market funds? Should we combine any of these approaches? Should we adopt more than one of these methods of distinguishing retail funds, so that a fund could use the method that is lowest cost and best fits their investor base?
- We ask commenters to provide empirical justification for any comments on a shareholder characteristics approach to distinguishing retail and institutional money market funds.

d. Economic Effects of the Proposed Retail Exemption

In addition to the costs and benefits of a retail exemption discussed above, implementing any retail exemption to the floating NAV requirement may have effects on efficiency, competition, and capital formation. A retail exemption to the floating NAV requirement could make retail money market funds more attractive to investors than floating NAV funds without a retail exemption, assuming that retail investors prefer such funds. If so, we anticipate a retail exemption could reduce the impact we expect on the number of funds and assets under management, discussed in section III.E below. However, these positive effects on capital formation could be reversed to the extent that the costs funds incur in implementing a retail exemption are passed on to shareholders, or shareholders give up potentially higher yields. As discussed above, a retail exemption to the floating NAV requirement could involve operational costs, with the extent of those costs likely being higher for funds sold primarily through intermediaries than for funds sold directly to investors. These operational costs, depending on their magnitude, might affect capital formation and also competition (depending on the different ability of funds to absorb these costs).

A retail exemption to the floating NAV requirement could have negative effects on competition by benefitting fund groups with large percentages of retail investors, especially where those retail investors invest directly in the funds rather than through intermediaries, relative to other funds.[242] A retail exemption could have a negative effect on competition to the extent that it favors fund groups that already offer separate retail and institutional money market funds and thus might not need to reorganize an existing money market fund into two separate funds to implement the exemption. On the other hand, as discussed above, we believe that the majority of money market funds currently are owned by both retail and institutional investors (although many funds are separated into retail and institutional classes), and therefore relatively few funds would benefit from this competitive advantage. Fund groups that can offer multiple retail funds will have a competitive advantage over those that cannot if investors with large liquidity needs are willing to spread their investments across multiple retail funds to avoid the redemption threshold.

[241] Some institutional money market funds do not offer same-day settlement. *See, e.g.,* Money Market Obligations Trust, Federated New York Municipal Cash Trust (FNTXX), Registration Statement (Form N–1A) (Feb. 28, 2013) (stating that redemption proceeds normally are wired or mailed within one business day after receiving a request in proper form). Some retail money market funds do offer same-day settlement. *See, e.g.,* Dreyfus 100% U.S. Treasury Money Market Fund (DUSXX), Registration Statement (Form N–1A) (May 1, 2012) (stating that if a redemption request is received in proper form by 3:00 p.m., Eastern time, the proceeds of the redemption, if transfer by wire is requested, ordinarily will be transmitted on the same day).

[242] Fund groups with large percentages of retail investors, and in particular, direct investors, may be better positioned to satisfy growing demand if we were to adopt the proposed retail exemption to our floating NAV proposal. *See* Invesco FSOC Comment Letter, *supra* note 192 (''Imposing a distinction between 'retail' versus 'institutional' funds would therefore unduly favor those MMF complexes with a preponderance of direct individual investors or affiliated omnibus account platforms over those with a more diverse investor basis and those with using unaffiliated intermediaries.'').

A retail exemption may promote efficiency by tying the floating NAV requirement to the shareholders that are most likely to redeem from a fund in response to deviations between its stable share price and market-based NAV per share. However, to the extent that a retail exemption fails to distinguish effectively institutional from retail shareholders, it may have negative effects on efficiency by permitting ''gaming behavior'' by shareholders with institutional characteristics who nonetheless invest in retail funds. It may also negatively affect fund efficiency to the extent that, to take advantage of a retail exemption, a fund that currently separates institutional and retail investors through different classes instead would need to create separate and distinct funds, which may be less efficient. The costs of such a re-organization are discussed in this Release below.

We request comment on the effects of a retail exemption to the floating NAV proposed on efficiency, competition, and capital formation.

- Would implementing a retail exemption have an effect on efficiency, competition, or capital formation? Which methods of distinguishing retail and institutional investors discussed above, if any, would result in the most positive effects on efficiency, competition, and capital formation?
- Would the floating NAV proposal have less of a negative impact on capital formation with a retail exemption than without? Would it provide competitive advantages to fund groups that have large percentages of retail investors, especially where those retail investors invest directly in the funds rather than through intermediaries, relative to other funds that have lower percentages of retail investors?
- Would a retail exemption better promote efficiency by tying the floating NAV requirement to institutional shareholders instead of retail shareholders? Why or why not?

The qualitative costs and benefits of any retail exemption to the floating NAV proposal are discussed above. Because we do not know how attractive such funds would be to retail investors, we cannot quantify these qualitative benefits or costs. However, we can quantify the operational costs that money market funds, intermediaries, and money market fund service providers might incur in implementing and administering the retail exemption to the floating NAV requirement that we are proposing today.[243]

Although we do not have the information necessary to provide a point estimate[244] of the potential costs associated with a retail exemption, our staff has estimated the ranges of hours and costs that may be required to perform activities typically involved in making systems modifications, implementing fund policies and procedures, and performing related activities. These estimates include one-time and ongoing costs to establish separate funds if necessary, modify systems and related procedures and controls, update disclosure in a fund's prospectus and advertising materials to reflect any investment or redemption restrictions associated with the retail exemption, as well as ongoing operational costs. All estimates are based on the staff's experience and discussions with industry representatives. We first discuss the different categories of operational costs that might be incurred in implementing a retail exemption, and then we provide a total cost estimate that captures all of the categories of costs discussed below. We expect that only funds that determine that the benefits of taking advantage of the proposed retail exemption would be justified by the costs would take advantage of it and bear these costs. Otherwise, they would incur the costs of implementing a floating NAV generally.

Many money market funds are currently owned by both retail and institutional investors, although they are often separated into retail and institutional share classes. A fund relying on the proposed retail exemption would need to be structured to accept only retail investors as determined by the daily redemption limit, and thus any money market fund that currently has both retail and institutional shareholders would need to be reorganized into separate retail and institutional money market funds. One-time costs associated with this reorganization would include costs incurred by the fund's counsel to draft appropriate organizational documents and costs incurred by the fund's board of directors to approve such documents. One-time costs also would include the costs to update the fund's registration statement and any relevant contracts or agreements to reflect the reorganization, as well as costs to update prospectuses and to inform shareholders of the reorganization. Funds and intermediaries may also incur one-time costs in training staff to understand the operation of the fund and effectively implement the redemption restrictions.

The daily redemption limitation method of distinguishing retail and institutional investors that we are proposing today would also require funds to have policies and procedures reasonably designed to allow the conclusion that omnibus account holders apply the fund's redemption limits to beneficial owners invested through the omnibus accounts. Adopting such policies and procedures and building systems to implement them would also involve one-time costs for funds and intermediaries. Funds could either conclude that their policies are enforced by obtaining information regarding underlying investors in omnibus accounts (transparency), or use some other sort of method to reasonably verify that omnibus account holders are implementing the fund's redemption policies, such as entering into an agreement or getting certifications from the omnibus account holder. In preparing the following cost estimates, the staff assumed that funds would generally rely on financial intermediaries to implement redemption policies without undergoing the costs of entering into an agreement, because funds and intermediaries would typically take the approach that is the least expensive. However, some funds may undertake the costs of obtaining an explicit agreement despite the expense. Our staff estimates that the one-time costs necessary to implement the retail exemption to the floating NAV proposal, including the various organizational, operational, training, and other costs discussed above, would range from $1,000,000 to $1,500,000 for each fund that chooses to take advantage of the retail exemption.[245]

[243] The costs estimated in this section would be spread amongst money market funds, intermediaries, and money market fund service providers (*e.g.,* transfer agents). For ease of reference, we refer only to money market funds and intermediaries in our discussion of these costs. As with other costs we estimate in this Release, our staff has estimated the costs that a single affected entity would incur. We anticipate, however, that many money market funds and intermediaries may not bear the estimated costs on an individual basis. The costs of systems modifications, for example, likely would be allocated among the multiple users of the systems, such as money market fund members of a fund group, money market funds that use the same transfer agent, and intermediaries that use systems purchased from the same third party. Accordingly, we expect that the cost for many individual entities may be less than the estimated costs.

[244] We are using the term ''point estimate'' to indicate a specific single estimate as opposed to a range of estimates.

[245] Staff estimates that these costs would be attributable to the following activities: (i) Planning, coding, testing, and installing system modifications; (ii) drafting, integrating, and implementing related procedures and controls; and (iii) preparing training materials and administering training sessions for staff in affected areas. Our staff's estimates of these operational and related costs, and those discussed

Continued

Funds that choose to take advantage of the retail exemption would also incur ongoing costs. These ongoing costs would include the costs of operating two separate funds (retail and institutional) instead of separate classes of a single fund, such as additional transfer agent, accounting, and other similar costs. Funds and intermediaries would also incur ongoing costs related to enforcing the daily redemption limitation on an ongoing basis and monitoring to conclude that the limits are being effectively enforced. Other ongoing costs may include systems maintenance, periodic review and updates of policies and procedures, and additional staff training. Accordingly, our staff estimates that money market funds and intermediaries administering a retail exemption likely would incur ongoing costs of 20%–30% of the one-time costs, or between $200,000 and $450,000 per year.[246]

- Are the staff's cost estimates too high or too low, and, if so, by what amount and why? Are there operational or other costs associated with segregating retail investors other than those discussed above?
- Do commenters believe that the proposed retail exemption would involve expenses beyond those estimated? To what extent would the costs vary depending on how a retail exemption is structured? Which of the staff's assumptions would most significantly affect the costs? Has our staff identified the assumptions that most significantly influence the cost of a retail exemption?
- What kinds of ongoing activities would be required to administer the proposed retail exemption to the floating NAV requirement, and to what extent? Would it be less costly for some funds (*e.g.,* those that are directly sold to investors) to make use of a retail investor exemption? If so, how much would those funds save?

5. Effect on Other Money Market Fund Exemptions

a. Affiliate Purchases

Rule 17a–9 provides an exemption from section 17(a) of the Act to permit affiliated persons of a money market fund to purchase portfolio securities from the fund under certain circumstances, and it is designed to provide a means for an affiliated person to provide liquidity to the fund and prevent it from breaking the buck.[247] Under our floating NAV proposal, however, money market funds' share prices would ''float,'' and funds thus could not ''break the buck.'' Notwithstanding the inability of funds to ''break the buck'' under our floating NAV proposal, for the reasons discussed below, we propose to retain rule 17a–9 with the amendments, discussed below, for all money market funds (including government and retail money market funds that would be exempt from our floating NAV proposal).

Funds with a floating NAV would still be required to adhere to rule 2a–7's risk-limiting conditions to reduce the likelihood that portfolio securities experience losses from credit events and interest rate changes. Even with a floating NAV and limited risk, as specified by the provisions of rule 2a–7, money market funds face potential liquidity, credit and reputational issues in times of fund and market stress and the resultant incentives for shareholders to redeem shares.

In normal market conditions, that shareholders may request immediate redemptions from a fund with a portfolio that does not hold securities that mature in the same time frame generally is no cause for concern because funds typically can sell portfolio securities to satisfy shareholder redemptions without negatively affecting prices. In times of crisis when the secondary markets for portfolio assets become illiquid, funds might be unable to sell sufficient assets without causing large price movements that affect not only the non-redeeming shareholders but also investors in other funds that hold similar assets. Therefore, to provide fund sponsors with flexibility to protect shareholder interests, we are proposing to allow fund sponsors to continue to support money market fund operations through, for example, affiliate purchases (in reliance on rule 17a–9), provided such support is thoroughly and consistently disclosed.[248]

As exists today, money market fund sponsors that have a greater capacity to support their funds may have a competitive advantage over other fund sponsors that do not. The value of this competitive advantage depends on the extent to which fund sponsors choose to support their funds and may be reduced by the proposed enhanced disclosure requirements discussed in this Release which may disincentivize fund sponsors from supporting their funds. The value of potential sponsor support also will depend on whether investors view support as good news (because, for example, the sponsor stands behind the fund) or bad news (because, for

throughout this Release, are based on, among other things, staff experience implementing, or overseeing the implementation of, systems modifications and related work at mutual fund complexes, and included analyses of wage information from SIFMA's Management & Professional Earnings in the Securities Industry 2012, *see infra* note 996, for the various types of professionals staff estimates would be involved in performing the activities associated with our proposals. The actual costs associated with each of these activities would depend on a number of factors, including variations in the functionality, sophistication, and level of automation of existing systems and related procedures and controls, and the complexity of the operating environment in which these systems operate. Our staff's estimates generally are based on the use of internal resources because we believe that a money market fund (or other affected entity) would engage third-party service providers only if the external costs were comparable, or less than, the estimated internal costs. The total operational costs discussed here include the costs that are ''collections of information'' that are discussed in section IV of this Release.

[246] We recognize that adding new capabilities or capacity to a system (including modifications to related procedures and controls and related training) will entail ongoing annual maintenance costs and understand that those costs generally are estimated as a percentage of the initial costs of building or modifying a system.

[247] Absent a Commission exemption, section 17(a)(2) of the Act prohibits any affiliated person or promoter of or principal underwriter for a fund (or any affiliated person of such a person), acting as principal, from knowingly purchasing securities from the fund. For convenience, in this Release, we refer to all of the persons who would otherwise be prohibited by section 17(a)(2) from purchasing securities of a money market fund as ''affiliated persons.'' ''Affiliated person'' is defined in section 2(a)(3) of the Act.

Rule 17a–9, as adopted in 1996, provides an exemption from section 17(a) of the Act to permit affiliated persons of a money market fund to purchase a security from a money market fund that is no longer an eligible security (as defined in rule 2a–7), provided that the purchase price is (i) paid in cash; and (ii) equals the greater of amortized cost of the security or its market price (in each case including accrued interest). *See* Revisions to Rules Regulating Money Market Funds, Investment Company Act Release No. 21837 (Mar. 21, 1996) [61 FR 13956 (Mar.28, 1996)] (the ''1996 Adopting Release''). As part of the 2010 money market fund reforms (discussed in *supra* section II.D.1), we expanded the exemptive relief in rule 17a–9 to permit affiliates to purchase from a money market fund (i) a portfolio security that has defaulted, but that continues to be an eligible security (subject to the purchase conditions described); and (ii) any other portfolio security (subject to the purchase conditions described above), for any reason, provided the affiliated person remits to the fund any profit it realizes from the later sale of the security (''clawback provision''). *See* rule 17a–9(a), (b).

[248] Commenters have noted the importance of sponsor support under rule 17a–9 as a tool that funds can use as a support mechanism. *See, e.g.,* Comment Letter of U.S. Chamber of Commerce (Jan. 23, 2013) (available in File No. FSOC–2012–0003) (''U.S. Chamber Jan. 23, 2013 FSOC Comment Letter''), Federated Investors Alternative 1 FSOC Comment Letter, *supra* note 161. We are proposing amendments to require that money market funds disclose the circumstances under which a fund sponsor may offer any form of support to the fund (*e.g.,* capital contributions, capital support agreements, letters of indemnity), any limits on such support, past instances of support provided to the fund, and public notification to the Commission regarding current instances of support provided. *See infra* section III.F for a more detailed discussion.

example, the sponsor does not adequately monitor the portfolio manager). The decision to leave rule 17a–9 in place should not, in our opinion, impose any additional costs on money market funds, their shareholders, or others, or change the effects on efficiency or capital formation. We recognize, however, that permitting sponsor support (through rule 17a–9 transactions) may allow money market fund sponsors to prevent their fund from deviating from its stable share price, potentially undercutting our goal to increase the transparency of money market fund risks.

We request comment on retaining the rule 17a–9 exemption.

• Do commenters believe affiliated person support is important to funds, investors, or the securities markets even under our floating NAV proposal? Do commenters agree with our assumptions that liquidity concerns are likely to remain significant even with a floating NAV and that fund sponsors should continue to have this flexibility to protect shareholder interests? We note that rule 17a–9 was established and then expanded in 2010, in the context of stable values. If money market funds are required to float their NAVs, should we limit further the circumstances under which fund sponsors or advisers can use rule 17a–9? If so, how?

• Does permitting affiliated purchases for floating NAV money market funds reduce the transparency of fund risks that our floating NAV proposal is designed, in part, to achieve? If so, does the additional disclosure we are proposing mitigate such an effect? Are there additional ways we can mitigate such an effect?

• Should we allow only certain types of support or should we prohibit certain types of support? For example, should we allow sponsors to purchase under rule 17a–9 only liquidity-impaired assets, or should we prohibit sponsors from purchasing defaulted securities? Why or why not? If yes, what types of support should be permitted and what types should be prohibited? Why?

• Would the ability of fund sponsors to support the NAV of floating funds affect the way in which money market funds are structured and marketed? If so, how? Would it affect the competitive position of fund sponsors that are more or less likely to have available capital to support their funds?

• Do commenters agree that our proposed amendment would not impose additional costs on funds or shareholders or impact efficiency or capital formation?

• Instead of retaining 17a–9, should we instead repeal the rule and thereby prohibit certain types of sponsor support of money market funds? If so, why?

b. Suspension of Redemptions

Rule 22e–3 exempts money market funds from section 22(e) of the Act to permit them to suspend redemptions and postpone payment of redemption proceeds to facilitate an orderly liquidation of the fund.[249] Rule 22e–3 replaced temporary rule 22e–3T.[250] Rule 22e–3 is designed to allow funds to suspend redemptions before actually breaking the buck, reduce the vulnerability of investors to the harmful effects of heavy redemptions on funds, and minimize the potential for disruption to the securities markets.[251] Rule 22e–3 currently requires that a fund's board of directors, including a majority of disinterested directors, determine that the deviation between the fund's amortized cost price per share and the market-based net asset value per share may result in material dilution or other unfair results before it suspends redemptions.[252] We recognize that, under our floating NAV proposal, money market funds (including those exempt from the floating NAV requirement) generally would no longer be able to use amortized cost valuation for their portfolio holdings.[253] Instead, government and retail money market funds would use the penny rounding method of pricing to maintain a stable share price and other money market funds would have a floating NAV per share. Accordingly, for all money market funds, the current threshold under rule 22e–3 for suspending redemptions would need modification to conform to the new regulatory regime.

As discussed above, we recognize that our floating NAV proposal, in conjunction with our other proposals, may not be sufficient to eliminate the incentive for shareholders to redeem shares in times of fund and market stress. As such, floating NAV money market funds may still face liquidity issues that could force them to want to suspend redemptions and liquidate. Commenters have noted the benefits of rule 22e–3, including that the rule prevents a lengthy and disorderly liquidation process, like that experienced by the Reserve Primary Fund.[254] Therefore, despite a floating NAV fund's inability to break a buck, we believe the benefits of rule 22e–3 should be preserved. Accordingly, under our proposed amendment, all floating NAV money market funds would be permitted to suspend redemptions, when, among other requirements, the fund, at the end of a business day, has less than 15% of its total assets in weekly liquid assets.[255] As discussed below in our discussion of the liquidity fees and gates alternative proposal, we believe that when a fund's weekly liquid assets are at least 50% below the minimum required weekly liquidity (*i.e.,* weekly liquid assets have fallen from 30% to 15%), the fund is under sufficient stress to warrant that the fund's board be permitted to suspend redemptions in light of a decision to liquidate the fund (and therefore facilitate an orderly liquidation).

Government money market funds and retail money market funds, which would be exempt from the floating NAV requirement, would be able to suspend redemptions and liquidate if either (1) the fund, at the end of a business day, has less than 15% of its total assets in weekly liquid assets or (2) the fund's price per share as computed for purposes of distribution, redemption, and repurchase is no longer equal to its stable share price or the fund's board (including a majority of disinterested directors) determines that such a change is likely to occur.[256] This would allow those funds to suspend redemptions and liquidate if the fund came under liquidity stress or if the fund was about to ''break the buck.''

Because money market funds already comply with rule 22e–3, we do not believe that retaining the rule in the

[249] Rule 22e–3(a)(1).

[250] Rule 22e–3 was first adopted as an interim final temporary final shortly after the Temporary Guarantee Program was established. *See* Temporary Exemption for Liquidation of Certain Money Market Funds, Investment Company Act Release No. 28487 (Nov. 20, 2008) [73 FR 71919 (Nov. 26, 2008)] (establishing rule 22e–3T to facilitate compliance for those money market funds that elected to participate in the Temporary Guarantee Program and were therefore required to promptly suspend redemptions if the fund broke the buck). The temporary rule expired on expired October 18, 2009. *Id. See also infra* section II.C (discussing the Temporary Guarantee Program).

[251] *See* 2010 Adopting Release, *supra* note 92, at section II.H (noting that the rule is designed only to facilitate the permanent termination of the fund in an orderly manner). *See also* rule 22e–3(a)(2) (requiring the fund's board to irrevocably approve the fund's liquidation).

[252] Rule 22e–3(a)(1).

[253] As discussed above, money market funds would continue to be permitted to use amortized cost to value portfolio securities with a remaining maturity of 60 days or less.

[254] *See, e.g.,* ICI Jan. 24 FSOC Comment Letter, *supra* note 25; Comment Letter of Federated Investors, Inc. (Re: Alternative 2) (Jan. 25. 2013) (available in File No. FSOC–2012–0003) (''Federated Alternative 2 FSOC Comment Letter'').

[255] *See* proposed (FNAV) rule 22e–3(a) (requiring that the fund's board, including a majority of directors who are not interested persons of the fund, irrevocably has approved the liquidation of the fund).

[256] *See id.*

context of our floating NAV proposal would impose any additional costs on money market funds, their shareholders, or others, nor have any effects on competition, efficiency, or capital formation.[257]

We request comment on this proposed amendment.

- Do commenters believe that the ability to suspend redemptions (under the circumstances we propose) would be important to floating NAV funds, their investors, and the securities markets?
- Would this ability be important to a retail or government money market fund even though we are proposing to exempt these funds from the floating NAV requirement, in part, because they are less likely to face heavy redemptions in times of stress?
- Is it appropriate to allow a money market fund to suspend redemptions and liquidate if its level of weekly liquid assets falls below 15% of its total assets? Is there a different threshold based on daily or weekly assets that would better protect money market fund shareholders? What is that threshold, and why is it better? Is there a threshold based on different factors that would better protect money market fund shareholders? What are those factors, and why are they better? If so, is such suspension then appropriate only in connection with liquidation, or should it be broader?
- Is our conclusion correct that it will impose no costs nor have any effects on competition, efficiency, or capital formation?

6. Tax and Accounting Implications of Floating NAV Money Market Funds

a. Tax Implications

Money market funds' ability to maintain a stable value per share simplifies tax compliance for their shareholders. Today, purchases and sales of money market fund shares at a stable $1.00 share price generate no gains or losses, and money market fund shareholders therefore generally need not track the timing and price of purchase and sale transactions for capital gains or losses.

i. Realized Gains and Losses

If we were to require some money market funds to use floating NAVs, taxable investors in those money market funds, like taxable investors in other types of mutual funds, would experience gains and losses. Shareholders in floating NAV money market funds, therefore, could owe tax on any gains on sales of their money market fund shares, could have tax benefits from any losses, and would have to determine those amounts.[258] Because it is not possible to predict the timing of shareholders' future transactions and the amount of NAV fluctuations, we are not able to estimate the amount of any increase or decrease in shareholders' tax burdens. But, given the relatively small fluctuations in value that we anticipate would occur in floating NAV money market funds and our proposed exemption of certain funds from the floating NAV requirement, any changes in tax burdens likely would be minimal.

Commenters also have asserted that taxable investors in floating NAV money market funds, like taxable investors in other types of mutual funds, would be required to track the timing and price of purchase and sale transactions to determine the amounts of gains and losses realized.[259] For mutual funds other than stable-value money market funds, tax rules now generally require the funds or intermediaries to report to the IRS and the shareholders certain information about sales of shares, including sale dates and gross proceeds.[260] If the shares sold were acquired after January 1, 2012, the fund or intermediary must also report cost basis and whether any gain or loss is long or short term.[261] These new basis reporting requirements and the pre-2012 reporting requirements are collectively referred to as ''information reporting.'' Mutual funds and intermediaries, however, are not currently required to make reports to certain shareholders (including most institutional investors). The regulations call these shareholders ''exempt recipients.''[262]

We understand, based on discussions by our staff with staff at the Treasury Department and the IRS, that, by operation of the current tax regulations, if our floating NAV proposal is adopted, money market funds that float their NAV per share would no longer be excluded from the information reporting requirements currently applicable to mutual funds and intermediaries.[263] Because retail money market funds would not be required to use floating NAVs, the vast majority of floating NAV money market fund shareholders are expected to be exempt recipients (with respect to which information reporting is not required). Such exempt recipients would thus be required to track gains and losses, similar to the current treatment of exempt recipient holders of other mutual fund shares. If there are any money market fund shareholders for which information reporting is made, those shareholders would be able to make use of such reports in determining and reporting their tax liability. We also understand that the Treasury Department and the IRS are considering alternatives for modifying forms and guidance (1) to include net information reporting by the funds of realized gains and losses for sales of all mutual fund shares; and (2) to allow summary income tax reporting by shareholders.[264]

We anticipate that these modifications, if effected, could reduce burdens and costs to shareholders when reporting annual realized gains or losses from transactions in a floating NAV money market fund. We recognize that if these modifications are not made, the tax reporting effects of a floating NAV could be quite burdensome for money market fund investors that typically engage in frequent transactions. Regardless of the applicability of net information reporting or of summary income tax reporting, however, all shareholders of floating NAV money market funds would be required to recognize and report taxable gains and losses with respect to redemptions of fund shares, which does not occur today

[257] The Commission considered rule 22e–3's costs, benefits, and effects on competition, efficiency, and capital formation, which this amendment would preserve, when it adopted the rule. *See* 2010 Adopting Release, *supra* note 92, at sections II.H, V, and VI.

[258] In its proposed recommendation, the FSOC recognized the potential increased tax-compliance burdens associated with a floating NAV for both money market funds and shareholders. FSOC Proposed Recommendations, *supra* note 114, at 33–34.

[259] *See, e.g.,* Comment Letter of Investment Company Institute (Feb. 16, 2012) (available in File No. 4–619) (''ICI Feb. 2012 PWG Comment Letter'') (enclosing a submission by the Investment Company Institute Working Group on Money Market Fund Reform Standing Committee on Investment Management International Organization of Securities Commissions) (''To be sure, investors already face these burdens [tracking purchases and sales for tax purposes] in connection with investments in long-term mutual funds. But most investors make fewer purchases and sales from long-term mutual funds because they are used for long-term saving, not cash management.'').

[260] Regulations exclude sales of stable-value money market funds from this reporting obligation. *See* 26 CFR 1.6045–1(c)(3)(vi).

[261] The new reporting requirements (often referred to as ''basis reporting'') were instituted by section 403 of the Energy Improvement and Extension Act of 2008 (Division B of Pub. L. 110–343) (codified at 26 U.S.C. 6045(g), 6045A, and 6045B); *see also* 26 CFR 1.6045–1; Internal Revenue Service Form 1099–B.

[262] *See* 26 CFR 1.6045–1(c)(3).

[263] *See supra* note 260.

[264] For 2012, the IRS allowed certain taxpayers to include summary totals in their Federal income tax returns, adding ''Available upon request'' where transaction details might otherwise have been required. *See* 2012 Instructions for Form 8949—Sales and Other Dispositions of Capital Assets, p. 3, col. 1, ''Exception 2,'' *available at http://www.irs.gov/pub/irs-pdf/i8949.pdf.*

with respect to shares of stable-value money market funds.[265]

We request comment on the burdens of tax compliance for money market fund shareholders (the impact on funds is discussed in the operational costs section below).

• If any shareholders of a floating NAV money market fund are not exempt recipients (and thus receive the information reporting that other non-exempt-recipient shareholders of other mutual funds currently receive), how difficult would it be for those shareholders to use that information to determine and report taxable gains and losses? Would it be any more difficult for floating NAV money market fund shareholders than other mutual fund shareholders? What kinds of costs, by type and amount, would be involved?

• In the case of floating NAV fund shareholders that are exempt recipients (which are not required recipients of information reporting), what types and amounts of costs would those shareholders incur to track their share purchases and sales and report any taxable gains or losses?

• As discussed above, mutual funds and intermediaries are not required to provide information reporting for exempt recipients, including virtually all institutional investors. Do mutual funds and intermediaries provide this information to shareholders even if tax law does not require them to do so? If not, would money market funds and intermediaries be able to use their existing systems and processes to access this information if investors request it as a result of our floating NAV proposal? Would doing so involve systems modifications or other costs in addition to those we estimate in section III.A.7, below? Would institutions or other exempt recipients find it useful or more efficient to receive this information from funds rather than to develop it themselves?

• Would exempt-recipient investors continue to invest in floating NAV funds if there continues to be no information reporting with respect to them?

• Would exempt-recipient investors invest in floating NAV money market funds if there is no administrative relief related to summary reporting of capital gains and losses, as discussed above? What would be the effect on the utility of floating NAV money market funds if the anticipated administrative relief is not provided? Would investors be able to use floating NAV money market funds in the same way or for the same purposes absent the anticipated administrative relief?

ii. Wash Sales

In addition to the tax obligations that may arise through daily fluctuations in purchase and redemption prices of floating NAV money market funds (discussed above), special ''wash sale'' rules apply when shareholders sell securities at a loss and, within 30 days before or after the sale, buy substantially identical securities.[266] Generally, if a shareholder incurs a loss from a wash sale, the loss cannot be deducted, and instead must be added to the basis of the new, substantially identical securities, which effectively postpones the loss deduction until the shareholder recognizes gain or loss on the new securities.[267] Because many money market fund investors automatically reinvest their dividends (which are often paid monthly), virtually all redemptions by these investors would be within 30 days of a dividend reinvestment (*i.e.,* purchase). Under the wash sale rules, the losses realized in those redemptions would be disallowed in whole or in part until an investor disposed of the replacement shares (or longer, if that disposition is also a wash sale). We understand that the Treasury Department and IRS are actively considering administrative relief under which redemptions of floating NAV money market fund shares that generate losses below a *de minimis* threshold would not be subject to the wash sale rules. We recognize, however, that money market funds would still incur operational costs to establish systems with the capability of identifying wash sale transactions, assessing whether they meet the *de minimis* criterion, and adjusting shareholder basis as needed when they do not.[268]

We request comment on the tax implications related to our floating NAV proposal.

• Would investors continue to invest in floating NAV money market funds absent administrative relief from the Treasury Department and IRS relating to wash sales? What would be the effect on the utility of floating NAV money market funds if the anticipated administrative relief is not provided? Would investors be able to use floating NAV money market funds in the same way or for the same purposes absent the anticipated administrative relief?

b. Accounting Implications

If we were to adopt our floating NAV proposal, some money market fund shareholders may question whether they would be able to treat their fund shares as ''cash equivalents'' on their balance sheets. We understand that classifying money market fund investments as cash equivalents is important because, among other things, investors may have debt covenants that mandate certain levels of cash and cash equivalents.[269]

Current U.S. GAAP defines cash equivalents as ''short-term, highly liquid investments that are readily convertible to known amounts of cash and that are so near their maturity that they present insignificant risk of changes in value because of changes in interest rates.'' [270] In addition, U.S. GAAP includes an investment in a money market fund as an example of a cash equivalent.[271] Notwithstanding, some shareholders may be concerned given this guidance came before money market funds using floating NAVs.[272]

Except as noted below, the Commission believes that an investment in a money market fund with a floating NAV would meet the definition of a ''cash equivalent.'' We believe the adoption of floating NAV alone would not preclude shareholders from classifying their investments in money market funds as cash equivalents because fluctuations in the amount of cash received upon redemption would likely be insignificant and would be consistent with the concept of a 'known' amount of cash. The RSFI Study supports our belief by noting that floating NAV money market funds are not likely to experience significant fluctuations in value.[273] The floating NAV requirement is also not expected to change the risk profile of money market fund portfolio investments. Rule 2a–7's risk-limiting conditions should result in fluctuations in value from changes in interest rates and credit risk being insignificant.

As is the case today with stable share price money market funds, events may occur that give rise to credit and liquidity issues for money market funds and shareholders would need to reassess if their investments continue to meet the definition of a cash equivalent. For example, during the financial crisis,

[265] Money market funds also would incur costs in gathering and transmitting this information to money market fund shareholders that they would not incur absent our proposal, but these costs are discussed in the operational costs discussed below.

[266] *See* 26 U.S.C. 1091.

[267] *Id.*

[268] These operational costs are discussed in *infra* section III.A.7.

[269] In addition, some corporate investors may perceive cash and cash equivalents on a company's balance sheet as a measure of financial strength.

[270] *See* Financial Accounting Standards Board Accounting Standards Codification (''FASB ASC'') paragraph 305–10–20.

[271] *Id.*

[272] *See, e.g.,* ICI Jan. 24 FSOC Comment Letter, *supra* note 25.

[273] *See* RSFI Study, *supra* note 21.

certain money market funds experienced unexpected declines in the fair value of their investments due to deterioration in the creditworthiness of their assets and as a result, portfolios of money market funds became less liquid. Investors in these money market funds would have needed to determine whether their investments continued to meet the definition of a cash equivalent. If events occur that cause shareholders in floating NAV money market funds to determine their shares are not cash equivalents, the shares would need to be classified as investments, and shareholders would have to treat them either as trading securities or available-for-sale securities.[274]

Do commenters believe using a floating NAV would preclude money market funds from being classified as cash equivalents under GAAP?

• Would shareholders be less likely to invest in floating NAV money market funds if the shares held were classified for financial statement purposes as an ''investment'' rather than ''cash and cash equivalent?''

• Are there any other accounting-related costs or burdens that money market fund shareholders would incur if we require money market funds to use floating NAVs?

c. Implications for Local Government Investment Pools

We also recognize that many states have established local government investment pools (''LGIPs''), money market fund-like investment pools that invest in short-term securities,[275] that are required by law or investment policies to maintain a stable NAV per share.[276] The Government Accounting Standards Board (''GASB'') states that LGIPs that are operated in a manner consistent with rule 2a–7 (*i.e.,* a ''2a7-like pool'') may use amortized cost to value securities (and presumably, facilitate maintaining a stable NAV per share).[277] Our floating NAV proposal, if adopted, may have implications for LGIPs. In order to continue to manage LGIPs, state statutes and policies may need to be amended to permit the operation of investment pools that adhere to rule 2a–7 as we propose to amend it.[278] Because we are unable to predict how various state legislatures and other market participants will react to our floating NAV proposal, we do not have the information necessary to provide a reasonable estimate of the impact on LGIPs or the potential effects on efficiency, competition, and capital formation. We note, however, that it is possible that states could amend their statutes or policies to permit the operation of LGIPs that comply with rule 2a–7 as we propose to amend it. We request comment on this aspect of our proposal.

• Would our floating NAV proposal affect LGIPs as described above? Are there other ways in which LGIPs would be affected? If so, please describe.

• Are there other costs that we have not considered?

• How do commenters think states and other market participants would react to our floating NAV proposal? Do commenters believe that states would amend their statutes or policies to permit LGIPs to have a floating NAV per share provided the fund complies with rule 2a–7, as we propose to amend it? If so, what types and amounts of costs would states incur? If not, would there be any effect on efficiency, competition, or capital formation?

7. Operational Implications of Floating NAV Money Market Funds

Money market funds (or their transfer agents) are required under rule 2a–7 to have the capacity to redeem and sell fund shares at prices based on the funds' current net asset value per share pursuant to rule 22c–1 rather than $1.00, *i.e.,* to transact at the fund's floating NAV.[279] Intermediaries, although not subject to rule 2a–7, typically have separate obligations to investors with regard to the distribution of proceeds received in connection with investments made or assets held on behalf of investors.[280] Prior to adopting these amendments to rule 2a–7, the ICI submitted a comment letter detailing the modifications that would be required to permit funds to transact at the fund's floating NAV.[281] Accordingly, we expect that money market funds and transfer agents already have laid the foundation required to use floating NAVs.

We recognize, however, that funds, transfer agents, intermediaries, and others in the distribution chain may not currently have the capacity to process transactions at floating NAVs constantly, as would be required under our proposal.[282] Accordingly, we expect that sub-transfer agents, fund accounting departments, custodians, intermediaries, and others in the distribution chain would need to develop and overlay additional controls and procedures on top of existing systems in order to implement a floating NAV on a continual basis. In each case, the controls and procedures for the accounting systems at these entities would have to be modified to permit those systems to calculate a money

[274] *See* FASB ASC paragraph 320–10–25–1.

[275] LGIPs tend to emulate typical money market funds by maintaining a stable NAV per share through investments in short-term securities. *See infra* III.E.1, Table 2, note N.

[276] *See, e.g.,* U.S. Chamber of Commerce Letter to the Hon. Elisse Walter (Feb. 13, 2013), *available at http://www.centerforcapitalmarkets.com/wp-content/uploads/2010/04/2013-2.13-Floating-NAV-Qs-Letter.pdf. See also, e.g.,* Virginia's Local Government Investment Pool Act, which sets certain prudential investment standards but leaves it to the state treasury board to formulate specific investment policies for Virginia's LGIP. *See* Va. Code Ann. § 2.2–4605(A)(3). Accordingly, the treasury board instituted a policy of managing Virginia's LGIP in accordance with ''certain risk limiting provisions to maintain a stable net asset value at $1.00 per share'' and ''GASB '2a–7 like' requirements.'' Virginia LGIP's Investment Circular, June 30, 2012, *available at http://www.trs.virginia.gov/cash/lgip.aspx.* Not all LGIPs are currently managed to maintain a stable NAV, however, *see infra* section III.E.1, Table 2, note N.

[277] *See* GASB, Statement No. 31, Accounting and Financial Reporting for Certain Investments and for External Investment Pools (Mar. 1997).

[278] *See, e.g.,* Comment Letter of American Public Power Assoc., et al., File No. FSOC–2012–0003 (Feb. 13, 2013) (''If the SEC rules are changed to adopt a daily floating NAV, states would have to alter their own statutes in order to comply, as many state statues cite rule 2a–7 as the model for their management of the LGIPs'').

[279] *See* rule 2a–7(c)(13). *See also* 2010 Adopting Release, *supra* note 92, at nn.362–363.

[280] *See, e.g.,* 2010 Adopting Release, *supra* note 92, at nn.362–363. Examples of intermediaries that offer money market funds to their customers include broker-dealers, portals, bank trust departments, insurance companies, and retirement plan administrators. *See* Investment Company Institute, Operational Impacts of Proposed Redemption Restrictions on Money Market Funds, at 13 (2012), *available at http://www.ici.org/pdf/ppr_12_operational_mmf.pdf* (''ICI Operational Impacts Study'').

[281] *See, e.g.,* Comment Letter of the Investment Company Institute (Sept. 8, 2009) (available in File No. S7–11–09) (''ICI 2009 Comment Letter'') (describing the modifications that would be necessary if the Commission adopted the requirement, currently reflected in rule 2a–7(c)(13), that money market funds (or their transfer agents) have the capacity to transact at a floating NAV, to: (i) Fund transfer agent recordkeeping systems (*e.g.,* special same-day settlement processes and systems, customized transmissions, and reporting mechanisms associated with same-day settlement systems and proprietary systems used for next-day settlement); (ii) a number of essential ancillary systems and related processes (*e.g.,* systems changes for reconciliation and control functions, transactions accepted via the Internet and by phone, modifying related shareholder disclosures and phone scripts, education and training for transfer agent employees and changes to the systems used by fund accountants that transmit net asset value data to fund transfer agents); and (iii) sub-transfer agent/recordkeeping arrangements (explaining that similar modifications likely would be needed at various intermediaries).

[282] Even though a fund complex's transfer agent system is the primary recordkeeping system, there are a number of additional subsystems and ancillary systems that overlay, integrate with, or feed to or from a fund's primary transfer agent system, incorporate custom development, and may be proprietary or vendor dependent (*e.g.,* print vendors to produce trade confirmations). *See* ICI Operational Impacts Study at 20, *supra* note 280. The systems of sub-transfer agents and other parties may also require modifications related to our floating NAV proposal.

market fund's floating NAV each business day and to communicate that value to others in the distribution chain on a permanent basis. In addition, we understand that, under our floating NAV proposal, money market funds and other recordkeepers would incur additional costs to track portfolio security gains and losses, provide ''basis reporting,'' and monitor for potential wash-sale transactions, as discussed above in section III.A.6. We believe, however, that funds, in many cases, should be able to leverage existing systems that track this information for other mutual funds.

We understand that the costs to modify a particular entity's existing controls and procedures would vary depending on the capacity, function and level of automation of the accounting systems to which the controls and procedures relate and the complexity of those systems' operating environments.[283] Procedures and controls that support systems that operate in highly automated operating environments would likely be less costly to modify while those that support complex operations with multiple fund types or limited automation or both would be more costly to change.[284] Because each system's capabilities and functions are different, an entity would likely have to perform an in-depth analysis of our proposed rules to calculate the costs of modifications required for its own system. While we do not have the information necessary to provide a point estimate of the potential costs of modifying procedures and controls, we expect that each entity would bear one-time costs to modify existing procedures and controls in the functional areas that are likely to be impacted by our proposal. Our staff has estimated that the one-time costs of implementation for an affected entity would range from $1.2 million (for entities requiring less extensive modifications) to $2.3 million (for entities requiring more extensive modifications).[285] Staff also estimates that the annual costs to keep procedures and controls current and to provide continuing training would range from 5% to 15% of the one-time costs.[286]

We anticipate, however, that many money market funds, transfer agents, custodians, and intermediaries in the distribution chain may not bear the estimated costs on an individual basis and therefore experience economies of scale. For example, the costs would likely be allocated among the multiple users of affected systems, such as money market funds that are members of a fund group, money market funds that use the same transfer agent or custodian, and intermediaries that use systems purchased from the same third party. Accordingly, we expect that the cost for many individual entities that would have to process transactions at floating NAVs may be less than the estimated costs.

We request comment on this analysis and our range of estimated costs to money market funds, transfer agents, custodians, and intermediaries.

- To what extent would transfer agents, fund accounting departments, custodians, and intermediaries need to develop and implement additional controls and procedures or modify existing ones under our floating NAV proposal?
- To what extent do intermediaries, as a result of their separate obligations to investors regarding distribution of proceeds, have the capacity to process (on a continual basis) transactions at a fund's floating NAV?
- Do money market funds and others expect they would incur costs in addition to those we estimate above or that they would incur different costs? If so, what are these costs?
- Would the costs incurred by money market funds and others in the distribution chain discussed above be passed on to retail (and other) investors in the form of higher fees?
- If a number of money market funds already report daily shadow prices using ''basis point'' rounding, are there additional operational costs that funds would incur to price their shares to four decimal places? If so, please describe. Are there means by which these operational costs can be reduced while still providing sufficient price transparency?
- Do all funds have the ready capability to price their shares to four decimal places? For those funds that do so already, we seek comment on the costs involved in developing this capability. For funds that do not have the capability, what types and amounts of costs would be incurred?
- What type of ongoing maintenance and training would be necessary, and to what extent? Do commenters agree that such costs would likely range between 5% and 15% of one-time costs? If not, is there a more accurate way to estimate these costs?
- To what extent would money market funds or others experience economies of scale?
- We request that intermediaries and others provide data to support the costs they expect they would incur and an explanation of the work they have already undertaken as a result of rule 2a–7's current requirement that money market funds (or their transfer agents) have the capacity to transact at a floating NAV.

In addition, funds would incur costs to communicate with shareholders the change to a floating NAV per share. Although funds (and their intermediaries that provide information to beneficial owners) already have the means to provide shareholders the values of their money market fund holdings, our staff anticipates that they would incur additional costs associated with programs and systems modifications necessary to provide shareholders with access to that information online, through automated phone systems, and on shareholder statements under our floating NAV proposal and to explain to shareholders that the value of their money market funds shares will fluctuate.[287]

Our staff anticipates that these communication costs would vary among funds (or their transfer agents) and fund intermediaries depending on the current capabilities of the entity's Web site, automated or manned phone systems, systems for processing shareholder statements, and the number of investors. We believe that money market funds themselves would need to perform an in-depth analysis of our proposed rules in order to estimate the necessary systems modifications. While we do not have the information necessary to provide a point estimate of the potential costs of systems modifications, our staff

[283] *See, e.g.,* ICI Operational Impacts Study at 37, *supra* note 280 (noting that the modifications necessary to transact at a floating NAV would ''require in some cases minor and other instances major modifications—depending on the complexity of the systems and the types of intermediaries and investors'' involved).

[284] *See, e.g., id.* at 41 (reporting that half of the respondents in its survey reported that their transfer agent systems ''already had the capability to process money market trades'' at a floating value, while the other respondents would need to modify their transfer agent systems to comply with the requirement to have the capacity to transact at a floating NAV).

[285] Staff estimates that these costs would be attributable to the following activities: (i) Drafting, integrating, and implementing procedures and controls; (ii) preparation of training materials; and (iii) training. *See also supra* note 245 (discussing the bases of our staff's estimates of operational and related costs).

[286] As noted throughout this Release, we recognize that adding new capabilities or capacity to a system (including modifications to related procedures and controls) will entail ongoing annual maintenance costs and understand that those costs generally are estimated as a percentage of initial costs of building or expanding a system.

[287] Staff expects these costs would include software programming modifications, as well as personnel costs that would include training and scripts for telephone representatives to enable them to respond to investor inquiries.

has estimated that the costs for a fund (or its transfer agent) or intermediary that may be required to perform these activities would range from $230,000 to $490,000.[288] Staff also estimates that funds (or their transfer agents) and their intermediaries would have ongoing costs to maintain automated phone systems and systems for processing shareholder statements, and to explain to shareholders that the value of their money market fund shares will fluctuate, and that these costs would range from 5% to 15% of the one-time costs.[289] We request comment on this aspect of our proposal.

• Do commenters agree with our estimated range of costs to funds (or their transfer agents) and fund intermediaries to communicate with shareholders the change to a floating NAV per share? If not, we request detailed estimates of the types and amounts of costs.

Money market funds' ability to maintain a stable value also facilitates the funds' role as a cash management vehicle and provides other operational efficiencies for their shareholders.[290] Money market fund shareholders generally are able to transact in fund shares at a stable value known in advance. This permits money market fund transactions to settle on the same day that an investor places a purchase or sell order, and allows a shareholder to determine the exact value of his or her money market fund shares (absent a liquidation event) at any time.[291] These features have made money market funds an important component of systems for processing and settling various types of transactions.[292]

Commenters have asserted that money market funds with floating NAVs would be incompatible with these systems because, among other things, transactions in shares of these money market funds, like other types of mutual fund transactions, would generally not settle on the same day that an order is placed, and the value of the shares of these money market funds could not be determined precisely before that day's NAV had been calculated.[293] Requiring money market funds to use floating NAVs, the commenters assert, would require money market fund shareholders and service providers to reprogram their systems or manually reconcile transactions, increasing staffing costs.[294] Others have asserted that similar considerations could affect features that are particularly appealing to retail investors, such as ATM access, check writing, electronic check payment processing services and products, and U.S. Fedwire transfers.[295] We note that we are proposing an exemption for retail funds which we expect would significantly alleviate any such concerns about the costs of altering those features, because funds that take advantage of the retail exemption would be able to maintain a stable price, and accordingly, such features would be unaffected. Nonetheless, not all funds with these features may choose to take advantage of the proposed retail exemption, and therefore, some funds may need to make additional modifications to continue offering these features. We have included estimates of the costs to make such modifications below. We seek comment on the extent to which these features may be affected by our proposal and the proposed retail exemption.

• Would money market funds and financial intermediaries continue to provide the retail-focused services discussed above if we were to require money market funds to use floating NAVs? If not, why not?

• Would investors reduce or eliminate their money market fund investments if these services were no longer available or if the cost of these services increases?

Commenters also assert that requiring money market funds to use floating NAVs would extend the settlement cycle from same-day settlement to next-day settlement, which would expose parties to transactions to increased risk (*e.g.,* during a day in which a transaction to be paid by proceeds from a sale of money market fund shares is still open, one party to the transaction could default).[296] But a money market

[288] Staff estimates that these costs would be attributable to the following activities: (i) Project assessment and development; (ii) project implementation and testing; and (iii) written and telephone communication. *See also supra* note 245 (discussing the bases of our staff's estimates of operational and related costs).

[289] As noted throughout this Release, we recognize that adding new capabilities or capacity to a system will entail ongoing annual maintenance costs and understand that those costs generally are estimated as a percentage of initial costs of building or expanding a system.

[290] *See, e.g.,* Federated Investors Alternative 1 FSOC Comment Letter, *supra* note 161; Comment Letter of Steve Fancher, et al. (Jan. 22, 2013) (available in File No. FSOC–2012–0003); Comment Letter of Steve Morgan, et al. (Jan. 22, 2013) (available in File No. FSOC–2012–0003) (''Steve Morgan FSOC Comment Letter''); Comment Letter of Edward Jones (Feb. 15, 2013) (available in File No. FSOC–2012–0003) (''Edward Jones FSOC Comment Letter'') (citing cash management benefits for individual investors in particular); Comment Letter of T. Rowe Price (Jan. 30, 2013) (available in File No. FSOC–2012–0003) (''T. Rowe Price FSOC Comment Letter'').

[291] *See, e.g.,* ICI Jan. 24 FSOC Comment Letter, *supra* note 25 (noting how same-day settlement is vitally important to many investors and describing how such same-day settlement is facilitated by a stable NAV). We note, however, that not all money market fund transactions settle on the same day. *See, e.g.,* ICI 2009 Comment Letter, *supra* note 281 (describing the systems and processes involved to permit same-day settlement and those involved for next-day settlement).

[292] *See, e.g.,* Comment Letter of John D. Hawke (Dec. 15, 2011) (available in File No. 4–619) (''Hawke Dec 2011 PWG Comment Letter'') (identifying various types of systems, including among others trust accounting systems at bank trust departments; corporate payroll processing systems and processing systems used to manage corporations' cash balances; processing systems used by federal, state, and local governments to manage their cash balances; and municipal bond trustee cash management systems).

[293] Hawke Dec 2011 PWG Comment Letter, *supra* note 292 (''The net result of a floating NAV would be to make Money Funds not useful to hold the large, short-term cash balances used in these automated transaction processing systems across a wide variety of businesses and applications.''); Comment Letter of Cachematrix Holdings LLC (Dec. 12, 2011) (available in File No. 4–619) (''Cachematrix PWG Comment Letter'') (''A stable share price is critical to same-day and next-day processing, shortened settlement times, float management, and mitigation of counterparty risk among firms.''); Comment Letter of State Street Global Advisors (Sept. 8, 2009) (available in File No. S7–11–09) (''[T]he stable NAV simplifies transaction settlement, which permits money market funds to offer shareholders same day settlement options, as well as ATM access, check writing, and ACH/FedWire transfers.'').

[294] *See, e.g.,* Hawke Dec 2011 PWG Comment Letter, *supra* note 292 (stating that ''[m]anual processing [required to reconcile the day-to-day fluctuations in the value of money market funds with a floating NAV] would mean more staffing requirement, more costs associated with staffing the function, and errors and delays in completing the process'' and that reprogramming systems would ''take many years and hundreds of millions of dollars to complete across a wide range of businesses and applications for which stable value money funds currently are used to hold short-term liquidity''); Cachematrix PWG Comment Letter, *supra* note 293 (''[A]n entire industry has programmed accounting, trading and settlement systems based on a stable share price. The cost for each bank to retool their sub-accounting systems to accommodate a fluctuating NAV could be in the millions of dollars. This does not take into account the costs that each bank would then pass on to the thousands of corporations that use money market trading systems.'').

[295] *See, e.g.,* Comment Letter of Fidelity Investments (Feb. 14, 2013) (available in File No. FSOC–2012–0003) (''Fidelity FSOC Comment Letter''). ([B]roker-dealers offer clients a variety of features that are available generally only to accounts with a stable NAV, including ATM access, check writing, and ACH and Fedwire transfers. A floating NAV would force MMFs that offer same day settlement on shares redeemed through wire transfers to shift to next day settlement or require fund advisers to modify their systems to accommodate floating NAV MMFs.''); Edward Jones FSOC Comment Letter, *supra* note 290; ICI Feb 2012 PWG Comment Letter, *supra* note 259 (''[E]limination of the stable NAV for money market funds would likely force brokers and fund sponsors to consider how or whether they could continue to provide such services to money market fund investors.'').

[296] *See, e.g.,* Hawke Dec 2011 PWG Comment Letter, *supra* note 292 (''Both parties would carry the unsettled transaction as an open position for one extra day and each party would be exposed for that time to the risk that its counterparty would default during the extra day, or that the bank holding the cash overnight (or over the weekend) would fail. For a bank involved in making a

fund with a floating NAV could still offer same-day settlement. The fund could price its shares each day and provide redemption proceeds that evening. Indeed, we are aware of two floating NAV money market funds that normally operate this way.[297] Alternatively, funds could price their shares periodically (*e.g.,* at noon and 4 p.m. each day) to provide same-day settlement.[298] We recognize that pricing services may incur operational costs to modify their systems (and pass these costs along to funds) to provide pricing multiple times each day and seek comment on the nature and amounts of these costs.

- Do commenters expect to incur the types of costs described above (*e.g.,* increased staffing costs to manually reconcile transactions)? Are there additional costs we have not identified?
- What kinds of costs, specifically, do commenters expect to incur? What kinds of employee costs would be involved?
- Would an extended settlement cycle impose costs on money market fund investors? If so, what kinds of costs and how much?
- Would money market funds extend the settlement cycle or would they exercise either of those other options?
- Would exercising either of the two options discussed above impose costs on money market funds? If so, how much? Are there options that we have not identified that money market funds could use to provide same-day settlement?
- Would extending the settlement cycle cause investors to leave or not invest in money market funds?
- Do commenters agree that a delay in settlement for some money market fund transactions could expose parties to the transactions to increased counterparty risk? To what extent would this occur, and how does the nature of this risk differ from counterparty risk that arises in other aspects of a money market fund shareholder's business?
- Do commenters agree that money market funds generally could still offer same-day settlement if required to use a floating NAV?
- Do fund pricing services have the capacity to provide pricing multiple times each day? If not, what types and amounts of costs would pricing services incur to develop this capacity? Would pricing services pass these costs down to funds?
- Are the money market funds that currently same-day settle with a floating NAV representative of what a broader industry of floating NAV money market funds could achieve? Are there additional costs or complications in conducting such same-day settlement for larger funds than smaller funds?

In addition to money market funds and other entities in the distribution chain, each money market fund shareholder would also likely be required to perform an in-depth analysis of our floating NAV proposal and its own existing systems, procedures, and controls to estimate the systems modifications it would be required to undertake. Because of this, and the variation in systems currently used by institutional money market fund shareholders, we do not have the information necessary to provide a point estimate of the potential costs of systems modifications. Nevertheless, our staff has attempted to describe the types of activities typically involved in making systems modifications and estimated a range of hours and costs that may be required to perform these activities. In addition, the Commission requests from commenters information regarding the potential costs of system modifications for money market fund shareholders.

Our staff has prepared ranges of estimated costs, taking into account variations in the functionality, sophistication, and level of automation of money market fund shareholders' existing systems and related procedures and controls, and the complexity of the operating environment in which these systems operate.[299] In deriving its estimates, our staff considered the need to modify systems and related procedures and controls related to recordkeeping, accounting, trading, cash management, and bank reconciliations, and to provide training concerning these modifications.

Staff estimates that a shareholder whose systems (including related procedures and controls) would require less extensive or labor-intensive modifications would incur one-time costs ranging from $123,000 to $253,000.[300] Staff estimates that a shareholder whose systems (including related procedures and controls) would require more extensive or labor-intensive modifications would incur one-time costs ranging from $1.4 million to $2.9 million.[301] In addition, staff estimates the annual maintenance costs to these systems and procedures and controls, and the costs to provide continuing training, would range from 5% to 15% of the one-time implementation costs.[302] We request comment on our analysis and the nature and extent of the costs money market fund shareholders anticipate they would incur as a result of our floating NAV proposal.

- Are shareholder systems in fact unable to accommodate a floating NAV, even if the NAV typically fluctuates very little (a fraction of a penny) on a day-to-day basis?
- If shareholder systems are unable to accommodate a floating NAV, what kinds of programming costs would shareholders incur in reprogramming the systems and how do they compare to our staff's estimates above?
- Do shareholders have other systems they use to manage their investments that fluctuate in value? If so, could these systems be used for money market funds? If not, why not?
- How much would it cost to adapt existing shareholder systems (currently used to accommodate investments that fluctuate in value) to accommodate money market funds with floating NAVs and how do these costs compare to our staff's estimates above?

payment in anticipation of an incoming funds transfer as part of these processing systems, this change from same-day to next-day processing of money fund redemptions would turn intra-day overdrafts into overnight overdrafts, resulting in much greater default and funding risks to the bank. This extra day's float would mean more risk in the system and a larger average float balance that each party must carry and finance.''); Cachematrix PWG Comment Letter, *supra* note 293 (''A stable share price is critical to same-day and next-day processing, shortened settlement times, float management, and mitigation of counterparty risk among firms.'').

[297] *See, e.g.,* the prospectus for the DWS Variable NAV Money Fund, dated December 1, 2011, *available at http://www.sec.gov/Archives/edgar/data/863209/000008805311001627/nb120111ict-vnm.txt* (''If the fund receives a sell request prior to the 4:00 p.m. Eastern time cut-off, the proceeds will normally be wired on the same day. However, the shares sold will not earn that day's dividend.''); prospectus for the Northern Funds, dated December 7, 2012, *available at http://www.sec.gov/Archives/edgar/data/916620/000119312512495705/d449473d485apos.htm* (''Redemption proceeds normally will be sent or credited on the next Business Day or, if you are redeeming your shares through an authorized intermediary, up to three Business Days, following the Business Day on which such redemption request is received in good order by the deadline noted above, unless payment in immediately available funds on the same Business Day is requested.'').

[298] We understand that pricing vendors may not provide continual pricing throughout the day. Instead, money market funds could establish periodic times at which the fund would price its shares.

[299] Some money market fund shareholders do not use systems and would not use them under this proposal (*e.g.,* many retail investors), and these shareholders of course would not incur any systems modifications costs.

[300] Staff estimates that these costs would be attributable to the following activities: (i) Planning, coding, testing, and installing system modifications; (ii) drafting, integrating, implementing procedures and controls; (iii) preparation of training materials; and (iv) training. *See also supra* note 245 (discussing the bases of our staff's estimates of operational and related costs).

[301] *Id.*

[302] *See supra* note 286.

8. Disclosure Regarding Floating NAV

We are proposing disclosure-related amendments to rule 482 under the Securities Act [303] and Form N–1A in connection with the floating NAV alternative. We anticipate that the proposed rule and form amendments would provide current and prospective shareholders with information regarding the operations and risks of this reform alternative. In keeping with the enhanced disclosure framework we adopted in 2009,[304] the proposed amendments are intended to provide a layered approach to disclosure in which key information about the proposed new features of money market funds would be provided in the summary section of the statutory prospectus (and, accordingly, in any summary prospectus, if used) with more detailed information provided elsewhere in the statutory prospectus and in the statement of additional information (''SAI'').

a. Disclosure Statement

The move to a floating NAV would be designed to change the investment expectations and behavior of money market fund investors. As a measure to achieve this change, we propose to require that each money market fund, other than a government or retail fund, include a bulleted statement disclosing the particular risks associated with investing in a floating NAV money market fund on any advertisement or sales material that it disseminates (including on the fund Web site). We also propose to include wording designed to inform investors about the primary risks of investing in money market funds generally in this bulleted disclosure statement. While money market funds are currently required to include a similar disclosure statement on their advertisements and sales materials,[305] we propose amending this disclosure statement to emphasize that money market fund sponsors are not obligated to provide financial support, and that money market funds may not be an appropriate investment option for investors who cannot tolerate losses.[306]

Specifically, we would require floating NAV money market funds to include the following bulleted disclosure statement on their advertisements and sales materials:

- You could lose money by investing in the Fund.
- You should not invest in the Fund if you require your investment to maintain a stable value.
- The value of shares of the Fund will increase and decrease as a result of changes in the value of the securities in which the Fund invests. The value of the securities in which the Fund invests may in turn be affected by many factors, including interest rate changes and defaults or changes in the credit quality of a security's issuer.
- An investment in the Fund is not insured or guaranteed by the Federal Deposit Insurance Corporation or any other government agency.
- The Fund's sponsor has no legal obligation to provide financial support to the Fund, and you should not expect that the sponsor will provide financial support to the Fund at any time.[307]

We also propose to require a substantially similar bulleted disclosure statement in the summary section of the statutory prospectus (and, accordingly, in any summary prospectus, if used).[308]

With respect to money market funds that are not government or retail funds, we propose to remove current requirements that money market funds state that they seek to preserve the value of shareholder investments at $1.00 per share.[309] This disclosure, which was adopted to inform investors in money market funds that a stable net asset value does not indicate that the fund will be able to maintain a stable NAV,[310] will not be relevant once funds are required to ''float'' their net asset value.

As discussed above, the floating NAV proposal would provide exemptions to the floating NAV requirement for government and retail money market funds.[311] Accordingly, the proposed amendments to rule 482 and Form N–1A would require government and retail money market funds to include a bulleted disclosure statement on the fund's advertisements and sales materials and in the summary section of the fund's statutory prospectus (and, accordingly, in any summary prospectus, if used) that does not discuss the risks of a floating NAV, but that would be designed to inform investors about the risks of investing in money market funds generally.[312] We propose to require each government and retail fund to include the following bulleted disclosure statement in the summary section of its statutory prospectus (and, accordingly, in any summary prospectus, if used), and on any advertisement or sales material that it disseminates (including on the fund Web site):

- You could lose money by investing in the Fund.
- The Fund seeks to preserve the value of your investment at $1.00 per

[303] Rule 482 applies to advertisements or other sales materials with respect to securities of an investment company registered under the Investment Company Act that is selling or proposing to sell its securities pursuant to a registration statement that has been filed under the Investment Company Act. *See* rule 482(a). This rule describes the information that is required to be included in an advertisement, including a disclosure statement that must be used on money market fund advertisements. *See* rule 482(b).

Our proposal would also affect fund supplemental sales literature (*i.e.,* sales literature that is preceded or accompanied by a statutory prospectus). Rule 34b–1 under the Investment Company Act prescribes the requirements for supplemental sales literature. Because rule 34b–1(a) cross-references the requirements of rule 482(b)(4), any changes made to that provision will affect the requirements for fund supplemental sales literature.

[304] *See* Enhanced Disclosure and New Prospectus Delivery Option for Registered Open-End Management Investment Companies, Investment Company Act Release No. 28584 (Jan. 13, 2009) [74 FR 4546 (Jan. 26, 2009)] (''Summary Prospectus Adopting Release'') at paragraph preceding section III (adopting rules permitting the use of a summary prospectus, which is designed to provide key information that is important to an informed investment decision).

[305] *See supra* note 303. Rule 482(b)(4) (which currently requires a money market fund to include the following disclosure statement on its advertisements and sales materials: An investment in the Fund is not insured or guaranteed by the Federal Deposit Insurance Corporation or any other government agency. Although the Fund seeks to preserve the value of your investment at $1.00 per share, it is possible to lose money by investing in the Fund).

[306] *See infra* note 607 and accompanying text (discussing the extent to which discretionary sponsor support has the potential to confuse money market fund investors); *supra* note 141 and accompanying text (noting that survey data shows that some investors are unsure about the amount of risk in money market funds and the likelihood of government assistance if losses occur).

[307] *See* proposed (FNAV) rule 482(b)(4)(i). If an affiliated person, promoter, or principal underwriter of the fund, or an affiliated person of such person, has entered into an agreement to provide financial support to the fund, the fund would be permitted to omit the last bulleted sentence from the disclosure statement for the term of the agreement. *See* Note to paragraph (b)(4), proposed (FNAV) rule 482(b)(4).

[308] *See* proposed (FNAV) Item 4(b)(1)(ii)(A) of Form N–1A. Item 4(b)(1)(ii) currently requires a money market fund to include the following statement in its prospectus: An investment in the Fund is not insured or guaranteed by the Federal Deposit Insurance Corporation or any other government agency. Although the Fund seeks to preserve the value of your investment at $1.00 per share, it is possible to lose money by investing in the Fund.

[309] *See* Item 4(b)(1)(ii) of Form N–1A; proposed (FNAV) Item 4(b)(1)(ii)(A) of Form N–1A.

[310] *See* Registration Form Used by Open-End Management Investment Companies, Investment Company Act Release No. 23064 (Mar. 13, 1998) [63 FR 13916 (Mar. 23, 1998)] (release amending disclosure) (''Registration Statement Adopting Release''); Revisions to Rules Regulating Money Market Funds, Investment Company Act Release No. 18005 (Feb. 20, 1990) [56 FR 8113 (Feb. 27, 1991)] (adopting release); Revisions to Rules Regulating Money Market Funds, Investment Company Act Release No. 17589 (July 17, 1990) [55 FR 30239 (July 25, 1990)] (''1990 Proposing Release'').

[311] *See supra* sections III.A.3 and III.A.4 and proposed (FNAV) rules 2a–7(c)(2) and (c)(3).

[312] *See supra* notes 305–306 and accompanying text.

share, but cannot guarantee such stability.

• An investment in the Fund is not insured or guaranteed by the Federal Deposit Insurance Corporation or any other government agency.

• The Fund's sponsor has no legal obligation to provide financial support to the Fund, and you should not expect that the sponsor will provide financial support to the Fund at any time.[313]

The proposed disclosure statements are intended to be one measure to change the investment expectations and, therefore, the behavior of money market fund investors. The risk-limiting conditions of rule 2a–7 and past experiences of money market fund investors have created expectations of a stable, cash-equivalent investment. As discussed above, one reason for such expectation may have been the role of sponsor support in maintaining a stable net asset value for money market funds.[314] In addition, we are concerned that investors, under the floating NAV proposal, will not be fully aware that the value of their money market fund shares will increase and decrease as a result of the changes in the value of the underlying portfolio securities.[315] In proposing the disclosure statement, we have taken into consideration investor preferences for clear, concise, and understandable language.[316] We also considered whether language that was stronger in conveying potential risks associated with money market funds would be effective for investors.[317] In addition, we considered whether the proposed disclosure statement should be limited to only money market fund advertisements and sales materials, as discussed above. Although we acknowledge that the summary section of the prospectus must contain a discussion of key risk factors associated with a floating NAV money market fund, we believe that the importance of the disclosure statement merits its placement in both locations, similar to how the current money market fund legend is required in both money market fund advertisements and sales materials and the summary section of the prospectus.[318]

We request comment on the disclosure statements [319] proposed to be required on any money market fund advertisements or sales materials, as well as in the summary section of a fund's statutory prospectus (and, accordingly, in any summary prospectus, if used).

• Would the disclosure statement proposed to be used by floating NAV funds adequately alert investors to the risks of investing in a floating NAV fund, and would investors understand the meaning of each part of the proposed disclosure statement? Will investors be fully aware that the value of their money market fund shares will increase and decrease as a result of the changes in the value of the underlying portfolio securities? If not, how should the proposed disclosure statement be amended?

• Would the disclosure statement proposed to be used by government and retail money market funds, which are not subject to the floating NAV requirement, adequately alert investors to the risks of investing in those types of funds, and would investors understand the meaning of each part of the proposed disclosure statement? If not, how should the proposed disclosure statement be amended?

• Would different shareholder groups or different types of funds benefit from different disclosure statements? For example, should retail and institutional investors receive different disclosure statements, or should funds that offer cash management features such as check writing provide different disclosure statements from funds that do not? Why or why not? If yes, how should the disclosure statement be tailored to different shareholder groups and fund types?

• Will the proposed disclosure statement respond effectively to investor preferences for clear, concise, and understandable language?

• Would the following variations on the proposed disclosure statement be any more or less useful in alerting shareholders to the risks of investing in a floating NAV fund (as applicable) and/or the risks of investing in money market funds generally?

○ Removing or amending the following bullet point in the proposed disclosure statement: ''The Fund's sponsor has no legal obligation to provide financial support to the Fund, and you should not expect that the sponsor will provide financial support to the Fund at any time.''

○ Removing or amending the following bullet point in the proposed disclosure statement: ''The value of the securities in which the Fund invests may in turn be affected by many factors, including interest rate changes and defaults or changes in the credit quality of a security's issuer.''

○ Amending the final bullet point in the proposed disclosure statement to read: ''Your investment in the Fund therefore may experience losses.''

○ Amending the final bullet point in the proposed disclosure statement to read: ''Your investment in the Fund therefore may experience gains or losses.''

• Would investors benefit from requiring the proposed disclosure statement also to be included on the front cover page of a money market fund's prospectus (and on the cover page or beginning of any summary prospectus, if used)?

• Would investors benefit from any additional types of disclosure in the summary section of the statutory prospectus or on the prospectus' cover page? If so, what else should be included?

• Should we provide any instruction or guidance in order to highlight the proposed disclosure statement on fund advertisements and sales materials (including the fund's Web site) and/or lead investors efficiently to the

[313] *See* proposed (FNAV) rule 482(b)(4)(ii) and proposed (FNAV) item 4(b)(1)(ii)(B) of Form N–1A; *see also supra* notes 305 and 308 (discussing the current corresponding disclosure requirements for money market funds). If an affiliated person, promoter, or principal underwriter of the fund, or an affiliated person of such person, has entered into an agreement to provide financial support to the fund, the fund would be permitted to omit the last bulleted sentence from the disclosure statement that appears on a fund advertisement or fund sales material, for the term of the agreement. *See* Note to paragraph (b)(4), proposed (FNAV) rule 482(b)(4).

Likewise, if an affiliated person, promoter, or principal underwriter of the fund, or an affiliated person of such person, has entered into an agreement to provide financial support to the fund, and the term of the agreement will extend for at least one year following the effective date of the fund's registration statement, the fund would be permitted to omit the last bulleted sentence from the disclosure statement that appears on the fund's registration statement. *See* Instruction to proposed (FNAV) item 4(b)(1)(ii) of Form N–1A.

[314] *See supra* section II.B.3.

[315] *See* Fidelity FSOC Comment Letter, *supra* note 295 (finding, from its study, that 81% of its retail money market fund investors understood that securities held by these funds have some small day-to-day fluctuations). However, the study did not address the extent to which these investors understood that these fluctuations could impact the value of their shares of money market funds, rather than the value of the underlying portfolio securities.

[316] *See* Study Regarding Financial Literacy Among Investors, a study by staff of the U.S. Securities and Exchange Commission (Aug. 2012), *available at http://www.sec.gov/news/studies/2012/917-financial-literacy-study-part1.pdf*, at vi.

[317] *See* Molly Mercer et al., *Worthless Warnings? Testing the Effectiveness of Disclaimers in Mutual Fund Advertisements,* 7 J. Empirical Legal Stud. 429 (2010) (evaluating the usefulness of legends in mutual fund advertisements regarding performance advertising).

[318] *See supra* notes 305 and 308.

[319] In the questions that follow, we use the term ''disclosure statement'' to mean the new disclosure statement that we propose to require floating NAV funds to incorporate into their prospectuses and advertisements and sales materials or, alternatively and as appropriate, the new disclosure statement that we propose to require government or retail funds to incorporate into their prospectuses and advertisements and sales materials.

disclosure statement?[320] For example, with respect to the fund's Web site, should we instruct that the proposed disclosure statement be posted on the fund's home page or be accessible in no more than two clicks from the fund's home page?

b. Disclosure of Tax Consequences and Effects on Fund Operations

The proposed requirement that money market funds transition to a floating NAV would entail certain additional tax- and operations-related disclosure, which disclosure requirements would not necessitate rule and form amendments.[321] As discussed above, if we were to require certain money market funds to use a floating NAV, taxable investors in money market funds, like taxable investors in other types of mutual funds, may experience taxable gains and losses.[322] Currently, funds are required to describe in their prospectuses the tax consequences to shareholders of buying, holding, exchanging, and selling the fund's shares.[323] Accordingly, we expect that, pursuant to current disclosure requirements, floating NAV money market funds would include disclosure in their prospectuses about the tax consequences to shareholders of buying, holding, exchanging, and selling the shares of the floating NAV fund. In addition, we expect that a floating NAV money market fund would update its prospectus and SAI disclosure regarding the purchase, redemption, and pricing of fund shares, to reflect any procedural changes resulting from the fund's use of a floating NAV.[324] As discussed below, if we were to adopt the floating NAV alternative, the compliance date would be 2 years after the effective date of the adoption with respect to any amendments specifically related to the floating NAV proposal, including related amendments to disclosure requirements.[325]

We request comment on the disclosure that we expect floating NAV money market funds would include in their prospectuses about the tax consequences to shareholders of buying, holding, exchanging, and selling the shares of the fund, as well as the effects (if any) on fund operations resulting from the transition to a floating NAV.

- Should Form N–1A or its instructions be amended to more explicitly require any of the disclosure we discuss above, or any additional disclosure, to be included in a fund's prospectus and/or SAI?
- Is there any additional information about a floating NAV fund's operations that shareholders should be aware of that is not discussed above? If so, would such additional information already be covered under existing Form N–1A requirements, or would we need to make any amendments to the form or its instructions?

c. Disclosure of Transition to Floating NAV

A fund must update its registration statement to reflect any material changes by means of a post-effective amendment or a prospectus supplement (or ''sticker'') pursuant to rule 497 under the Securities Act.[326] We would expect that, to meet this requirement, at the time that a stable NAV money market fund transitions to a floating NAV (or adopts a floating NAV in the course of a merger or other reorganization),[327] it would update its registration statement to include relevant related disclosure, as discussed in this section of the Release, by means of a post-effective amendment or a prospectus supplement. We request comment on this requirement.

- Besides requiring a fund that transitions to a floating NAV to update its registration statement by filing a post-effective amendment or prospectus supplement, should we also require that, when a fund transitions to a floating NAV, it must notify shareholders individually about the risks and operational effects of a floating NAV on the fund, such as a separate mailing or email notice? Would shareholders be more likely to understand and appreciate these risks and operational effects (disclosure of which would be included in the fund's registration statement, as discussed above) if they were to receive such individual notification? If so, what information should this individual notification include? What would be an appropriate time frame for this notification? How would such notification be accomplished, and what costs would be incurred in providing such notification?

d. Request for Comment on Money Market Fund Names

As discussed above, our floating NAV proposal would provide exemptions to the floating NAV requirements for government money market funds and retail money market funds. We request comment on whether we should require new terminology in money market fund names[328] to reduce the risk of investor confusion that might result from permitting some types of funds to maintain a stable price, while requiring others types of funds to use a floating NAV.

- Given that, under our floating NAV proposal, some funds' share prices would increase and decrease as a result of changes in the value of the securities in which the fund invests, should we require new terminology in money market fund names to reduce any risk of investor confusion that might result from both stable price money market funds and floating NAV money market funds using the same term ''money market fund'' in their names? For example, should we require money market funds to use either the term ''stable money market fund'' or ''floating money market fund,'' as appropriate, in their names? Why or why not?

e. Economic Analysis

The floating NAV proposal makes significant changes to the nature of money market funds as an investment vehicle. The proposed disclosure requirements in this section are intended to communicate to shareholders the nature of the risks that follow from the floating NAV proposal. In section III.E, we discussed how the floating NAV proposal might affect shareholders' use of money market funds and the resulting effects on the short-term financing markets. The factors and uncertain effects of those factors discussed in that section would influence any estimate of the incremental effects that the proposed disclosure requirements might have on either shareholders or the short-term financing markets. However, we believe that the proposed disclosure will better inform shareholders about the changes, which should result in shareholders making investment decisions that better match their investment preferences. We expect that this will have similar effects on efficiency, competition, and capital formation as those that are outlined in

[320] Such instruction or guidance would supplement current requirements for the presentation of the disclosure statement required by rule 482(b)(4). *See supra* note 305; rule 482(b)(5).

[321] Prospectus disclosure regarding the tax consequences of these activities is currently required by Form N–1A. *See* Item 11(f) of Form N–1A.

[322] *See supra* section III.A.6 (discussing the tax and economic implications of floating NAV money market funds).

[323] *See* Item 11(f) of Form N–1A.

[324] We expect that a money market fund would include this disclosure (as appropriate) in response to, for example, Item 11(''Shareholder Information'') and Item 23 (''Purchase, Redemption, and Pricing of Shares'') of Form N–1A.

[325] *See infra* section III.N.1.

[326] *See* 17 CFR 230.497.

[327] *See infra* section III.N.

[328] *See* rule 2a–7(b)(3) (setting forth the conditions for a fund to use a name that suggests that it is a money market fund or the equivalent, including using terms such as ''cash,'' ''liquid,'' ''money,'' ''ready assets,'' or similar terms in a fund's name).

section III.E rather than introduce new effects. We further believe that the effects of the proposed disclosure requirements will be small relative to the effects of the floating NAV proposal. The Commission staff cannot estimate the quantitative benefits of these proposed requirements at this time because of uncertainty about how increased transparency may affect different investors' understanding of the risks associated with money market funds.[329] We request additional data from commenters below to enable us to effectively calculate these effects.

We anticipate that all money market funds would incur costs to update their registration statements, as well as their advertising and sales materials (including the fund Web site), to include the proposed disclosure statement, and that floating NAV funds additionally would incur costs to update their registration statements to incorporate tax- and operations-related disclosure relating to the use of a floating NAV. We expect these costs generally would be incurred on a one-time basis. Our staff estimates that the average costs for a floating NAV money market fund to comply with these proposed disclosure amendments would be approximately $1,480 and that the compliance costs for a government or retail money market fund would be approximately $592.[330] Each money market fund in a fund group might not incur these costs individually.

We request comment on this economic analysis:

- Are any of the proposed disclosure requirements unduly burdensome, or would they impose any unnecessary costs?
- We request comment on the staff's estimates of the operational costs associated with the proposed disclosure requirements.
- We request comment on our analysis of potential effects of these proposed disclosure requirements on efficiency, competition, and capital formation.

9. Transition

The PWG Report suggests that a transition to a floating NAV could itself result in significant redemptions.[331] Money market fund investors could seek to redeem shares ahead of other investors to avoid realizing losses when their money market funds switch to a floating NAV. Investors may anticipate their funds' NAVs per share being less than $1.00 when the switch occurs or they may fear their funds might incur liquidity costs from heavy redemptions resulting from the behavior of other investors.

To avoid large numbers of preemptive redemptions by shareholders and allow sufficient time for funds and intermediaries to cost-effectively adapt to the new requirements, we propose to delay compliance with this aspect of the proposed rules for a period of 2 years from the effective date of our proposed rulemaking. Accordingly, money market funds subject to our floating NAV proposal could continue to price their shares as they do today for up to 2 years following this date. On or before the compliance date, all stable value money market funds not exempted from the floating NAV proposal would convert to a floating NAV. However, we note that, under our floating NAV proposal, investors who prefer a stable price product also could invest in a government or retail money market fund. We request comment on the proposed transition.

If we were to adopt the floating NAV proposal, money market funds and their shareholders would have 2 years to understand the implications of and implement our reform. We believe this would benefit money market funds and their shareholders by allowing money market funds to make this transition at the optimal time and potentially not at the same time as all other money market funds (which may be more likely to have a disruptive effect on the short-term financing markets, and thus not be perceived as optimal by funds). It would also provide time for investors such as corporate treasurers to modify their investment guidelines or seek changes to any statutory or regulatory constraints to which they are subject to permit them to invest in a floating NAV money market fund or other investments as appropriate.

Giving fund shareholders ample time to dispose of their investments in an orderly fashion also should benefit money market funds and their other shareholders because it would give funds additional time to respond appropriately to the level and timing of redemption requests.[332] We recognize, however, that shareholders might still preemptively redeem shares at or near the time that the money market fund converts from a stable value to a floating NAV if they believe that the market value of their shares will be less than $1.00. We expect, however, that money market fund sponsors would use the relatively long compliance period to select an appropriate conversion date that would minimize this risk. We therefore expect that providing shareholders, funds, and others a relatively long time to assess the effects of the regulatory change if adopted would mitigate the risk that the transition to a floating NAV, itself, could prompt significant redemptions.[333]

We considered an even longer transition period, including the 5-year period in FSOC's proposed floating NAV recommendation.[334] FSOC's

[329] Likewise, uncertainty regarding how the proposed disclosure may affect different investors' behavior would make it difficult for the SEC staff to measure the quantitative benefits of the proposed requirements. With respect to the proposed disclosure statement, there are many possible permutations on specific wording that would convey the specific concerns identified in this Release, and the breadth of these permutations makes it difficult for SEC staff to test how investors would respond to each wording variation.

[330] Staff estimates that these costs would be attributable to amending the fund's disclosure statement and updating the fund's advertising and sales materials. *See supra* note 245 (discussing the bases of our staff's estimates of operational and related costs). The costs associated with these activities are all paperwork-related costs and are discussed in more detail in *infra* section IV.A.7.

We expect the new required disclosure would add minimal length to the current required prospectus disclosure, and thus would not increase the number of pages in, or change the printing costs of, a fund's prospectus. Based on conversations with fund representatives, the Commission understands that, in general, unless the page count of a prospectus is changed by at least four pages, printing costs would remain the same.

[331] PWG Report, *supra* note 111, at 22. Other commenters have voiced additional concern that redemptions as a result of the transition to a floating NAV could be destabilizing to the financial markets. *See, e.g.,* ICI Jan. 24 FSOC Comment Letter, *supra* note 25; Comment Letter from American Association of State Colleges and Universities (Jan. 21, 2011) (available in File No. 4–619).

[332] Comment Letter of Thrivent Mutual Funds (Jan. 10, 2011) (available in File No. 4–619) (''Any change [to a floating NAV] could be implemented with sufficient advanced notice to allow institutional investors to modify their investment guidelines to permit investment in a floating NAV fund, where appropriate. A mass exodus assumes that investors have a clear alternative, which they do not, and come to the same conclusion in tandem, which is improbable given the lack of clear alternatives.''); Richmond Fed PWG Comment Letter, *supra* note 139 (''If informed well ahead of a change [to a floating NAV], investors are more likely to move gradually, mitigating the disruption.''). In addition, a relatively long compliance period would provide money market funds sufficient time to modify and/or establish the systems necessary to transact permanently at a floating NAV.

[333] In its proposal, FSOC suggested a transition period of 5 years. FSOC Proposed Recommendations, *supra* note 114, at 31.

[334] *See* FSOC Proposed Recommendations, *supra* note 114, at 31 (''To reduce potential disruptions and facilitate the transition to a floating NAV for investors and issuers, existing MMFs could be grandfathered and allowed to maintain a stable NAV for a phase-out period, potentially lasting five years. Instead of requiring these grandfathered funds to transition to a floating NAV immediately, the SEC would prohibit any new share purchases in the grandfathered stable-NAV MMFs after a

Continued

proposed recommendation, however, would have required money market funds to re-price their shares at $100 per share, and would have grandfathered existing money market funds (which could continue to maintain a stable value) but required investments after a specified date to be made in floating NAV money market funds. Money market fund sponsors therefore would have had to take a corporate action to re-price their shares and, if they chose to rely on the grandfathering, to form new floating NAV money market funds to accept new investments after the specified date. Money market funds and others in the distribution chain may be better able to implement basis point rounding as we propose, and therefore may not need a 5-year transition period. Indeed, some commenters on FSOC's proposed recommendation, which could require a longer transition period than our proposal, supported a 2-year transition period.[335]

We request comment on our proposed compliance date.

- Would our proposed transition period mitigate operational or significant redemption risks that could result from requiring money market funds to use floating NAVs?
- If not, how much time would be sufficient to allow money market fund shareholders that do not wish to remain in a money market fund with a floating NAV to identify alternatives without posing operational or significant redemption risk?
- Do commenters agree that a compliance period of 2 years is sufficient to address operational issues associated with converting funds to floating NAVs? Should the compliance period be shorter or longer? Why? Would a 5-year transition period, consistent with FSOC's proposed floating NAV recommendation, be more appropriate?
- Do fund sponsors anticipate converting (at an appropriate time) existing stable value money market funds to floating NAV funds or would sponsors establish new funds? If sponsors expect to establish new funds, are there costs other than those we describe below (related to a potential grandfathering provision)?
- Are there other measures we could take that would minimize the risks that could arise from investors seeking preemptively to redeem their shares in advance of a fund's adoption of a floating NAV?
- Should we provide a grandfathering provision, in addition to, or in lieu of, a relatively long compliance date? If we adopted a grandfathering provision, how long should the grandfathering period last? Would a grandfathering provision better achieve our objective of facilitating an orderly transition?

*B. Standby Liquidity Fees and Gates*

As an alternative to the floating NAV proposal discussed above, we are proposing to continue to allow money market funds to transact at a stable share price under normal conditions but to (1) require money market funds to institute a liquidity fee in certain circumstances and (2) permit money market funds to impose a gate in certain circumstances. In particular, this fees and gates alternative proposal would require that if a money market fund's weekly liquid assets fell below 15% of its total assets (the ''liquidity threshold''), the fund must impose a liquidity fee of 2% on all redemptions unless the board of directors of the fund (including a majority of its independent directors) determines that imposing such a fee would not be in the best interest of the fund. The board may also determine that a lower fee would be in the best interest of the fund.[336]

We also are proposing that when a money market fund's weekly liquid assets fall below 15% of total assets, the money market fund board would also have the ability to impose a temporary suspension of redemptions (also referred to as a ''gate'') for a limited period of time if the board determines that doing so is in the fund's best interest. Such a gate could be imposed, for example, if the liquidity fees were not proving sufficient in slowing redemptions to a manageable level.

Under this option, rule 2a–7 would continue to permit money market funds to use the penny rounding method of pricing so long as the funds complied with the conditions of the rule, but would not permit use of the amortized cost method of valuation. We would eliminate the use of the amortized cost method of valuation for money market funds under the fees and gates alternative for the same reasons we are proposing to do so under the retail and government exemptions to the floating NAV alternative.[337] We do not believe that allowing continued use of amortized cost valuation for all securities in money market funds' portfolios is appropriate given that these funds will already be valuing their securities using market factors on a daily basis due to new Web site disclosure requirements and given that penny rounding otherwise achieves the same level of price stability.

As previously discussed, the financial crisis of 2007–2008 exposed contagion effects from heavy redemptions in money market funds that had significant impacts on investors, funds, and the markets. We have designed the fees and gates alternative to address certain of these issues. Although it is impossible to know what exactly would have happened if money market funds had operated with fees and gates at that time, we expect that if money market funds were armed with such tools, they would have been able to better manage the heavy redemptions that occurred and to limit the spread of contagion, regardless of the reason for the redemptions.

During the crisis, some investors redeemed at the first sign of market stress, and could do so without bearing any costs even if their actions imposed costs on the fund and the remaining shareholders. As discussed in greater detail below, if money market funds had imposed liquidity fees during the crisis, it could have resulted in those investors re-assessing their redemption decisions because they would have been required to pay for the costs of their redemptions. Based on the level of redemption activity that occurred during the crisis, we expect that many money market funds would have faced liquidity pressures sufficient to cross the liquidity thresholds we are proposing today that would trigger the use of fees and gates. If funds therefore had imposed fees, this might have caused some investors to choose not to redeem because the direct costs of the liquidity fee may have been more tangible than the uncertain possibility of potential future losses. In addition, funds that imposed fees would likely have been able to better manage the impact of the redemptions that investors submitted, and any contagion effects may have been limited, because the fees would have helped offset the costs of the liquidity provided to redeeming

predetermined date, and any new investments would have to be made in floating-NAV MMFs.'').

[335] *See* BlackRock FSOC Comment Letter, *supra* note 204 (''We agree that a transition period is extremely important to avoid market disruption. Assuming existing funds are grandfathered as CNAV funds and no new shares are purchased, a transition period of two years from the effective date of a new rule should suffice.''); HSBC FSOC Comment Letter, *supra* note 196 (''[W]e believe a 2–3 year transition period should be sufficient for the industry, investors and regulators to prepare for any required changes to products, systems etc.''). *But see* U.S. Chamber Jan. 23, 2013 FSOC Comment Letter, *supra* note 248 (suggesting a transition period of up to 5 years could be necessary).

[336] We would not require, but would permit, government funds to impose fees and gates, as discussed below. Unlike under the floating NAV alternative, we are not proposing to exempt retail funds from our fees and gates proposal. *See infra* section III.B.5 of this Release.

[337] *See* section III.A.3 and III.A.4 of this Release.

shareholders, and any excess could have been used to repair the NAV of the fund, if necessary. Regardless of the incentives to redeem, a liquidity fee would make redeeming investors pay for the costs of liquidity and, even if investors redeem from a fund, gates can directly respond to a run by halting redemptions.

If a fund had been able to impose a redemption gate at the time, it also would have been able to stop mounting redemptions and possibly generate additional internal liquidity in the fund while the gate was in place. However, fees and gates do not address all of the factors that may lead to heavy redemptions in money market funds.[338] For example, they do not eliminate the incentive to redeem in times of stress to receive the $1.00 stable share price before the fund breaks the buck, or prevent investors from seeking to redeem to obtain higher quality securities, better liquidity, or increased transparency. Nonetheless, for the reasons discussed above, they provide tools that should serve to address many of the types of issues that arose during the crisis by allocating more explicitly the costs of liquidity and stopping runs.

As discussed in section III.C, we also request comment on whether we should combine this option with our floating NAV alternative. This reform would be intended to achieve our goals of preserving the benefits of stable share price money market funds for the widest range of investors and the availability of short-term financing for issuers, while enhancing investor protection and risk transparency, making funds more resilient to mass redemptions, and improving money market funds' ability to manage and mitigate potential contagion from high levels of redemptions, as further discussed below.

1. Analysis of Certain Effects of Liquidity Fees and Gates

As discussed in the RSFI Study and in section II above, shareholders may redeem money market fund shares for several reasons under stressed market conditions.[339] One of these incentives relates to the current rounding convention in money market fund valuation and pricing that can allow early redeeming shareholders to redeem for $1.00 per share, even when the market-based NAV per share of the fund is lower than that price. As discussed in section III.A above, the floating NAV proposal is principally focused on mitigating this incentive by causing redeeming shareholders to receive the market value of redeemed shares. However, as the RSFI Study details, there are a variety of other factors that may motivate shareholders to redeem assets from money market funds in times of stress. Adverse economic events or financial market conditions can cause shareholders to engage in flights to quality, liquidity, or transparency (or combinations thereof).[340] When money market funds may have to absorb, suddenly, high levels of redemptions that are expected to be in excess of the fund's internal sources of liquidity, investors may expect that fund managers will deplete the fund's most liquid assets first to meet redemptions and may have to sell securities at a loss (because of transitory liquidity costs) or even ''fire sale'' prices.[341] Accordingly, shareholder redemptions during such periods can impose expected future liquidity costs on the money market fund that are not reflected in a $1.00 share price based on current amortized cost valuation.

Because the circumstances under which liquidity becomes expensive historically have been infrequent, we expect that liquidity fees only will be imposed when the fund's board of directors considers the fund's liquidity costs to be at a premium and the liquidity fee, if imposed, will apply only to those shareholders who redeem and cause the fund to incur that cost. Under normal market conditions, fund shareholders would continue to enjoy unfettered liquidity for money market fund shares.[342] As such, liquidity fees are designed to preserve the current benefits of principal stability, liquidity, and a market yield under most market conditions, but reduce the likelihood that ''when markets are dislocated, costs that ought to be attributed to a redeeming shareholder are externalized on remaining shareholders and on the wider market.'' [343]

In addition to liquidity fees, our proposal also would allow money market funds to impose redemption gates after the liquidity threshold is reached. Our proposal on liquidity fees and gates, however, could affect shareholders by potentially limiting the full, unfettered redeemability of money market fund shares under certain conditions, a principle embodied in the Investment Company Act.[344] Currently, a money market fund generally can suspend redemptions only [345] after obtaining an exemptive order from the Commission or in accordance with rule 22e–3, which requires the fund's board of directors to determine that the fund is about to ''break the buck''

[338] *See infra* nn 361 and 362 and accompanying text.

[339] *See* RSFI Study, *supra* note 21, at 2–4.

[340] *See id.* at 7–14; Qi Chen et al., *Payoff Complementarities and Financial Fragility: Evidence from Mutual Fund Outflows,* 97 J. Fin. Econ. 239–262 (2010). Prime money market funds can be particularly susceptible to redemptions in a flight to quality, liquidity or transparency because they hold similar portfolios and thus can present a correlated risk of loss of quality or loss of liquidity (and particularly when the financial system is strained because most of their non-governmental assets are short-term debt obligations of large banks.) *See infra* section III.J. *See also* Harvard Business School FSOC Comment Letter, *supra* note 24; Angel FSOC Comment Letter, *supra* note 60.

[341] *See, e.g.,* Comment Letter of Americans for Financial Reform (Feb. 20, 2012) (available in File No. FSOC–2012–0003); BlackRock FSOC Comment Letter, *supra* note 204; Philip E. Strahan & Basak Tanyeri, *Once Burned, Twice Shy: Money Market Fund Responses to a Systemic Liquidity Shock,* Boston College Working Paper (July 2012) (finding that in response to the September 2008 run on money market funds, the funds first responded by selling their safest and most liquid holdings). *See also* Stephan Jank & Michael Wedow, *Sturm und Drang in Money Market Funds: When Money Market Funds Cease to be Narrow, Deutsche Bundesbank Discussion Paper No. 20/2008* (finding that German money market funds enhanced their yield by investing in less liquid securities in the lead up to the 2007–2008 subprime crisis, but then experienced runs during the crisis, while more liquid money market funds functioned as a safe haven). We note that other mutual funds also may tend to deplete their most liquid assets first to meet redemptions, but the incentive to redeem because of the potential for declining fund liquidity may be stronger in money market funds because of their use as a cash management vehicle and the resulting heightened sensitivity to potential losses.

[342] *See* Comment Letter of J.P. Morgan Asset Management (Jan. 14, 2013) (available in File No. FSOC–2012–0003) (''J.P. Morgan FSOC Comment Letter'') (''the standby character of [fees and gates] proposals appropriately balances the goal of allowing MMFs to operate normally when not under stress, yet promote stability, flexibility and reasonable fairness when stressed.''); Comment Letter of Wells Fargo Funds Management, LLC (Jan. 17, 2013) (available in File No. FSOC–2012–0003) (''Wells Fargo FSOC Comment Letter'') (stating that standby fees and gates are narrowly tailored, ''imposed to address [run risk] while preserving money market funds' key attributes'').

[343] HSBC Global Asset Management, *Liquidity Fees; a proposal to reform money market funds* (Nov. 3, 2011) (''HSBC 2011 Liquidity Fees Paper'').

[344] Section III.B.3 *infra* discusses the rationale for the exemptions from the Investment Company Act and related rules proposed to permit money market funds to impose standby liquidity fees and gates.

[345] There are limited exceptions specified in section 22(e) of the Act in which a money market fund (and any other mutual fund) may suspend redemptions, such as (i) for any period (A) during which the New York Stock Exchange is closed other than customary week-end and holiday closings or (B) during which trading on the New York Stock Exchange is restricted, or (ii) during any period in which an emergency exists as a result of which (A) disposal by the fund of securities owned by it is not reasonably practical or (B) it is not reasonably practical for the fund to determine the value of its net assets. The Commission also has granted orders in the past allowing funds to suspend redemptions. *See, e.g.,* In the Matter of The Reserve Fund, Investment Company Act Release No. 28386 (Sept. 22, 2008) [73 FR 55572 (Sept. 25, 2008)] (order); Reserve Municipal Money-Market Trust, et al., Investment Company Act Release No. 28466 (Oct. 24, 2008) [73 FR 64993 (Oct. 31, 2008)] (order).

(specifically, that the extent of deviation between the fund's amortized cost price per share and its current market-based net asset value per share may result in material dilution or other unfair results to investors).[346] Under our proposal, a money market fund board could decide to temporarily suspend redemptions once it had crossed the same thresholds that can trigger the imposition of a liquidity fee.[347] The fund could use such a gate to assess the viability of the fund, to create a ''circuit breaker'' giving time for a market panic to subside, or to create ''breathing room'' to permit more fund assets to mature and provide internal liquidity to the fund.[348] In the 2009 Proposing Release, we requested comment on whether we should include a provision in rule 22e–3 that would permit fund directors to temporarily suspend redemptions during certain exigent circumstances.[349] Many commenters on our 2009 Proposing Release supported our permitting such a temporary suspension of redemptions.[350]

We are proposing a combination of liquidity fees and gates because we believe that liquidity fees and gates, while both aimed at helping funds better and more systematically manage high levels of redemptions, do so in different ways and thus with somewhat different tradeoffs. Liquidity fees are designed to reduce shareholders' incentives to redeem when it is abnormally costly for the fund to provide liquidity by requiring redeeming shareholders to bear at least some of the liquidity costs of their redemption (rather than transferring those costs to remaining shareholders).[351] To the extent that liquidity fees paid exceed such costs, they also can help increase the fund's net asset value for remaining shareholders which would have a restorative effect if the fund has suffered a loss. As one commenter has said, a liquidity fee can ''provide a strong disincentive for investors to make further redemptions by causing them to choose between paying a premium for current liquidity or delaying liquidity and benefitting from the fees paid by redeeming investors.'' [352] This explicit pricing of liquidity costs in money market funds could offer significant benefits to such funds and the broader short-term financing market in times of potential stress by lessening both the frequency and effect of shareholder redemptions.[353] Unlike liquidity fees, gates are designed to halt a run by stopping redemptions long enough to allow (1) fund managers time to assess the appropriate strategy to meet redemptions, (2) liquidity buffers to grow organically as securities mature, and (3) shareholders to assess the level of liquidity in the fund and for any shareholder panic to subside. We also note that gates are the one regulatory reform discussed in this Release and the FSOC Proposed Recommendations that definitively stops a run on a fund (by blocking all redemptions).

Fees and gates also may have different levels of effectiveness under different stress scenarios. For example, we expect that liquidity fees will be able to reduce the harm to non-redeeming shareholders and the broader markets when a fund faces heavy redemptions during periods in which its true liquidity costs are less than the fund's imposed liquidity fee. Redemptions during this time will increase the value of the fund, which, in turn, will stabilize the fund to the extent remaining shareholders' incentive to redeem shares is decreased. However, it is possible that liquidity fees might not be fully effective during periods of systemic crises because, for example, shareholders might choose to redeem from money market funds irrespective of the level of a fund's true liquidity costs and imposition of the liquidity fee.[354] In those cases, gates could function as useful circuit breakers, allowing the fund time to rebuild its own internal liquidity and shareholders to pause to reconsider whether a redemption is warranted.

Finally, research in behavioral economics suggests that liquidity fees may be particularly effective in dampening a run because, when faced with two negative options, investors tend to prefer possible losses over certain losses, even when the amount of possible loss is significantly higher than the certain loss.[355] Unlike gates, when a liquidity fee is imposed, investors would make an economic decision over whether to redeem. Therefore, under this behavioral economic theory, investors fearing that a money market fund may suffer losses may prefer to stay in the money market fund and avoid payment of the liquidity fee (despite the possibility that the fund might suffer a future loss) rather than redeem and lock in payment of the liquidity fee.

We are proposing a combination of fees and gates, with a fee as the initial default but with an optional ability for a fund's board to replace the fee with a gate, or impose a gate immediately, in each case as the board deems best for the fund.[356] We are proposing this structure as the initial default (rather than imposing a gate as the default) because we believe that a fee has the potential to be less disruptive to fund shareholders and the short-term financing markets because a fee allows fund shareholders to continue to transact in times of stress (although at a cost).[357] At the same time, if the board

[346] Rule 22e–3(a)(1).

[347] *See* proposed (Fees & Gates) rule 2a–7(c)(2)(ii).

[348] *See, e.g.,* Angel FSOC Comment Letter, *supra* note 60 (''gates that limit MMMF redemptions to the natural maturity of the MMMF portfolios can prevent the forced selling of assets and transform a disorderly run into an orderly walk to quality''); ICI Jan. 24 FSOC Comment Letter, *supra* note 25 (noting that a gate provides time for the fund to rebuild its liquidity as portfolio securities mature).

[349] Being able to impose a temporary suspension of redemptions to calm instances of heightened redemptions had been recommended by an industry report. ICI 2009 Report, *supra* note 56, at 85–89 (recommending that the Commission permit a fund's directors to suspend temporarily the right of redemption if the board, including a majority of its independent directors, determines that the fund's net asset value is ''materially impaired'').

[350] *See, e.g.,* Comment Letter of Charles Schwab Investment Management, Inc. (Sept. 4, 2009) (available in File No. S7–11–09) (''Schwab 2009 Comment Letter''); Comment Letter of the Dreyfus Corporation (Sept. 8, 2009) (available in File No. S7–11–09) (''Dreyfus 2009 Comment Letter''); Comment Letter of Federated Investors, Inc. (Sept. 8, 2009) (available in File No. S7–11–09); T. Rowe Price 2009 Comment Letter, *supra* note 208. One commenter opposed the Commission permitting a temporary suspension of redemptions. *See* Comment Letter of Fund Democracy and the Consumer Federation of America (Sept. 8, 2009) (available in File No. S7–11–09) (stating that such a ''free time-out provision would increase incentives to run for the exits before the fund is closed and virtually guarantee that, once the fund was reopened, a flood of redemptions will follow. The provision provides a potential escape valve that will reduce fund managers' incentives to protect the fund's NAV. The provision provides virtually no benefit to shareholders while serving primarily to protect fund managers' interests.'').

[351] *See, e.g.,* Wells Fargo FSOC Comment Letter, *supra* note 342 (stating that a standby liquidity fee would ''provide an affirmative reason for investors to avoid redeeming from a distressed fund'' and ''those who choose to redeem in spite of the liquidity fee will help to support the fund's market-based NAV and thus reduce or eliminate the potential harm associated with the timing of their redemptions to other remaining investors'').

[352] *See* ICI Jan. 24 FSOC Comment Letter, *supra* note 25.

[353] We note that investors owning securities directly—as opposed to through a money market fund—naturally bear these liquidity costs. They bear these costs both because they bear any losses if they have to sell a security at a discount in times of stress to obtain their needed liquidity and because they directly bear the risk of a less liquid investment portfolio if they sell their most liquid holdings first to obtain needed liquidity.

[354] *See* RSFI Study, *supra* note 21, at 7–14 (discussing different possible explanations for why shareholders may redeem from money market funds in times of stress).

[355] *See, e.g.,* Daniel Kahneman, Thinking, Fast and Slow (2011), at 278–288.

[356] *See* proposed (Fees & Gates) rule 2a–7(c)(2).

[357] *See, e.g.,* Comment Letter of UBS on the IOSCO Consultation Report on Money Market Fund Systemic Risk Analysis and Reform Options (May 25, 2012), *available at http://www.iosco.org/library/pubdocs/pdf/IOSCOPD392.pdf*) (''UBS IOSCO Comment Letter'') (''we are convinced that [partial

determines that a fee is insufficient to protect the interests of non-redeeming shareholders, it still has the option of imposing a gate (and perhaps later lifting the gate, but keeping in place the fee).

Many participants in the money market fund industry have expressed support for imposing some form of a liquidity fee or gate on redeeming money market fund investors when the fund comes under stress as a way of reducing, in a targeted fashion, the fund's susceptibility to heavy redemptions.[358] Liquidity fees and gates are known to be able to reduce incentives to redeem,[359] and they have been used successfully in the past by certain non-money market fund cash management pools to stem redemptions during times of stress.[360]

We recognize that the prospect of a fund imposing a liquidity fee or gate could raise a concern that shareholders will engage in preemptive redemptions if they fear the imminent imposition of fees or gates (either because of the fund's situation or because such redemption restrictions have been triggered in other money market funds).[361] We expect the opportunity for preemptive redemptions will decrease as a result of the amount of discretion fund boards would have in imposing liquidity fees and gates, because shareholders would not be able to accurately predict when, and under what circumstances, fees and gates may be imposed.[362] Shareholders also might rationally choose to follow other shareholders' redemptions even when those other shareholders' decisions are not necessarily based on superior private information.[363] General stress in the short-term markets or fears of stress at a particular fund could trigger redemptions as shareholders try to avoid the fee.

While we acknowledge that liquidity fees may not always preclude redemptions, fees are designed so that as redemptions begin to increase, if liquidity costs exceed the prescribed threshold for imposing a fee and the fund imposes a fee, the run will be halted. The fees, once imposed, should both curtail the level of redemptions, and fees paid by those that do redeem should, at least partially, cover liquidity costs incurred by funds and may even potentially repair the NAV of any funds that have suffered losses. One

single swinging pricing] is more efficient than gates as prices are more efficient signals of scarcity than quantitative rationing''); Comment Letter of BNP Paribas on the IOSCO Consultation Report on Money Market Fund Systemic Risk Analysis and Reform Options (May 25, 2012), *available at http://www.iosco.org/library/pubdocs/pdf/IOSCOPD392.pdf* (''BNP Paribas IOSCO Comment Letter'') (''It would not make sense to restrict the redeemer willing to pay the price of liquidity.'').

[358] *See, e.g.,* BlackRock FSOC Comment Letter, *supra* note 204; J.P. Morgan FSOC Comment Letter, *supra* note 342; Northern Trust FSOC Comment Letter, *supra* note 174; Comment Letter of the Securities Industry and Financial Markets Association (''SIFMA'') (Jan. 14, 2013) (available in File No. FSOC–2012–0003) (''SIFMA FSOC Comment Letter''); Vanguard FSOC Comment Letter, *supra* note 172. *See also* David M. Geffen & Joseph R. Fleming, *Dodd-Frank and Mutual Funds: Alternative Approaches to Systemic Risk,* Bloomberg Law Reports (Jan. 2011) (''The alternative suggested here is that, during a period of illiquidity, as declared by a money market fund's board (or, alternatively, the SEC or another designated federal regulator), a money market fund may impose a redemption fee on a large share redemption approximately equal to the cost imposed by the redeeming shareholder and other redeeming shareholders on the money market fund's remaining shareholders. . . . The redemption fee causes the large redeeming shareholder to internalize the cost of the negative externality that the redemption otherwise would impose on non-redeeming shareholders.''). *But see, e.g.,* Comment Letter of the U.S. Chamber of Commerce on the IOSCO Consultation Report on Money Market Fund Systemic Risk Analysis and Reform Options (May 24, 2012), *available at http://www.iosco.org/library/pubdocs/pdf/IOSCOPD392.pdf* (''Imposing a liquidity fee is akin to implementing a variable NAV, and as such, would preclude a number of companies from investing in money market mutual funds. Although the liquidity fee may not be imposed until the fund's portfolio falls below a specified threshold or when there is a high volume of redemptions, corporate treasurers have an obligation to ensure that ''a dollar in will be a dollar out'' and therefore, will not risk investing cash in an investment product that may not return 100 cents on the dollar.''); Comment Letter of Federated Investors, Inc. on the IOSCO Consultation Report on Money Market Fund Systemic Risk Analysis and Reform Options (May 25, 2012) *available at http://www.iosco.org/library/pubdocs/pdf/IOSCOPD392.pdf* (''Federated IOSCO Comment Letter'') (''Federated believes that liquidity fees . . . are simply a different way to break the dollar . . . and would generate large preemptive redemptions from MMFs'').

[359] *Cf.* G.W. Schwert & P.J. Seguin, *Securities Transaction Taxes: An Overview of Costs, Benefits and Unresolved Questions,* 49 Financial Analysts Journal 27 (1993); K.A. Froot & J. Campbell, *International Experiences with Securities Transaction Taxes,* in The Internationalization of Equity Markets (J. Frankel, ed., 1994), at 277–308.

[360] A Florida local government investment pool experienced a run in 2007 due to its holdings in SIV securities. The fund suspended redemptions and ultimately reopened but after the fund (and each shareholder's interest) had been split into two separate funds: One holding the more illiquid securities previously held by the pool (called ''Fund B'') and one holding the remaining securities of the fund. Fund B reopened with a 2% redemption fee and did not generate a run upon its reopening. *See* David Evans and Darrell Preston, *Florida Investment Chief Quits; Fund Rescue Approved,* Bloomberg (Dec. 4, 2007); Helen Huntley, *State Wants Fund Audit,* Tampa Bay Times (Dec. 11, 2007). Some European enhanced cash funds also successfully used fees or gates during the financial crisis to stem redemptions. *See* Elias Bengtsson, *Shadow Banking and Financial Stability: European Money Market Funds in the Global Financial Crisis* (2011) (''Bengtsson''), *available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1772746&download=yes*; Julie Ansidei, et al., *Money Market Funds in Europe and Financial Stability,* European Systemic Risk Board Occasional Paper No. 1, at 36 (June 2012), *available at http://www.esrb.europa.eu/pub/pdf/occasional/20120622_occasional_paper.pdf.*

[361] *See, e.g.,* FSOC Proposed Recommendations, *supra* note 114, at 62–63; Harvard Business School FSOC Comment Letter, *supra* note 24 (''news that one MMF has initiated redemption restrictions could set off a system-wide run by panic-stricken investors who are anxious to redeem their shares before other funds also initiate restrictions''); Comment Letter of The Systemic Risk Council (Jan. 18, 2013) (available in File No. FSOC 2012–0003) (''Systemic Risk Council FSOC Comment Letter'') (stating that temporary gates or fees that come down in a crisis do not address the structural problem of the $1.00 NAV and would move up a run on money market funds). Empirical evidence in the equity and futures markets demonstrates that investors may trade in advance of circuit breakers being triggered so as to not be left in temporarily illiquid positions. Investors have been found to trade ahead of predictable market closings and price limit hits. Empirical studies document trading pressure before trading halts. *See* Y. Amihud & H. Mendelson, *Trading Mechanisms and Stock Returns: An Empirical Investigation,* 42 J. Fin. 533–553 (1987); Y. Amihud & H. Mendelson, *Volatility, Efficiency and Trading: Evidence from the Japanese Stock Market,* 46 J. Fin. 1765–1789 (1991); H.R. Stoll & R. E. Whaley, *Stock Market Structure and Volatility,* 3 Review of Financial Studies 37–71 (1990); M.S. Gerety & J.H. Mulherin, *Trading Halts and Market Activity: An Analysis of Volume at the Open and the Close,* 47 J. Fin. 1765–1784 (1992). Empirical studies show trading volume accelerates before a price limit hits. *See* Y. Du, et al., *An Analysis of the Magnet Effect under Price Limits,* 9 International Review of Fin. 83–110 (2009); G.J. Kuserk & P.R. Locke, *Market Making With Price Limits,* 16 J. Futures Markets 677–696 (1996). An experimental study finds that mandated market closures accelerate trading activity when an interruption is imminent. *See* L.F. Ackert, et al., *An Experimental Study of Circuit Breakers: The Effects of Mandated Market Closures and Temporary Halts on Market Behavior,* 4 J. Financial Markets 185–208 (2001). Empirical studies report trading volume increases following trading halts and price limit hits. *See, e.g.,* S.A. Corwin & M.L. Lipson, *Order Flow and Liquidity around NYSE Trading Halts,* 55 J. Fin. 1771–1801 (2000); W.G. Christie, et al., *Nasdaq Trading Halts: The Impact of Market Mechanisms on Prices, Trading Activity, and Execution Costs,* 57 J. Fin. 1443–1478 (2002); and C.M.C. Lee, et al., *Volume, Volatility, and New York Stock Exchange Trading Halts,* 49 J. Fin. 183–213 (1994). *See also* K.A. Kim & S.G. Rhee, *Price Limit Performance: Evidence from the Tokyo Stock Exchange,* 52 J. Fin. 885–901 (1997).

[362] *See* A. Subrahmanyam, *On Rules Versus Discretion in Procedures to Halt Trade,* 47 J. Economics and Business 1–16 (1995); A. Subrahmanyam, *The Ex-Ante Effects of Trade Halting Rules on Informed Trading Strategies and Market Liquidity,* 6 Rev. Financial Economics 1–14 (1997).

[363] Theoretical models show investors may rationally follow others' actions, even though these other investors' decisions are not necessarily based on superior private information. *See* S. Bikhchandani, et al., *A Theory of Fads, Fashion, Custom, and Cultural Change as Informational Cascades,* 100 J. Pol. Econ. 992–1026 (1992); I. Welch, *Sequential Sales, Learning, and Cascades,* 47 J. Fin. 695–732 (1992). Experimental data demonstrates investors may overreact to uninformative trades. *See* C. Camerer & K. Weigelt, *Information Mirages in Experimental Asset Markets,* 64 J. Bus. 463–493 (1991). Price limits, which are loosely akin to trading suspensions, may help to protect markets from destabilizing trades. *See* F. Westerhoff, *Speculative markets and the effectiveness of price limits,* 28 J. Econ. Dynamics and Control 493–508 (2003).

circumstance under which liquidity fees would not self-correct is if the amount of the fee is less than or exactly equal to the fund's realized liquidity costs. Gates would not be self-correcting in the event of realized portfolio losses, but they can help the fund preserve assets and generate more internal liquidity as assets mature. Some commenters have considered whether liquidity fees and gates might precipitate a run. For example, some commenters have expressed their view that a liquidity fee or gate would not accelerate a run, stating that such redemptions would likely trigger the fee or gate and that, once triggered, the fee or gate would then lessen or halt redemptions.[364] Even if investors have an incentive to redeem, their redemptions eventually will cause a fee or gate to come down and halt the run.

Under this proposal, money market funds would have the benefit of being able to use the penny rounding method of pricing for their portfolios. As discussed further below in section III.F.4 and III.F.5, they would also have to provide much fuller transparency of the market-based NAV per share of the funds and the marked-based value of the funds' portfolio securities. This increased transparency is designed to allow better shareholder understanding of deviations between the fund's value using market-based factors and its stable price. It also is aimed at helping investors better understand any risk involved in money market fund investments as a result of rule 2a–7's rounding convention. However, retaining these valuation and pricing methods for money market funds does not eliminate the ability of investors to redeem ahead of other investors from a money market fund that is about to ''break the buck'' and consequently may permit those early redeemers to receive $1.00 per share instead of its market value as discussed in section III.A above. Nevertheless, in times of fund or market stress the fund is likely to impose either liquidity fees or gates, which will limit the ability of redeeming shareholders to receive more than their pro-rata share of the market-based value of the fund's assets.

Requiring that boards impose liquidity fees absent a finding that the fee is not in the best interest of the fund, and permitting them to impose gates once the fund has crossed certain thresholds could offer advantages to the fund in addition to better and more systematically managing liquidity and redemption activity. They could provide fund managers with a powerful incentive to carefully monitor shareholder concentration and shareholder flow to lessen the chance that the fund would have to impose liquidity fees or gates in times of market stress (because larger redemptions are more likely to cause the fund to breach the threshold). Such a requirement also could encourage portfolio managers to increase the level of daily and weekly liquid assets in the fund, as that would tend to lessen the likelihood of a liquidity fee or gate being imposed.[365] Further, because our proposal provides the board discretion not to impose the liquidity fee (or to impose a lower liquidity fee) and gives boards the option to impose gates, the boards of directors can impose fees or gates when the board determines that it is in the best interest of the fund to do so.

The prospect of facing fees and gates when a fund is under stress serves to make the risk of investing in a money market fund more transparent and to better inform and sensitize investors to the inherent risks of investing in money market funds. Fees and gates also could encourage shareholders to monitor and exert market discipline over the fund to reduce the likelihood that either the imposition of fees or gates will become necessary in that fund.[366] An additional benefit to the board's determination of liquidity fees and gates is that they create an incentive for money market fund managers to better and more systemically manage redemptions in all market conditions.[367]

Our proposal on liquidity fees and gates, however, could affect shareholders by potentially limiting the full, unfettered redeemability of money market fund shares under certain conditions, a principle embodied in the Investment Company Act.[368] Thus, this alternative, if adopted, could result in some shareholders redeeming their money market fund shares and moving their assets to alternative products (or government money market funds) out of concern that the *potential* imposition of a liquidity fee or gate could make investment in a money market fund less attractive due to less certain liquidity.[369] We also recognize that the imposition of a gate may affect the efficiency of money market fund shareholders' investment allocations and have corresponding impacts on capital formation if the redemption

[364] *See, e.g.,* HSBC EC Letter, *supra* note 156 (''Some commentators have objected that a trigger-based liquidity fee would cause investors to seek to redeem prior to the imposition of the fee. We disagree with this argument, which misunderstands the cause of investor redemptions. . . . A liquidity fee would be imposed *as a consequence of* investors' loss of confidence/flight to quality. It could not, therefore, be the cause of investors' loss of confidence/flight to quality.'') (emphasis in original); J.P. Morgan FSOC Comment Letter, *supra* note 342 (standby liquidity fees ''do not prevent an initial run, but they do provide a useful tool to slow a run after one has begun''); SIFMA FSOC Comment Letter, *supra* note 358 (''the operation of the proposed gate and liquidity fee themselves will stem any exodus and damper its effect''); Wells Fargo FSOC Comment Letter, *supra* note 342 (''To the extent that investor redemptions made for the purpose of avoiding a liquidity fee have the effect of accelerating a run . . . the redemption gate and liquidity fee apply an equally strong countermeasure. First, the redemption gate would halt the run, and second, the ensuing imposition of liquidity fees would either cause further redemption activity to cease or monetize further redemptions into transactions that are accretive, rather than dilutive, to a fund's market-to-market NAV. The redemption gate and liquidity fee operate to effectively reverse and repair any accelerated redemption activity the existence of the liquidity fee might otherwise induce. Redemption gates and liquidity fee mechanisms applying to all other money market funds would also mitigate any contagion risk.'').

[365] *See, e.g.,* Vanguard FSOC Comment Letter, *supra* note 172 (a standby liquidity fee along with daily disclosure of the fund's liquidity levels ''will serve as an effective tool to force investment advisors, particularly those managing funds with highly concentrated shareholder bases, to manage their funds with adequate liquidity to prevent the [standby liquidity fee] from ever being triggered'').

[366] *See, e.g.,* Vanguard FSOC Comment Letter, *supra* note 172 (a standby liquidity fee ''will encourage advisors and investors to self-police to avoid triggering the fee'').

[367] *See, e.g.,* HSBC 2011 Liquidity Fees Letter, *supra* note 343 (a liquidity fee ''will result in more effective pricing of risk (in this case, liquidity risk) . . . [and] act as a market-based mechanism for improving the robustness and fairness'' of money market funds); BlackRock FSOC Comment Letter, *supra* note 204 (''A fund manager will focus on managing both assets and liabilities to avoid triggering a gate. On the liability side, a fund manager will be incented to know the underlying clients and model their behavior to anticipate cash flow needs under various scenarios. In the event a fund manager sees increased redemption behavior or sees reduced liquidity in the markets, the fund manager will be incented to address potential problems as early as possible.'')

[368] Section III.B.3 *infra* discusses the rationale for the exemptions from the Investment Company Act and related rules proposed to permit money market funds to impose standby liquidity fees and gates.

[369] *See infra* section III.E for a discussion of the potential effects on money market fund investments and capital formation as a result of this alternative, if adopted. *See also* Comment Letter of Fidelity (Feb. 3, 2012) (available in File No. 4–619) (finding in a survey of their retail money market fund customers that 43% would stop using a money market fund with a 1% non-refundable redemption fee charged if the fund's NAV per share fell below $0.9975 and 27% would decrease their use of such a fund); Federated IOSCO Comment Letter, *supra* note 358 (stating that they anticipate ''that many investors will choose not to invest in MMFs that are subject to liquidity fees, and will redeem existing investments in MMFs that impose a liquidity fee'' but noting that ''[s]hareholder attitudes to redemption fees on MMFs are untested''). *But see* HSBC EC Letter, *supra* note 156 (''A liquidity fee [triggered by a fall in the fund's market-based NAV] should also be acceptable to investors, because it can be rationalized in terms of investor protection. (When we've presented the case for a liquidity fee in these terms to our investors, they have generally been receptive.)'').

restriction prevents shareholders from moving cash invested in money market funds to other investment alternatives that might be preferable at the time.

We request comment on our discussion of the economic basis and tradeoffs for this alternative.

• Would our proposal on liquidity fees and gates achieve our goals of preserving the benefits of stable share price money market funds for the widest range of investors and the availability of short-term financing for issuers while enhancing investor protection and risk transparency, making funds more resilient to mass redemptions and improving money market funds' ability to manage and mitigate potential contagion from high levels of redemptions? Are there other benefits that we have not identified and discussed?

• Would a liquidity fee provide many of the same potential benefits as the proposed floating NAV? If not, what are the differences in potential benefits? Would it result in a more effective pricing of liquidity risk into the funds' share prices and a fairer allocation of that cost among shareholders? Would a liquidity fee that potentially restores the fund's shadow price reduce some remaining shareholders incentive to redeem?

• Would the prospect of a fee or gate encourage investors to limit their concentration in a particular fund? Would an appropriately structured threshold for liquidity fees and gates provide an incentive for fund managers to monitor shareholder concentration and flows as well as portfolio composition to minimize the possibility of a fund applying a fee or gate? Would it encourage better board monitoring of the fund? Would it encourage shareholders to monitor and exert appropriate discipline over the fund? Would shareholders underestimate whether a fee or gate would ever be imposed by the board? How would the prospect of a fee or gate affect shareholder behavior?

• How will the liquidity fees or gates affect the fund's portfolio choices? Will it affect the way funds manage their weekly liquid assets?

• Funds currently have the ability to delay the payment of redemption proceeds for up to seven days.[370] Are there considerations that make funds hesitant to impose this delay that would also make funds hesitant to impose fees or gates? What are those factors?

• Would the expected imposition of a liquidity fee or gate increase redemption activity as the fund's liquidity levels near the threshold? Would the prospect of a liquidity fee or gate create an incentive to redeem during times of potential stress by shareholders fearing that such a fee or gate might be imposed, thus inciting a run? If so, do commenters agree that in such a case the redemptions would trigger a fee or gate and slow or halt redemptions? If not, are there ways in which we could modify our proposed threshold for liquidity fees and gates such that a run could not arise without triggering fees or gates? What information would be needed for investors to reliably predict that a fund is on the verge of imposing fees or gates? Would the necessary information be readily available under our proposal?

• Are some types of shareholders more likely than other types of shareholders to attempt to redeem in anticipation of the imposition of the fee or gate? Are there ways that we could reduce the risk of pre-emptive redemptions? Would imposition of a fee or gate as a practical matter lead to liquidation of that fund? If so, should this be a concern?

• Is penny rounding sufficient to allow government money market funds to maintain a stable price? Should we also permit these funds to use amortized cost valuation? If so, why?

• Should we prohibit advisers to money market funds from charging management fees while the fund is gated? How might this affect advisers' incentives to make recommendations to the board when it is considering whether to not impose a liquidity fee or gate?

We note that we are not proposing to repeal or otherwise modify rule 17a–9 (permitting sponsors to support money market funds through portfolio purchases in some circumstances) under this proposal. Therefore, money market fund sponsors would be able to continue to support the money market funds they manage by purchasing securities from money market fund portfolios at their amortized cost value (or market price, if greater). Instead, we are requiring greater and more timely disclosure of any sponsor support of a money market fund, as further described in section III.F.1 below. We note that some sponsors could use such support to prevent a money market fund from breaching a threshold that would otherwise require the board to consider imposition of a liquidity fee. Such support could benefit fund shareholders by preventing them from incurring the costs or loss of liquidity that a liquidity fee or gate may entail. However, because such support would be discretionary, its possibility may create uncertainty about whether fund investors will have to bear the costs and burdens of a liquidity fee or gate in times of stress, which could lead to unpredictable shareholder behavior and inefficient shareholder allocation of investments if their expectations of risk turn out to be misplaced. Our continuing to permit sponsor support of money market funds, albeit with greater transparency,[371] also could favor money market fund groups with a well-capitalized sponsor that is better able to provide discretionary support to its affiliated money market funds and thus avoid the imposition of fees or gates. Nonetheless, even the expectation of possible discretionary sponsor support may tend to slow redemptions. We request comment on the retention of rule 17a–9 under this proposal.

• Should we continue to allow this type of sponsor support of money market funds, given the enhanced transparency requirements? Would allowing sponsor support prevent or limit this proposal from achieving the goal of enhancing investor protection and improving money market funds' ability to manage high levels of redemptions? If so, how? Should we instead prohibit sponsor support under this option? If so, why? If we prohibited sponsor support, how would this advance investor protection if such support would protect the value or liquidity of the fund? Should we modify rule 17a–9 to limit or condition sponsor support?

• Would sponsors provide support to prevent a money market fund from breaching a liquidity threshold? Would sponsors be more willing and able to provide support to stabilize the fund under the liquidity fees and gates proposal than they were to support money market funds before the 2007–2008 financial crisis? Why or why not?

As discussed further below, we also are proposing to require that money market funds disclose their market-based NAVs and levels of daily and weekly liquid assets on a daily basis on the funds' Web sites.[372]

2. Terms of the Liquidity Fees and Gates

We are proposing that if a money market fund's weekly liquid assets fall or remain below 15% of its total assets at the end of any business day, the next business day it must impose a 2% liquidity fee on each shareholder's redemptions, unless the fund's board of directors (including a majority of its independent directors) determines that

[370] *See* section 22(e) of the Investment Company Act.

[371] *See infra* section III.F.

[372] *See infra* section III.F.

such a fee would not be in the best interest of the fund or determines that a lower fee would be in the best interest of the fund.[373] Any fee imposed would be lifted automatically once the money market fund's level of weekly liquid assets had risen to or above 30%, and it could be lifted at any time by the board of directors (including a majority of its independent directors) if the board determines to impose a different fee or if it determines that imposing the fee is no longer in the best interest of the fund.[374]

In addition, once the fund had crossed below the 15% threshold, the fund's board of directors (including a majority of its independent directors) would be able to temporarily suspend redemptions and gate the fund if the board determines that doing so is in the best interest of the fund.[375] Any gate imposed also would be automatically lifted once the fund's weekly liquid assets had risen back to or above 30% of its total assets (although the board of directors (including a majority of its independent directors) could lift the gate earlier.[376] Any money market fund that imposes a gate would need to lift that gate within 30 days and a money market fund could not impose a gate for more than 30 days in any 90-day period.[377] Under this proposal, we also would amend rule 22e–3 to permit the suspension of redemptions and liquidation of a money market fund if the fund's level of weekly liquid assets falls below 15% of its total assets.[378]

a. Discretionary Versus Mandatory Liquidity Fees and Gates

We are proposing a default liquidity fee that the money market fund's board of directors can modify or remove if it is in the best interest of the fund, because this structure offers the possibility of achieving many of the benefits of both fully discretionary and automatic (regulatory mandated) redemption restriction triggers. A purely discretionary trigger allows a fund board the flexibility to determine when a restriction is necessary, and thus allows tailoring of the triggering of the fee to the market conditions at the time, and the specific circumstances of the fund. However, a purely discretionary trigger creates the risk that a fund board may be reluctant to impose restrictions, even when they would benefit the fund and the short-term financing markets. They may not impose such restrictions out of fear that doing so signals trouble for the individual fund or fund complex (and thus may incur significant business and reputational effects) or could incite redemptions in other money market funds in anticipation that fees may be imposed in those funds as well. Fully discretionary triggers also provide shareholders with little advance knowledge of when such a restriction might be triggered and fund boards could end up applying them in a very disparate manner. Fully discretionary triggers also may present operational difficulties for fund managers who suddenly may need to implement a liquidity fee and may not have systems in place that can rapidly institute a fee whose trigger and size was previously unknown.

Automatic triggers set by the Commission may mitigate these potential concerns, but they create a risk of imposing costs on shareholders when funds are not truly distressed or when liquidity is not abnormally costly. Establishing thresholds that result in the imposition of a fee, unless the board makes a finding that such a fee is not in the best interest of the fund, balances these tradeoffs by providing some transparency to shareholders on potential fee or gate triggers and giving some guidance to boards on when a fee or gate might be appropriate. At the same time, it also allows boards to avoid imposing a fee or gate when it would be inappropriate in light of the circumstances of the fund and the conditions in the market.

Our proposed rule essentially creates a default liquidity fee of a pre-determined size, imposed when the fund's weekly liquid assets have dropped below a certain threshold. However, it provides the fund's board flexibility to alter the default option—for example, by imposing a gate instead of a fee or by imposing a fee at a different threshold or imposing a lower percentage fee—as long as it determines that doing so is in the best interest of the fund.

We request comment on our proposed default structure for the liquidity fees and gates.

- Should the imposition of a liquidity fee or gate be fully discretionary or should it have a completely automatic trigger? Why?
- Would a money market fund's board of directors impose a fully discretionary fee or gate during times of stress on the money market fund despite its possible unpopularity with investors and potential competitive disadvantage for the fund or fund group if other funds are not imposing a liquidity fee or gate? On the other hand, would a fund's board of directors be able to best determine when a fee or gate should be imposed rather than an automatic trigger?
- What operational complexities would be involved in a fully discretionary liquidity fee? Would fund complexes and their intermediaries be able to program systems in advance to accommodate the immediate imposition of a liquidity fee whose trigger and size were unknown in advance?

b. Threshold for Liquidity Fees and Gates

We are proposing that a liquidity fee automatically be imposed on money market fund redemptions if the fund's weekly liquid assets fall below 15% of its total assets, unless the fund's board of directors (including a majority of its independent directors) determines that a fee would not be in the best interest of the fund.[379] We also are proposing that, once the fund has crossed below this threshold, the money market fund board also would have the ability to impose a temporary gate for a limited period of time provided that the board of directors (including a majority of its independent directors) determines that imposing a gate is in the fund's best interest.[380] Any fee or gate imposed would be automatically lifted when the fund's weekly liquid assets had risen back to or above 30% of its total assets (although the board of directors (including a majority of its independent directors) could lift the fee or gate earlier if the board determined it was in the best interest of the fund.[381]

[373] Proposed (Fees & Gates) rule 2a–7(c)(2)(i). A ''business day,'' defined in rule 2a–7 as ''any day, other than Saturday, Sunday, or any customary business holiday,'' would end after 11:59 p.m. on that day. *See* rule 2a–7(a)(4). If the shareholder of record making the redemption was a direct shareholder (and not a financial intermediary), we would expect the fee to apply to that shareholder's net redemptions for the day. In order to provide the money market fund flexibility, if a liquidity fee were in place for more than one business day, the fund's board could vary the level of the liquidity fee (subject to the 2% limit) if the board determined that a different fee level was in the best interest of the fund. Proposed (Fees & Gates) rule 2a–7(c)(2)(i)(A). The new fee level would take effect the next business day following the board's determination. *Id.*

[374] Proposed (Fees & Gates) rule 2a–7(c)(2)(i)(B).

[375] The fund must reject any redemption requests it receives while the fund is gated. *See* proposed (Fees & Gates) rule 2a–7(c)(2)(ii).

[376] Proposed (Fees & Gates) rule 2a–7(c)(2)(ii).

[377] Proposed (Fees & Gates) rule 2a–7(c)(2)(ii). We also note that an adviser to a money market fund could seek an exemptive order from the Commission to allow for continued gating beyond 30 days if such gating would be necessary or appropriate in the public interest and consistent with the protection of investors and the purposes fairly intended by the policy and provisions of the Investment Company Act.

[378] *See* proposed (Fees & Gates) rule 22e–3.

[379] *See* proposed (Fees & Gates) rule 2a–7(c)(2)(i).

[380] *See* proposed (Fees & Gates) rule 2a–7(c)(2)(ii).

[381] Proposed (Fees & Gates) rule 2a–7(c)(2).

Our proposed 15% weekly liquid asset threshold is a default for money market funds imposing liquidity fees that requires the board to consider taking action. Fund boards of directors have the flexibility to impose a liquidity fee or gate if weekly liquid assets fall below this threshold (or they may determine not to impose a liquidity fee or gate at all), and can continue to reconsider their decision in light of new events as long as the fund is below this liquidity threshold.[382] Several industry commenters have recommended basing imposition of a liquidity fee on the money market fund's level of weekly liquid assets, with their proposed thresholds ranging from 7.5% to 15% of weekly liquid assets.[383] As shown in the chart below, our staff's analysis of Form N–MFP data shows that, between March 2011 and October 2012, there were two months in which funds reported weekly liquid assets below 15% (one fund in May 2011, and four funds in June 2011) and there were two months in which funds reported weekly liquid assets of at least 15% but below 20% (one fund in March 2011, and one fund in February 2012).

Fees and gates are a tool to mitigate problems in funds, so we selected a threshold that would indicate distress in a fund, but also one that few funds would cross in the ordinary course of business, allowing funds and their boards to avoid the costs of frequent unnecessary consideration of fees and gates. The analysis below shows that if the triggering threshold was between 25–30% weekly liquid assets, funds would have crossed this threshold every month except one during the period, and if it was set at between 20–25% weekly liquid assets, some funds would have crossed it nearly every other month. However, the analysis shows that funds rarely cross the threshold of between 15–20% weekly liquid assets during normal operations, and that during the time period analyzed, there were only 2 months that had any funds below the 15% weekly liquid assets threshold.

DISTRIBUTION OF WEEKLY LIQUID ASSETS IN PRIME MONEY MARKET FUNDS, MARCH 2011—OCTOBER 2012[384]

| Date | [0.00–0.05] | [0.05–0.10] | [0.10–0.15] | [0.15–0.20] | [0.20–0.25] | [0.25–0.30] | Total |
|---|---|---|---|---|---|---|---|
| Mar–11 | | | | 1 | 1 | 11 | 259 |
| Apr–11 | | | | | | 3 | 261 |
| May–11 | | 1 | | | 2 | 9 | 260 |
| Jun–11 | | | 4 | | 2 | 25 | 257 |
| Jul–11 | | | | | | 3 | 257 |
| Aug–11 | | | | | 3 | 10 | 256 |
| Sep–11 | | | | | | 5 | 256 |
| Oct–11 | | | | | 1 | 6 | 258 |
| Nov–11 | | | | | | 4 | 257 |
| Dec–11 | | | | | | 7 | 256 |
| Jan–12 | | | | | | 3 | 256 |
| Feb–12 | | | | 1 | | 2 | 255 |
| Mar–12 | | | | | | 5 | 251 |
| Apr–12 | | | | | | | 248 |
| May–12 | | | | | | 7 | 247 |
| Jun–12 | | | | | 1 | 4 | 245 |
| Jul–12 | | | | | 1 | 3 | 245 |
| Aug–12 | | | | | | 4 | 244 |
| Sep–12 | | | | | 1 | 6 | 241 |
| Oct–12 | | | | | | 2 | 241 |

Because the data on liquidity is reported at the end of the month, it could be the case that more than four money market funds' level of weekly liquid assets fell below 15% on other days of the month during our period of study. However, this number may overestimate the percentage of funds that are expected to impose a fee or gate because we expect that funds would increase their risk management around their level of weekly liquid assets in response to the fees and gates requirement to avoid breaching the liquidity threshold. Using this information to inform our choice of the appropriate level for a weekly liquid asset threshold, we are proposing a 15% weekly liquid assets threshold to balance the desire to have such consideration triggered while the fund still had liquidity reserves to meet redemptions but also not set the trigger at a level that frequently would be tripped by normal fluctuations in liquidity levels that typically would not indicate a fund under stress.

We are proposing to require that any fee or gate be lifted automatically once the fund's weekly liquid assets have risen back above 30% of the fund's assets—the minimum currently mandated under rule 2a–7—and thus a fee or gate would appear to be no longer justified. We considered whether a fee or gate should be lifted automatically before the fund's weekly liquid assets were completely restored to their required minimum—for example, once they had risen to 25%. However, we preliminarily believe that automatically removing such a restriction before the fund's level of weekly liquid assets was fully replenished may result in a fund being unable to maintain a liquidity fee or gate to protect the fund even when the fund is still under stress and before stressed market conditions have fully subsided. We note that a fund's board can always determine to lift a fee or gate before the fund's level of weekly liquid assets is restored to 30% of its assets.

There are a number of factors that a fund's board of directors may consider in determining whether to impose a liquidity fee once the fund's weekly liquid assets have fallen below 15% of its total assets. For example, it may want to consider why the level of weekly

[382] *See infra* text preceding n.385.

[383] *See, e.g.,* BlackRock FSOC Comment Letter, *supra* note 204 (recommending an automatic trigger of 15% weekly liquid assets); ICI Jan. 24 FSOC Comment Letter, *supra* note 25 (recommending an automatic trigger of between 7.5% and 15% weekly liquid assets); Vanguard FSOC Comment Letter, *supra* note 172 (recommending an automatic trigger of 15% weekly liquid assets).

[384] For purposes of our analysis, the monthly distribution of prime money market funds with weekly liquid assets above 30% is not shown.

liquid assets has fallen. Is it because the fund is experiencing mounting redemptions during a time of market stress or is it because a few large shareholders unexpectedly redeemed for idiosyncratic reasons unrelated to current market conditions? Another relevant factor to the fund board may be whether the fall in weekly liquid assets has been accompanied by a fall in the fund's shadow price. The fund board also may want to consider whether the fall in weekly liquid assets is likely to be very short-term. For example, will the fall in weekly liquid assets be cured in the next day or two when securities currently in the fund's portfolio qualify as weekly liquid assets? Many money market funds ''ladder'' the maturities of their portfolio securities, and thus it could be the case that a fall in weekly liquid assets will be rapidly cured by the portfolio's maturity structure.

We considered instead proposing a threshold based on the shadow price of the money market fund. For example, one money market fund sponsor has suggested that we require money market funds' boards of directors to consider charging a liquidity fee on redeeming shareholders if the shadow price of a fund's portfolio fell below a specified threshold.[385] This commenter asserted that such a trigger would ensure that shareholders only pay a fee when redemptions would actually cause the fund to suffer a loss and thus redemptions clearly disadvantage remaining shareholders. However, we are concerned that a money market fund being able to impose a fee only when the fund's shadow price has fallen by some amount below $1.00 in certain cases may come too late to mitigate the potential consequences of heavy redemptions and to fully protect investors. Heavy redemptions can impose adverse economic consequences on a money market fund even before the fund actually suffers a loss. They can deplete the fund's most liquid assets so that the fund is in a substantially weaker position to absorb further redemptions or losses. In addition, our proposed threshold is a default trigger for the liquidity fee—the board is not required to impose a liquidity fee when the fund's weekly liquid assets have fallen below 15%. Thus, a board can take into account whether the money market fund's shadow price has deteriorated in determining whether to impose a liquidity fee or gate when the fund's weekly liquid assets have fallen below the threshold. A threshold based on shadow prices also raises questions about whether and to what extent shareholders differentiate between realized (such as those from security defaults) and market-based losses (such as those from market interest rate changes) when considering a money market fund's shadow price. If shareholders do not redeem in response to market-based losses (as opposed to realized losses), it may be inappropriate to base a fee on a fall in the fund's shadow price if such a fall is only temporary. On the other hand, a temporary decline in the shadow price using market-based factors can lead to realized losses from a shareholder's perspective if redemptions cause a fund with an impaired NAV to ''break the buck.''

We also considered proposing a threshold based on the level of daily liquid assets rather than weekly liquid assets. We expect that a money market fund would meet heightened shareholder redemptions first by depleting the fund's daily liquid assets and next by depleting its weekly liquid assets, as daily liquid assets tend to be the most liquid. Accordingly, basing this threshold on weekly liquid assets thus provides a deeper picture of the fund's overall liquidity position, as a fund whose weekly liquid assets have fallen to 15% has likely depleted all of its daily liquid assets. In addition, a fund's levels of daily liquid assets may be more volatile because they are one of the first assets used to satisfy day-to-day shareholder redemptions, and thus more difficult to use as a gauge of true fund distress. Finally, as noted above, funds are able under the Investment Company Act to delay payment of redemption requests for up to seven days. Thus, substantial depletion of weekly liquid assets may be a better indicator of true fund distress. We also considered a trigger that would combine liquidity and market-based NAV thresholds but have preliminarily concluded that a single threshold would accomplish our goals without undue complexity and would be easier for investors to understand.

We request comment on our default threshold for liquidity fees and our threshold on when a money market fund's board may impose a gate.

- What should be the trigger either for a default liquidity fee or for a board's ability to impose a gate? Rather than our proposed trigger based on a fund's level of weekly liquid assets, should it be based on the fund's shadow price or its level of daily liquid assets? Should it be based on a certain fall in either the fund's weekly liquid assets or shadow price? Why and what extent of a fall? Should it be based on some other factor? Should it be based on a combination of factors?
- If we considered a threshold based on the fund's shadow price, do shareholders differentiate between realized and market-based losses (such as those from security defaults versus those from market interest rate changes) when considering a money market fund's shadow price? If so, how does it affect their propensity to redeem shares when one or more funds have losses?
- Should we permit a fund board to impose a liquidity fee or gate even before a fund passes the trigger requiring the default fee to be considered if the board determines that an early imposition of a liquidity fee or gate would be in the best interest of the fund? Would that reduce the benefits discussed above of having an automatic default trigger? What concerns would arise from permitting imposition of a fee or gate before a fund passes the thresholds we may establish?
- What extent of decline in weekly liquid assets should trigger consideration of a fee or gate and why? Should it be more or less than 15% weekly liquid assets, such as 10% or 20%?
- How do fund holdings of weekly liquid assets vary within the calendar month, between Form N–MFP filing dates? How do net shareholder redemptions vary within the calendar month, between Form N–MFP filing dates? How accurately can the fund forecast the net redemptions of its shareholders? When is the fund more likely to make forecasting errors?
- Should a liquidity fee or gate not be required until the fund suffers an actual loss in value? Why or why not and if so, how much of a loss in value?
- Is one type of threshold less susceptible to preemptive runs? If so, why?
- Are there other factors that a board might consider in determining whether to impose a fee or gate? Should we require that boards consider certain factors? If so, which factors and why?

c. Size of Liquidity Fee

We are proposing that the liquidity fee be set at a default rate of 2%, although a fund's board could impose a lower liquidity fee (or no fee at all) if it determines that a lower level is in the best interest of the fund.[386] Commenters have suggested that liquidity fee levels ranging from 1% to 3% could be effective.[387] We selected a default fee of

[385] HSBC FSOC Comment Letter, *supra* note 196 (suggesting setting the market-based NAV trigger at $0.9975).

[386] *See* proposed (Fees & Gates) rule 2a–7(c)(2)(i)(A).

[387] *See, e.g.,* Vanguard FSOC Comment Letter, *supra* note 172 (recommending a fee of between 1

2% because we believe that a liquidity fee set at this level is high enough that it may impose sufficient costs on redeeming shareholders to deter redemptions in a crisis, but is low enough to permit investors who wish to redeem despite the cost to receive their proceeds without bearing unwarranted costs.[388] A 2% level should also permit a fund to recoup the costs of liquidity it may bear, while repairing the fund if it has incurred losses.[389] We recognize that establishing any fixed fee level may not precisely address the circumstances of a particular fund in a crisis, and accordingly are proposing to make this 2% level a default, which a fund board may lower or eliminate in accordance with the circumstances of any individual fund.

We also considered whether we should require a liquidity fee with an amount explicitly tied to market indicators of changes in liquidity costs for money market funds. For example, one fund manager suggested that the amount of the liquidity fee charged could be based on the anticipated change in the market-based NAV of the fund's portfolio from the redemption, assuming a horizontal slice of the fund's portfolio was sold to meet the redemption request.[390] This firm asserted that such a liquidity fee would proportionately target the extent that the redemption was causing a material disadvantage to remaining investors in the fund and it would be clear to investors how the fee would advance investor protection.

There may be a number of drawbacks to such a ''market-sized'' liquidity fee, however. First, it does not provide significant transparency in advance to shareholders of the size of the liquidity fee they may have to pay in times of stress. It could also reduce the fees' efficacy in stemming redemptions if investors fear that the fee might go up in the future. This lack of transparency may hinder shareholders' ability to make well-informed decisions. It also may be difficult for money market funds to rapidly determine precise liquidity costs in times of stress when the short-term financing markets may be generally illiquid. Indeed, our staff gave no-action assurances to money market funds relating to valuation during the 2008 financial crisis because determining pricing in the then-illiquid markets was so difficult.[391] We also understand that a liquidity fee that is not fixed in advance and indeed may change from day-to-day may be considerably more difficult and expensive for money market funds to implement and administer from an operational perspective. Such a fee would require real-time inputs of pricing factors into fund systems that would need to be rapidly disseminated through chains of financial intermediaries in order to apply to daily redemptions from the large number of beneficial owners that hold money market fund shares through omnibus accounts. A floating fee would assume sale of a horizontal cross section of assets but we do not think that is how portfolio securities would be sold to meet redemptions.

These factors have led us to propose a default liquidity fee of a fixed size, but to allow the board of directors (including a majority of its independent directors) to impose a smaller-sized liquidity fee if it determines that such a smaller fee would be in the best interest of the fund.[392] We preliminarily believe that such a default may provide the best combination of directing boards of directors to a liquidity fee size that may be appropriate in many stressed market conditions, but providing flexibility to boards to lower the size of that liquidity fee if it determines that a smaller fee would better and more fairly estimate and allocate liquidity costs to redeeming shareholders. Some factors that boards of directors may want to consider in determining whether to impose a smaller-sized liquidity fee than 2% include the shadow price of the money market fund at the time, relevant market indicators of liquidity stress in the markets, changes in spreads for portfolio securities (whether based on actual sales, dealer quotes, pricing vendor mark-to-model or matrix pricing, or otherwise), changes in the liquidity profile of the fund in response to redemptions and expectations regarding that profile in the immediate future, and whether the money market fund and its intermediaries are capable of rapidly putting in place a fee of a different amount. We are not proposing to allow fund boards to impose a larger liquidity fee than 2% because we understand that, even in ''fire sales'' or other crisis situations, money market funds typically have not realized haircuts greater than 2% when selling portfolio securities, and believe that investors should not face unwarranted costs when redeeming their shares. In addition, the staff has noted in the past that fees greater than 2% raise questions regarding whether a fund's securities remain ''redeemable.''[393] If a fund continues to be under stress even with a 2% liquidity fee, the fund board may consider imposing a redemption gate or liquidating the fund pursuant to rule 22e–3.

We request comment on our proposed default size for the liquidity fee.

- What should be the amount of the liquidity fee? Should it be a default amount, a fixed amount, or an amount directly tied to the cost of liquidity in times of stress? If as proposed, we adopt a default fee, should it be 2%, 1%, or some other level? Should we give boards discretion to impose a higher fee if the board determines that it is in the best interest of the fund? Commenters are requested to please provide data to support your suggested fee level.
- If the amount of the liquidity fee is tied to the cost of liquidity at the time of the redemption, how would that

and 3%); BlackRock FSOC Comment Letter, *supra* note 204 (recommending a standby liquidity fee of 1%); ICI Jan. 24 FSOC Comment Letter, *supra* note 25 (recommending a 1% fee).

[388] *See, e.g.,* Vanguard FSOC Comment Letter, *supra* note 172 (''We believe a fee in this amount [1–3%] will serve as an adequate deterrent to investors who may attempt to flee a fund out of fear, but would still allow those investors who have a need to access their cash the ability to redeem a portion of their holdings.''); ICI Jan. 24 FSOC Comment Letter, *supra* note 25 (''A liquidity fee set at this level [1%] would discourage redemptions, but allow the fund to continue to provide liquidity to investors. . . . Investors truly in need of liquidity would have access to it, but at a pre-determined cost.'').

[389] *See, e.g.,* ICI Jan. 24 FSOC Comment Letter, *supra* note 25 (''Insofar as investors choose to redeem, the fee would benefit remaining shareholders by mitigating liquidation costs and potentially rebuilding NAVs.'').

[390] HSBC FSOC Comment Letter, *supra* note 196.

[391] *See* Investment Company Institute, SEC Staff No-Action Letter (Oct. 10, 2008) (not recommending enforcement action through January 12, 2009, if money market funds used amortized cost to shadow price portfolio securities with maturities of 60 days or less in accordance with Commission interpretive guidance and noting: ''You state that under current market conditions, the shadow pricing provisions of rule 2a–7 are not working as intended. You believe that the markets for short-term securities, including commercial paper, may not necessarily result in discovery of prices that reflect the fair value of securities the issuers of which are reasonably likely to be in a position to pay upon maturity. You further assert that pricing vendors customarily used by money market funds are at times not able to provide meaningful prices because inputs used to derive those prices have become less reliable indicators of price.'').

[392] *See* proposed (Fees & Gates) rule 2a–7(c)(2)(i).

[393] Section 2(a)(32) of the Act [15 U.S.C. 80a–2(a)(32)] defines the term ''redeemable security'' as a security that entitles the holder to receive approximately his proportionate share of the fund's net asset value. The Division of Investment Management informally took the position that a fund may impose a redemption fee of up to 2% to cover the administrative costs associated with redemption, ''but if that charge should exceed 2 percent, its shares may not be considered redeemable and it may not be able to hold itself out as a mutual fund.'' *See* John P. Reilly & Associates, SEC Staff No-Action Letter (July 12, 1979). This position is currently reflected in our rule 23c–3(b)(1) under the Act [17 CFR 270.23c–3(b)(1)], which permits a maximum 2% repurchase fee for interval funds and rule 22c–2(a)(1)(i) [17 CFR 270.22c–2(a)(1)(i)] which similarly permits a maximum 2% redemption fee to deter frequent trading in mutual funds.

amount be determined? Would a liquidity fee that changes depending on market circumstances provide shareholders with sufficient transparency on the size of the fee to be able to affect their purchase and redemption behavior? If the size of the liquidity fee changed depending on market circumstances, would money market funds be able to determine readily the amount of the liquidity fee during times of market dislocation? Would such a fee affect one type of investor more than another type of investor?

- Is a flat, fixed liquidity fee preferable to a variable fee that might be higher than the flat fee? Will the fund's ability to choose a lower liquidity fee result in any conflicts of interest between redeeming shareholders, non-redeeming shareholders, and the investment adviser?
- How should we weigh the risk that a flat liquidity fee may be higher or lower than the actual liquidity costs to the money market fund from the redemption, against the risk that a market-based liquidity fee may not provide sufficient advance transparency to shareholders and may be difficult to set appropriately in a crisis?
- How difficult would it be for money market funds and various intermediaries in the distribution chain of money market fund shares to handle from an operational perspective a liquidity fee that varied?

d. Default of Liquidity Fees

Our proposal provides that a liquidity fee be imposed once a non-government money market fund's weekly liquid assets has fallen below 15% of its total assets (which is one-half of its required 30% minimum), unless the board of directors determines that such a fee would not be in the best interest of the fund. After the fund has crossed that 15% liquidity threshold, the board could also impose a gate. Based on this default choice, the implicit ordering of redemption restrictions thus would be a liquidity fee, and if that fee is not sufficiently slowing redemptions, a gate (although once the liquidity fee threshold was crossed, a board would be able to immediately impose a gate instead of a fee). We proposed a liquidity fee, rather than a gate, as the default because we believe that a fee has the potential to be less disruptive to fund shareholders and the short-term financing markets because a fee allows fund shareholders to continue to transact in times of stress (although at a cost). Some industry commenters instead have suggested that money market funds impose a gate first.[394] Such a pause in redemption activity could provide time for any spike in redemptions to subside before redemptions were allowed with a fee. We request comment on liquidity fees being the default under this proposal.

- Should the implicit ordering in the proposed rule be reversed, with a default of the fund imposing a gate once the fund has crossed the weekly liquid asset threshold, unless or until the board determines to re-open with a liquidity fee? Why?
- Should there be a different threshold for consideration of a gate if we adopted a gate as the default? Why or why not? Should a gate be mandatory under certain circumstances? If so, under what circumstances? Should any mandatory gate have a pre-specified window? If so, how long should that gate be imposed?

e. Time Limit on Gates

We are proposing that a money market fund board must lift any gate it imposes within 30 days and that a board could not impose a gate for more than 30 days in any 90-day period. As noted above, a fund board could only impose a gate if it determines that the gate is in the best interest of the fund, and we would expect the board would lift the gate as soon as it determines that a gate is no longer in the best interest of the fund. This time limitation for the gate is designed to balance protecting the fund in times of stress while not unduly limiting the redeemability of money market fund shares, given the strong preference embodied in the Investment Company Act for the redeemability of open-end investment company shares.[395] We understand that investors use money market funds for cash management, and that lack of access to their money market fund investment for a long period of time can impose substantial costs and hardships.[396] Indeed, many shareholders in The Reserve Primary Fund informed us about these costs and hardships during that fund's lengthy liquidation.[397]

These concerns motivated us to propose a time period that would not freeze shareholders' money market fund investments for an excessively long period of time. On the other hand, we do want to provide some time for stressed market conditions to subside, for portfolio securities to mature and provide internal liquidity to the fund, and for potentially distressed fund portfolio securities to recover or be held to maturity. As of February 28, 2013, 43% of prime money market fund assets had a maturity of 30 days or less.[398] Accordingly, within a 30-day window for a gate, a substantial amount of a money market fund's assets could mature and provide cash to the fund to meet redemptions when the fund re-opened. We also note that some commenters suggested a 30-day time limit on any gate.[399] Balancing all of these factors led us to propose a 30-day time limit for any gate imposed. So that this 30-day time limit could not be circumvented, for example, by reopening the fund on the 29th day for a day before re-imposing the gate for potentially another 30-day period, we also are proposing that the fund cannot impose a gate for more than 30 days in any 90-day period. The 30-day limit is a maximum, and a money market fund board likely would need to meet regularly during any period in which a redemption gate is in place and would lift the gate promptly when it

[394] *See, e.g.,* ICI Jan. 24 FSOC Comment Letter, *supra* note 25; Vanguard FSOC Comment Letter, *supra* note 172.

[395] *See Investment Trusts and Investment Companies: Hearings on S. 3580 Before a Subcomm. of the Senate Comm. on Banking and Currency,* 76th Cong., 3d Sess. 291–292 (1940) (statement of David Schenker, Chief Counsel, Investment Trust Study, SEC).

[396] *See, e.g.,* Comment Letter of Thrivent Financial for Lutherans (Feb. 15, 2013) (available in File No. FSOC–2012–0003) (''Thrivent FSOC Comment Letter'') (''The proposed liquidity fees reduce the simplicity, reduce the liquidity for the majority of shareholders, increase the potential for losses, and as a result, dramatically alter the product. Money market funds' intended purpose is to be a liquidity product, but if the product is only liquid for the first 15% of investors that redeem, then it is no longer a liquidity product for the remaining 85%.'').

[397] *See* Kevin McCoy, *Primary Fund Shareholders Put in a Bind,* USA Today, Nov. 11, 2008, *available at http://usatoday30.usatoday.com/money/perfi/funds/2008-11-11-market-fund-side_N.htm* (discussing hardships faced by Reserve Primary Fund shareholders due to having their shareholdings frozen, including a small business owner who almost was unable to launch a new business, and noting that ''Ameriprise has used 'hundreds of millions of dollars' of its own liquidity for temporary loans to clients who face financial hardships while they await final repayments from the Primary Fund''); John G. Taft, Stewardship: Lessons Learned from the Lost Culture of Wall Street (2012), at 2 (''Now that the Reserve Primary Fund had suspended redemptions of Fund shares for cash, our clients had no access to their cash. This meant, in many cases, that they had no way to settle pending securities purchase and therefore no way to trade their portfolios at a time of historic market volatility. No way to make minimum required distributions from retirement plans. No way to pay property taxes. No way to pay college tuition. It meant bounced checks and, for retirees, interruption of the cash flow distributions they were counting on to pay their day-to-day living expenses.'').

[398] Based on Form N–MFP data, with maturity determined in the same manner as it is for purposes of computing the fund's weighted average life.

[399] *See, e.g.,* ICI Jan. 24 FSOC Comment Letter, *supra* note 25.

determines that the gate is no longer in the best interest of the fund.[400]

• Does a 30-day limit appropriately balance these objectives? Should there be a shorter time limit, such as 10 days? Should there be a longer time limit, such as 45 days? Why?

• Will our proposed limit on the number of days a fund can be gated in any 90-day period effectively prevent ''gaming'' of the 30-day gate limitation? Should it be a shorter window or larger window? 60 days? 120 days?

• Should we impose additional restrictions on a money market fund's use of a gate? Should we, for example, require the board of directors of a money market fund that has imposed a gate to meet each day or week that the gate is in place, and permit the gate to remain in place only if the board makes specified findings at these meetings? We could provide that a gate may only remain in place if the board, including a majority of the independent directors, finds that lifting the gate and meeting shareholder redemptions could result in material dilution or other unfair results to investors or existing shareholders. Would requiring the board to make such a finding to continue to use a gate help to prevent a fund from imposing a gate for longer than is necessary or appropriate? Would a different required finding better achieve this goal? Would fund boards be able to make such findings accurately, particularly during a crisis when a board may be more likely to impose a gate? Would such a requirement deter fund boards from keeping a gate in place when doing so may be in the best interest of the fund?

f. Application of Liquidity Fees to Omnibus Accounts

For beneficial owners holding mutual fund shares through omnibus accounts, we understand that, with respect to redemption fees imposed to deter market timing of mutual fund shares, financial intermediaries generally impose any redemption fees themselves to record or beneficial owners holding through that intermediary.[401] We understand that they do so often in accordance with contractual arrangements between the fund or its transfer agent and the intermediary. We would expect any liquidity fees to be handled in a similar manner, although we understand that some money market fund sponsors will want to review their contractual arrangements with their funds' financial intermediaries and service providers to determine whether any contractual modifications would be necessary or advisable to ensure that any liquidity fees are appropriately applied to beneficial owners of money market fund shares. We also understand that some money market fund sponsors may seek certifications or other assurances that these intermediaries and service providers will apply any liquidity fees to the beneficial owners of money market fund shares. We also recognize that money market funds and their transfer agents and intermediaries will need to engage in certain communications regarding a liquidity fee.

We request comment on the application of liquidity fees and gates to shares held through omnibus accounts.

• Do commenters agree with our view that liquidity fees likely will be handled by intermediaries in a manner similar to how they currently impose redemption fees? If not, how would liquidity fees be applied to shares held through financial intermediaries? Is our understanding correct that financial intermediaries generally apply any liquidity fees themselves to record or beneficial owners holding through that intermediary? Would they do so based on existing contractual arrangements or would funds make contractual modifications? What cost would be involved in any contractual modifications?

• Would funds in addition or instead seek certifications from financial intermediaries that they will apply any liquidity fees? What cost would be involved in any such certifications?

• What other methods might money market funds use to gain assurances that financial intermediaries will apply any liquidity fees appropriately? At what costs? Will some intermediaries not offer prime money market funds to avoid operational costs involved with fees and gates?

3. Exemptions To Permit Liquidity Fees and Gates

The Commission is proposing exemptions from various provisions of the Investment Company Act to permit a fund to institute liquidity fees and gates.[402] In the absence of an exemption, imposing gates could violate section 22(e) of the Act, which generally prohibits a mutual fund from suspending the right of redemption or postponing the payment of redemption proceeds for more than seven days, and imposing liquidity fees could violate rule 22c–1, which (together with section 22(c) and other provisions of the Act) requires that each redeeming shareholder receive his or her pro rata portion of the fund's net assets. The Commission is proposing to exercise its authority under section 6(c) of the Act to provide exemptions from these and related provisions of the Act to permit a money market fund to institute liquidity fees and gates notwithstanding these restrictions.[403] As discussed in more detail below, we believe that such exemptions do not implicate the concerns that Congress intended to address in enacting these provisions, and thus they are necessary and appropriate in the public interest and consistent with the protection of investors and the purposes fairly intended by the Act.

We do not believe that gates would conflict with the purposes underlying section 22(e), which was designed to prevent funds and their investment advisers from interfering with the redemption rights of shareholders for improper purposes, such as the preservation of management fees.[404] The board of a money market fund would impose gates to benefit the fund and its shareholders by making the fund better able to handle substantial redemptions, as discussed above.

We also propose to provide exemptions from rule 22c–1 to permit a money market fund to impose liquidity fees because a money market fund would impose liquidity fees to benefit the fund and its shareholders by providing a more systematic allocation of liquidity costs.[405] Remaining shareholders also may benefit if the fees help repair any decline in the fund's shadow price or lead to an increased

[400] The fund's board may also consider permanently suspending redemptions in preparation for fund liquidation under rule 22e–3 if the fund approaches the 30 day gating limit.

[401] *See* rule 22c–2. Our understanding of how financial intermediaries handle redemption fees in mutual funds is based on Commission staff discussions with industry participants and service providers.

[402] *See* proposed (Fees & Gates) rule 2a–7(c).

[403] 15 U.S.C. 80a–6(c). In order to clarify the application of liquidity fees and gates to variable contracts, we also would amend rule 2a–7 to provide that, notwithstanding section 27(i) of the Act, a variable contract sold by a registered separate account funding variable insurance contracts or the sponsoring insurance company of such account may apply a liquidity fee or gate to contract owners who allocate all or a portion of their contract value to a subaccount of the separate account that is either a money market fund or that invests all of its assets in shares of a money market fund. *See* proposed (Fees & Gates) rule 2a–7(c)(2)(iv). Section 27(i)(2)(A) makes it unlawful for any registered separate account funding variable insurance contracts or the sponsoring insurance company of such account to sell a variable contract that is not a ''redeemable security.''

[404] *See* 2009 Proposing Release, *supra* note 31, at n.281 and accompanying text.

[405] *See* proposed (Fees & Gates) rule 2a–7(c) (providing that, notwithstanding rule 22c–1, among other provisions, a money market fund may impose a liquidity fee under the circumstances specified in the proposed rule).

dividend paid to remaining fund shareholders. The amount of additional fees that the fund might collect in this regard would be only to further the purpose of the provision and could only be imposed under circumstances of stress on the fund.

A gate would also be similarly limited. It could only be imposed for a limited period of time and only under circumstances of stress on the fund. This aspect of gates, therefore, is akin to rule 22e–3, which also provides an exemption from section 22(e) to permit money market fund boards to suspend redemptions of fund shares in order to protect the fund and its shareholders from the harmful effects of a run on the fund, and to minimize the potential for disruption to the securities markets.[406] We are proposing to permit money market funds to be able to impose fees and gates because they may provide substantial benefits to money market funds and the short-term financing markets for issuers, as discussed above. However, because we recognize that fees and gates may impose hardships on investors who rely on their ability to freely redeem shares (or to redeem shares without paying a fee), we also have proposed limitations on when and for how long money market funds could impose these restrictions.[407]

We request comment on our proposed amendments allowing money market funds to institute fees and gates.

- Would the proposed amendments to rule 2a–7 provide sufficient exemptive relief to permit a money market fund to institute fees or gates with both the requirements of rule 2a–7 and the Investment Company Act? Are there other provisions of the Investment Company Act from which the Commission should consider providing an exemption?

4. Amendments to Rule 22e–3

Under this proposal, we also would amend rule 22e–3 to permit (but not require) the permanent suspension of redemptions and liquidation of a money market fund if the fund's level of weekly liquid assets falls below 15% of its total assets.[408] This will allow a money market fund that imposes a fee or a gate, but determines that it would not be in the best interest of the fund to continue operating, to permanently suspend redemptions and liquidate. As such, it will provide an additional tool to fund boards of directors to manage a fund in the best interest of the fund when that fund comes under stress regarding its liquidity buffers. It will allow fund boards to suspend redemptions and liquidate a fund that the board determines would be unable to stay open (or, if gated, re-open) without further harm to the fund, and prevents such a fund from waiting until its shadow price has declined so far that it is about to ''break the buck.''

We considered whether a money market fund's level of weekly liquid assets should have to fall further than the 15% threshold that allows the imposition of fees and gates for the fund to be able to permanently suspend redemptions and liquidate. A permanent suspension of redemptions could be considered more draconian because there is no prospect that the fund will re-open—instead the fund will simply liquidate and return money to shareholders. Accordingly, one could consider a lower weekly liquid asset threshold than 15% justified. However, we believe such considerations must be balanced against the risk that might be caused by establishing a lower threshold for enabling a permanent suspension of redemptions. For example, a fund with a fee or gate in place might know (based on market conditions or discussions with its shareholders or otherwise) that upon lifting the fee or gate it will experience a severe run. We would not want to force such a fund to lift the fee or re-open and weather enough of that run to deplete its weekly liquid assets below a lower threshold. We preliminarily believe this risk is great enough to warrant allowing money market funds to suspend redemptions permanently once the fund's weekly liquid assets fall below 15% of its total assets.

As under existing rule 22e–3, a money market fund also would still be able to suspend redemptions and liquidate if it determines that the extent of the deviation between its shadow price and its market-based NAV per share may result in material dilution or other unfair results to investors or existing shareholders.[409] Accordingly, a money market fund that suffers a default would still be able to suspend redemptions and liquidate before that credit loss lead to redemptions and a fall in its weekly liquid assets.

We request comment on our proposed amendments to rule 22e–3 under this proposal.

- Is it appropriate to allow a money market fund to suspend redemptions and liquidate if its level of weekly liquid assets falls below 15% of its total assets? Is there a different threshold based on daily or weekly assets that would better protect money market fund shareholders?
- Should a fund's ability to suspend redemptions and liquidate be tied only to adverse deviations in its shadow price? If so, is our current standard under rule 22e–3 appropriate or is there a different level of shadow price decline that should trigger a money market fund's ability to suspend redemptions and liquidate?

5. Exemptions From the Liquidity Fees and Gates Requirement

We are proposing that government money market funds (including Treasury money market funds) be exempt from any fee or gate requirement but that these funds be permitted to impose such a fee or gate under the regime we have described above if the ability to impose such fees and gates were disclosed in the fund's prospectus.[410] This exemption is based on a similar analysis to our proposed exemption of government money market funds from the floating NAV proposal and also on our desire to facilitate investor choice by providing a money market fund investment option for an investor who was unwilling or unable to invest in a money market fund that could impose liquidity fees or gates in times of stress.

As discussed in the RSFI Study, government money market funds historically have experienced inflows, rather than outflows, in times of stress due to flights to quality, liquidity, and transparency.[411] The assets of government money market funds tend to appreciate in value in times of stress rather than depreciate.[412] Accordingly,

[406] *See* 2010 Adopting Release, *supra* note 92, at text following n.379.

[407] *See* proposed (Fees & Gates) rule 2a–7(c)(2). *Cf.* 2010 Adopting Release, *supra* note 92, at text following n.379 (''Because the suspension of redemptions may impose hardships on investors who rely on their ability to redeem shares, the conditions of [rule 22e–3] limit the fund's ability to suspend redemptions to circumstances that present a significant risk of a run on the fund and potential harm to shareholders.'')

[408] *See* proposed (Fees & Gates) rule 22e–3.

[409] *See* proposed (Fees & Gates) rule 22e–3.

[410] *See* proposed (Fees & Gates) rule 2a–7(c)(2)(iii).

[411] *See* RSFI Study, *supra* note 21, at 6–13.

[412] Government money market funds tend to attract significant inflows of investments during times of broader market distress, which can appreciate their value. *See, e.g.,* figure 1 in *supra* section I.B (showing that during the 2008 Lehman crisis institutional share classes of government money market funds, which include Treasury and government funds, experienced heavy inflows). *Also see, e.g.,* ICI Jan. 24 FSOC Comment Letter, *supra* note 25 (noting government money market funds attracted an inflow of $192 billion during the week following the Lehman bankruptcy in September 2008); HSBC FSOC Comment Letter, *supra* note 196 (''As evidenced during the credit crisis of 2008, Treasury and government funds benefitted from a ''flight to quality'' during these

the portfolio composition of government money market funds means that these funds are less likely to need to use these restrictions. We also expect that some money market fund investors may be unwilling or unable to invest in a money market fund that could impose a fee or gate. For example, there could be some types of investors, such as sweep accounts, that may be unwilling or unable to invest in a money market fund that could impose a gate because such an investor requires the ability to immediately redeem at any point in time, regardless of whether the fund or the markets are distressed. Accordingly, exempting government money market funds from the fees and gates requirement would allow fund sponsors to offer a choice of money market fund investment products that meet differing liquidity needs, while minimizing the risk of adverse contagion effects from heavy money market fund redemptions. Based on our evaluation of these considerations and tradeoffs, and the more limited risk of heavy redemptions in government money market funds, we preliminarily believe that on balance it is preferable to exempt these funds from this potential requirement, but permit them to use liquidity fees and gates if they choose.

We note that Treasury money market funds generally would be exempt from any liquidity fees and gates requirement because at least 80% of their assets generally must be Treasury securities and overnight repurchase agreements collateralized with Treasury securities, each of which is a weekly liquid asset. Accordingly, it is highly unlikely for a Treasury money market fund to breach the 15% weekly liquid asset threshold that would allow imposition of a fee or gate. Most government money market funds similarly always would have at least 15% weekly liquid assets because of the nature of their portfolio, but it is possible to have a government money market fund with below 15% weekly liquid assets. We also note that government money market funds and Treasury money market funds do not necessarily have the same risk profile. For example, government money market funds generally have a much higher portion of their portfolios invested in securities issued by the Federal Home Loan Mortgage Corporation (Freddie Mac), the Federal National Mortgage Association (Fannie Mae), and the Federal Home Loan Banks and thus a higher exposure to the home mortgage market than Treasury money market funds. We note that this exemption would not apply to tax-exempt (or municipal) money market funds. As discussed above, because tax-exempt money market funds are not required to maintain 10% daily liquid assets, these funds may be less liquid than other money market funds, which could raise concerns that tax-exempt retail funds might not be able to manage even the lower level of redemptions expected in a retail money market fund. In addition, municipal securities typically present greater credit and liquidity risk than government securities and thus could come under pressure in times of stress.

We request comment on our proposed exemption of government money market funds from the proposed liquidity fees and gates requirement.

- Is this exemption appropriate, particularly in light of the redemptions from government funds in late June and early July 2011? Why or why not?
- Is it appropriate to give government money market funds the option to have the ability to impose fees and gates so long as they disclose the option to investors? Why or why not? What factors might lead a government fund to exercise this option?
- Should the exemption for government money market funds be extended to municipal money market funds? Why or why not?

We also considered whether there should be other exemptions from the proposed liquidity fees and gates requirement. For example, as discussed in section III.A.4 above, we are proposing an exemption for retail money market funds from any floating NAV requirement. We noted in that section how retail money market funds experienced fewer redemptions during the 2007–2008 financial crisis and thus may be less likely to suffer heavy redemptions in the future. However, unlike with government money market funds, a retail prime money market fund generally is subject to the same credit and liquidity risk as an institutional prime money market fund. In addition, a floating NAV requirement affects a shareholder's experience with a money market fund on a daily basis. Given the costs and burdens associated with a floating NAV requirement, and the potential limited benefit to retail shareholders on an ongoing basis given that they are less likely to engage in heavy redemptions, a retail exemption might be more appropriate on balance under a floating NAV requirement than under a liquidity fees and gates requirement. In contrast, a fee or gate requirement would not affect a money market fund unless the fund's weekly liquid assets fell below 15% of its total assets—*i.e.,* unless it came under stress. Exempting retail money market funds from this requirement thus could leave only institutional (and not retail) shareholders protected when the money market fund in which they have invested comes under stress. Given that such an exemption would merely relieve them in normal times of the costs and burden on those investors created by the prospect that the fund could impose a fee or gate if someday it came under stress, we preliminarily believe that a retail exemption may not be warranted for this alternative. We also considered methods of exempting some retail investors from a fee or gate requirement. For example, we could exempt small redemption requests, such as those below $10,000, or $100,000 per day, from any fee or gate requirement. Such small redemptions are less likely to materially impact the liquidity position of the fund. This type of exemption could retain the benefits of fees and gates for retail money market funds generally while providing some relief from the burdens for investors with smaller redemption needs. However, we are concerned that granting such exemptions could complicate the fees and gates requirement both as an operational matter and in terms of ease of shareholder understanding without providing substantial benefits.

We also have considered whether irrevocable redemption requests submitted at least a certain period in advance should be exempt as the fund should be able to plan for such liquidity demands and hold sufficient liquid assets. However, we are concerned that shareholders could try to ''game'' the fee or gate requirement through such exemptions, for example, by redeeming a certain amount every week and then reinvesting the redemption proceeds immediately if the cash is not needed. We also are concerned that allowing such an exception would add significantly to the cost and complexity of this requirement, as fund groups would need to be able to separately track which shares are subject to a fee or gate and which are not.

We request comment on other potential exemptions from the proposed liquidity fees and gates requirement.

- Should retail money market funds (including tax-exempt money market funds) or retail investors be exempt from any liquidity fee or gate provision? Should there be an exemption for small redemption requests, such as redemptions below $10,000? If so, below what level? If a retail money

systemic events''); Dreyfus FSOC Comment Letter, *supra* note 174 (noting its institutional government and institutional Treasury money market funds generally experienced high levels of net inflows during 2008).

market fund crossed the thresholds we are proposing for board consideration of a fee or gate, is there a reason not to allow the fund's board to protect the fund and its shareholders through the use of a liquidity fee or gate? Would investors ''game'' such exemptions?

• Should we create an exemption for shareholders that submit an irrevocable redemption request at least a certain period in advance of the needed redemption? Why or why not? With what period of advance notice? For each of these exemptions, could funds track the shares that are not subject to the fee or gate? What operational costs would be involved in including such an exemption? Would shareholders ''game'' such exemptions?

• Would further exemptions undermine the goal of the liquidity fee or gate in deterring or stopping heavy redemptions? Why or why not? Would exemptions from the fee or gate proposal make it more difficult or costly to implement or operationalize? How would any such difficulties compare to the benefits that could be obtained from such exemptions?

6. Operational Considerations Relating to Liquidity Fees and Gates

Money market funds and others in the distribution chain (depending on how they are structured) likely would incur some operational costs in establishing or modifying systems to administer a liquidity fee or gate. These costs likely would be incurred by, or spread amongst, a fund's transfer agents, sub-transfer agents, recordkeepers, accountants, portfolio accounting departments, and custodian. Money market funds and others also may be required to develop procedures and controls, and may incur other costs, for example to update systems necessary for confirmations and account statements to reflect the deduction of a liquidity fee from redemption proceeds. Money market funds and their intermediaries may need to establish new, or modify existing, systems or procedures that would allow them to administer temporary gates. Money market fund shareholders also might be required to modify their own systems to prepare for possible future liquidity fees, or manage gates, although we expect that only some shareholders would be required to make these changes.[413] They also may modify contracts or seek certifications from financial intermediaries that they will apply any liquidity fee.

These costs would vary depending on how a liquidity fee or gate is structured, including its triggering event, as well as on the capabilities, functions, and sophistication of the fund's and others' current systems. These factors will vary among money market funds, shareholders, and others, and particularly because we request comment on a number of ways in which we could structure a liquidity fee or gate requirement, we cannot ascertain at this stage the systems and other modifications any particular money market fund or other affected entity would be required to make to administer a liquidity fee or manage a gate. Indeed, we believe that money market funds and other affected entities themselves would need to engage in an in-depth analysis of this alternative in order to estimate the costs of the necessary systems modifications. While we do not have the information necessary to provide a point estimate of the potential costs of systems modifications needed to administer a liquidity fee or gate, our staff has estimated a range of hours and costs that may be required to perform activities typically involved in making systems modifications.[414] In estimating these hours and costs, our staff considered the need to modify the systems described above.

If a money market fund determines that it would only impose a flat liquidity fee of a fixed percentage known in advance (*e.g.,* it would only impose the default 2% liquidity fee) and have the ability to impose a gate, our staff estimates that a money market fund (or others in the distribution chain) would incur one-time systems modification costs (including modifications to related procedures and controls) that ranges from $1,100,000 to $2,200,000.[415] Our staff estimates that the one-time costs for entities to communicate with shareholders (including systems costs related to communications) about the liquidity fee or gate would range from $200,500 to $340,000.[416] In addition, we estimate that the costs for a shareholder mailing would range between $1.00 and $3.00 per shareholder.[417] We also recognize that adding new capabilities or capacity to a system will entail ongoing annual maintenance costs and understand that those costs generally are estimated as a percentage of initial costs of building or expanding a system. Our staff estimates that the costs to maintain and modify these systems required to administer a liquidity fee and the ability to administer a standby gate (to accommodate future programming changes), to provide ongoing training, and to administer the liquidity fee or gate on an ongoing basis would range from 5% to 15% of the one-time costs. Our staff understands that if a fund board imposes a liquidity fee whose amount could vary, the cost could exceed this range, but because such costs depend on to what extent the fee might vary, we do not have the information necessary to provide a reasonable estimate of how much more a varying fee might cost to implement.

Although our staff has estimated the costs that a single affected entity would incur, we anticipate that many money market funds, transfer agents, and other affected entities may not bear the estimated costs on an individual basis. Instead, the costs of systems modifications likely would be allocated among the multiple users of the systems, such as money market fund members of a fund group, money market funds that use the same transfer agent or custodian, and intermediaries that use systems purchased from the same third party. Accordingly, we expect that the cost for many individual entities may be less than the estimated costs due to economies of scale in allocating costs among this group of users.

Moreover, depending on how a liquidity fee or gate is structured, mutual fund groups and other affected entities already may have systems that could be adapted to administer a liquidity fee or gate at minimal cost, in which case the costs may be less than the range we estimate above. For example, some money market funds may be part of mutual fund groups in which one or more funds impose deferred sales loads or redemption fees

[413] Many shareholders use common third party-created systems and thus would not each need to modify their systems.

[414] Staff estimates that these costs would be attributable to the following activities: (i) Planning, coding, testing, and installing system modifications; (ii) drafting, integrating, and implementing related procedures and controls; and (iii) preparing training materials and administering training sessions for staff in affected areas. *See also supra* note 245 (discussing the bases of our staff's estimates of operational and related costs).

[415] Staff estimates that these costs would be attributable to the following activities: (i) Project planning and systems design; (ii) systems modification, integration, testing, installation, and deployment; (iii) drafting, integrating, implementing procedures and controls; and (iv) preparation of training materials. *See also supra* note 245 (discussing the bases of our staff's estimates of operational and related costs).

[416] Staff estimates that these costs would be attributable to the following activities: (i) modifying the Web site to provide online account information and (ii) written and telephone communications with investors. *See also supra* note 245 (discussing the bases of our staff's estimates of operational and related costs).

[417] Total costs of the mailing for individual funds would vary significantly depending on the number of shareholders that receive information from the fund by mail (as opposed to electronically).

under rule 22c–2, both of which require the capacity to administer a fee upon redemptions and may involve systems that could be adapted to administer a liquidity fee.

Our staff estimates that a money market fund shareholder whose systems (including related procedures and controls) required modifications to account for a liquidity fee or gate would incur one-time costs ranging from $220,000 to $450,000.[418] Our staff estimates that the costs to maintain and modify these systems and to provide ongoing training would range from 5% to 15% of the one-time costs.

We request comment on our estimate of operational costs associated with the liquidity fees and gates alternative.

- Do commenters agree with our estimates of operational costs?
- Are there operational costs in addition to those we estimate above? What systems would need to be reprogrammed and to what extent? What types of ongoing maintenance, training, and other activities to administer the liquidity fee or gate would be required, and to what extent?
- Are our estimates too high or too low and, if so, by what amount? To what extent would the estimate vary based on the event that would trigger the imposition of a liquidity fee or the manner in which the fee would be calculated once triggered? To what extent would the estimate vary based on how the gate is structured?
- To what extent would money market funds or others experience the economies of scale that we identify?

7. Tax Implications of Liquidity Fees

We understand that liquidity fees may have certain tax implications for money market funds and their shareholders. Similar to the liquidity fee we are proposing today, rule 22c–2 allows mutual funds to recover costs associated with frequent mutual fund share trading by imposing a redemption fee on shareholders who redeem shares within seven days of purchase. We understand that for tax purposes, shareholders of these mutual funds generally treat the redemption fee as offsetting the shareholder's amount realized on the redemption (decreasing the shareholder's gain, or increasing the shareholder's loss, on redemption).[419] Consistent with this characterization, funds generally treat the redemption fee as having no associated tax effect for the fund. We understand that our proposed liquidity fee, if adopted, would be treated for tax purposes consistently with the way that funds and shareholders treat redemption fees under rule 22c–2.[420]

If, as described above, a liquidity fee has no direct tax consequences for the money market fund, that tax treatment would allow the fund to use 100% of the fee to repair a market-based price per share that was below $1.0000. If redemptions involving liquidity fees cause the money market fund's shadow price to reach $1.0050, however, the fund may need to distribute to the remaining shareholders sufficient value to prevent the fund from breaking the buck (and thus rounding up to $1.01 in pricing its shares).[421] We understand that any such distribution would be treated as a dividend to the extent that the money market fund has sufficient earnings and profits. Both the fund and its shareholders would treat these additional dividends the same as they treat the fund's routine dividend distributions. That is, the additional dividends would be taxable as ordinary income to shareholders and would be eligible for deduction by the funds.

In the absence of sufficient earnings and profits, however, some or all of these additional distributions would be treated as a return of capital. Receipt of a return of capital would reduce the recipient shareholders' basis (and thus could decrease a loss, or create or increase a gain for the shareholder in the future when the shareholder redeems the affected shares).[422] Thus, in the event of any return of capital distributions, the shareholders, the fund, and other intermediaries might become subject to tax-payment or tax-reporting obligations that do not affect stable NAV funds currently operating under rule 2a–7.[423]

Finally, we understand that the tax treatment of a liquidity fee may impose certain operational costs on money market funds and their financial intermediaries and on shareholders. Either fund groups or their intermediaries would need to track the tax basis of money market fund shares as the basis changed due to any return of capital distributions, and shareholders would need to report in their annual tax filings any gains[424] or losses upon the sale of affected money market fund shares. We are unable to quantify any of the tax and operational costs discussed in this section because we are unable to predict how often liquidity fees will be imposed by money market funds and how often redemptions subject to liquidity fees would cause the funds to make return of capital distributions to the remaining shareholders.

We request comment on this aspect of our proposal.

- If liquidity fees cause the fund's shadow price to exceed $1.0049, will that result cause the fund to make a special distribution to current shareholders?
- Do money market funds and other intermediaries already have systems in place to track and report the variations in basis, and the gains and losses that might result from imposing liquidity fees? If not, what costs would be

[418] Staff estimates that these costs would be attributable to the following activities: (i) Project planning and systems design; (ii) systems modification, integration, testing, installation; and (iii) drafting, integrating, implementing procedures and controls. *See also supra* note 245 (discussing the bases of our staff's estimates of operational and related costs).

[419] *Cf.* 26 CFR 1.263(a)–2(e) (commissions paid in sales of securities by persons who are not dealers are treated as offsets against the selling price). *See also* Investment Income and Expenses (Including Capital Gains and Losses), IRS Publication 550, at 44 (''fees and charges you pay to acquire or redeem shares of a mutual fund are not deductible. You can usually add acquisition fees and charges to your cost of the shares and thereby increase your basis. A fee paid to redeem the shares is usually a reduction in the redemption price (sales price).''), *available at http://www.irs.gov/pub/irs-pdf/p550.pdf.*

[420] Referring to IRS guidance in a different context, one commenter suggested that our proposed liquidity fee also might be characterized for tax purposes as an investment expense for the shareholder and income to the fund. *See* ICI Jan. 24 FSOC Comment Letter, *supra* note 25. This commenter noted that, if the fund were required to treat the liquidity fee as ordinary income, the fund would have to distribute the income to avoid liability for the corporate level income tax and a 4% excise tax on the amount retained. In that case, the fund would not realize all of the benefit the liquidity fee is designed to provide. *Id.* (citing IRS Revenue Procedure 2009–10 as supporting the position that the fee received by the fund should be treated as a capital gain because it is being used to offset capital losses incurred by the fund on its portfolio in order to pay the redeeming shareholder and noting that because the capital gain would offset the capital loss, the fund would not have an additional distribution requirement). This commenter suggests that the IRS provide guidance to this effect (noting that in Revenue Procedure 2009–10, which provided only temporary administrative guidance, the IRS took this position with respect to amounts paid to a money market fund by the fund's adviser to prevent the fund from breaking the buck). *Id. See also Arrowsmith et al.* v. *Commissioner of Internal Revenue,* 344 U.S. 6 (1952).

[421] *See* proposed (Fees & Gates) rule 2a–7(g)(2).

[422] If the payment of liquidity fees forces a money market fund to make a return of capital distribution to avoid re-pricing its shares above $1.00, this could also create tax consequences for remaining shareholders in the fund.

[423] See the discussion above of the additional obligations that would be created by gains and losses recognized with respect to floating NAV funds.

[424] Redemptions subject to a liquidity fee would almost always result in losses, but gains are possible if a shareholder received a return of capital distribution with respect to some shares and the shareholder later redeemed the shares for $1.0000 each.

expected to be incurred to establish this capability? In light of the fact that it may be necessary to establish new systems to track this information, how does the cost of these new systems compare with the costs that would be incurred to accommodate floating NAVs?

8. Disclosure Regarding Liquidity Fees and Gates

In connection with the liquidity fees and gates alternative, we are also proposing alternate disclosure-related amendments to rule 2a–7, rule 482 under the Securities Act,[425] and Form N–1A. We anticipate that the proposed rule and form amendments would provide current and prospective shareholders with information regarding the operations and risks of this reform alternative, as well as current and historical information regarding the imposition of fees and gates. In keeping with the enhanced disclosure framework we adopted in 2009,[426] the proposed amendments are intended to provide a layered approach to disclosure in which key information about the proposed new features of money market funds would be provided in the summary section of the statutory prospectus (and, accordingly, in any summary prospectus, if used) with more detailed information provided elsewhere in the statutory prospectus and in the SAI.

a. Disclosure Statement

The Commission's liquidity fees and gates alternative proposal would permit funds to charge liquidity fees and impose redemption restrictions on money market fund investors. As a measure to achieve this reform, we propose to require that each money market fund (other than government money market funds that have chosen to rely on the proposed rule 2a–7 exemption for government money market funds from any fee or gate requirements), include a bulleted statement, disclosing the particular risks associated with investing in a fund that may impose liquidity fees or redemption restrictions, on any advertisement or sales material that it disseminates (including on the fund Web site). We also propose to include wording designed to inform investors about the primary general risks of investing in money market funds in this bulleted disclosure statement. While money market funds are currently required to include a similar disclosure statement on their advertisements and sales materials,[427] we propose amending this disclosure statement to emphasize that money market fund sponsors are not obligated to provide financial support, and that money market funds may not be an appropriate investment option for investors who cannot tolerate losses.[428]

Specifically, we would require each money market fund (other than government money market funds that have chosen to rely on the proposed rule 2a–7 exemption for government money market funds from any fee or gate requirements) to include the following bulleted disclosure statement on their advertisements and sales materials:

- You could lose money by investing in the Fund.
- The Fund seeks to preserve the value of your investment at $1.00 per share, but cannot guarantee such stability.
- The Fund may impose a fee upon sale of your shares when the Fund is under considerable stress.
- The Fund may temporarily suspend your ability to sell shares of the Fund when the Fund is under considerable stress.
- An investment in the Fund is not insured or guaranteed by the Federal Deposit Insurance Corporation or any other government agency.
- The Fund's sponsor has no legal obligation to provide financial support to the Fund, and you should not expect that the sponsor will provide financial support to the Fund at any time.[429]

We also propose to require a substantially similar bulleted disclosure statement in the summary section of the statutory prospectus (and, accordingly, in any summary prospectus, if used).[430]

As discussed above, the liquidity fees and gates proposal would exempt government money market funds from any fee or gate requirement, but a government money market fund would be permitted to charge liquidity fees and impose gates if the ability to charge liquidity fees and impose gates were disclosed in the fund's prospectus. Accordingly, the proposed amendments to rule 482 and Form N–1A would require government money market funds that have chosen to rely on this exemption to include a bulleted disclosure statement on the fund's advertisements and sales materials and in the summary section of the fund's statutory prospectus (and, accordingly, in any summary prospectus, if used) that does not include disclosure of the risks of liquidity fees and gates, but that includes additional detail about the risks of investing in money market funds generally. We propose to require each government money market fund that relies on the exemption to include the following bulleted disclosure statement in the summary section of its statutory prospectus (and, accordingly, in any summary prospectus, if used), and on any advertisement or sales material that it disseminates (including on the fund Web site):

- You could lose money by investing in the Fund.
- The Fund seeks to preserve the value of your investment at $1.00 per share, but cannot guarantee such stability.
- An investment in the Fund is not insured or guaranteed by the Federal Deposit Insurance Corporation or any other government agency.
- The Fund's sponsor has no legal obligation to provide financial support to the Fund, and you should not expect that the sponsor will provide financial support to the Fund at any time.[431]

[425] *See supra* note 303.

[426] *See* Summary Prospectus Adopting Release, *supra* note 304, at paragraph preceding section III.

[427] *See id.* Rule 482(b)(4) currently requires a money market fund to include to following disclosure statement on its advertisements and sales materials: An investment in the Fund is not insured or guaranteed by the Federal Deposit Insurance Corporation or any other government agency. Although the Fund seeks to preserve the value of your investment at $1.00 per share, it is possible to lose money by investing in the Fund.

[428] *See infra* note 607 and accompanying text (discussing the extent to which discretionary sponsor support has the potential to confuse money market fund investors); *supra* note 141 and accompanying text (noting that survey data shows that some investors are unsure about the amount of risk in money market funds and the likelihood of government assistance if losses occur).

[429] *See* proposed (Fees & Gates) rule 482(b)(4)(i). Rule 482(b)(4) currently requires a money market fund to include to following disclosure statement on its advertisements and sales materials: An investment in the Fund is not insured or guaranteed by the Federal Deposit Insurance Corporation or any other government agency. Although the Fund seeks to preserve the value of your investment at $1.00 per share, it is possible to lose money by investing in the Fund.

If an affiliated person, promoter, or principal underwriter of the fund, or an affiliated person of such person, has entered into an agreement to provide financial support to the fund, the fund would be permitted to omit this bulleted sentence from the disclosure statement for the term of the agreement. *See* Note to paragraph (b)(4), proposed (Fees & Gates) rule 482(b)(4).

[430] *See* proposed (Fees & Gates) Item 4(b)(1)(ii)(A) of Form N–1A. Item 4(b)(1)(ii) currently requires a money market fund to include the following statement in its prospectus: An investment in the Fund is not insured or guaranteed by the Federal Deposit Insurance Corporation or any other government agency. Although the Fund seeks to preserve the value of your investment at $1.00 per share, it is possible to lose money by investing in the Fund.

[431] *See* proposed (Fees & Gates) rule 482(b)(4)(ii) and proposed (Fees & Gates) Item 4(b)(1)(ii)(B) of Form N–1A. If an affiliated person, promoter, or principal underwriter of the fund, or an affiliated person of such person, has entered into an agreement to provide financial support to the fund, the fund would be permitted to omit this bulleted sentence from the disclosure statement that appears

The proposed disclosure statements are intended to be one measure to change the investment expectations of money market fund investors, including the expectation that a money market fund is a stable, riskless investment.[432] In addition, we are concerned that investors, under the liquidity fees and gates proposal, will not be fully aware of potential restrictions on fund redemptions. In proposing the disclosure statement, we have taken into consideration investor preferences for clear, concise, and understandable language and have also considered whether language that was stronger in conveying potential risks associated with money market funds would be effective for investors.[433] In addition, we considered whether the proposed disclosure statement should be limited to only money market fund advertisements and sales materials, as discussed above. Although we acknowledge that the summary section of the prospectus must contain a discussion of key risk factors associated with a money market fund, we believe that the importance of the disclosure statement merits its placement in both locations, similar to how the current money market fund legend is required in both money market fund advertisements and sales materials and the summary section of the prospectus.[434]

We request comment on the proposed disclosure statement.[435]

• Would the proposed disclosure statement adequately alert investors to the risks of investing in a money market fund, including a fund that could impose liquidity fees or gates under certain circumstances? Would investors understand the meaning of each part of the proposed disclosure statement? If not, how should the proposed disclosure statement be amended? Would the following variations on the proposed disclosure statement be any more or less useful in alerting shareholders to potential investment risks?

○ Removing or amending the following bullet in the proposed disclosure statement: ''The Fund's sponsor has no legal obligation to provide financial support to the Fund, and you should not expect that the sponsor will provide financial support to the Fund at any time.''

○ Including additional disclosure of the possibility that a temporary suspension of redemptions could become permanent if the board determines that the fund should liquidate.

○ Including additional disclosure to the effect that retail shareholders should not invest all or most of the cash that they might need for routine expenses (*e.g.,* mortgage payments, credit card bills, etc.) in any one money market fund, on account of the possibility that the fund could impose a liquidity fee or suspend redemptions.

○ Amending the final bullet in the proposed disclosure statement to read: ''Your investment in the Fund therefore may experience losses.''

• Will the proposed disclosure statement respond effectively to investor preferences for clear, concise, and understandable language?

• Would investors benefit from requiring this disclosure statement also to be included on the front cover page of a non-government money market fund's prospectus (and on the cover page or beginning of any summary prospectus, if used)?

• Should we provide any instruction or guidance in order to highlight the proposed disclosure statement on fund advertisements and sales materials (including the fund's Web site) and/or lead investors efficiently to the disclosure statement?[436] For example, with respect to the fund's Web site, should we instruct that the proposed disclosure statement be posted on the fund's home page or be accessible in no more than two clicks from the fund's home page?

b. Disclosure of the Effects of Liquidity Fees and Gates on Redemptions

Currently, funds are required to disclose any restrictions on fund redemptions in their registration statements.[437] We expect that, to comply with these requirements, money market funds (besides government money market funds that have chosen to rely on the proposed rule 2a–7 exemption from the fees and gates requirements) would disclose in the registration statement the effects that the potential imposition of fees and/or gates may have on a shareholder's ability to redeem shares of the fund. We believe that this disclosure would help investors understand the potential effect of their redemption decisions during periods that the fund experiences stress, and to evaluate the full costs of redeeming fund shares—one of the goals of this rulemaking.[438] Specifically, we would expect money market funds to briefly explain in the prospectus that if the fund's weekly liquid assets have fallen below 15% of its total assets, the fund will impose a liquidity fee of 2% on all redemptions, unless the board of directors of the fund (including a majority of its independent directors) determines that imposing such a fee would not be in the best interest of the fund or determines that a lesser fee would be in the best interest of the fund. We also would expect money market funds to briefly explain in the prospectus that if the fund's weekly liquid assets have fallen below 15% of its total assets, the fund board would be able to impose a temporary suspension of redemptions for a limited period of time and/or liquidate the fund. We also would expect money market funds to disclose in the prospectus that information about the historical occasions on which the fund's weekly liquid assets have fallen below 15% of its total assets, or the fund has imposed liquidity fees or redemption restrictions, appears in the funds' SAI (as applicable).[439]

In addition, we would expect money market funds to incorporate additional disclosure in the prospectus or SAI, as the fund determines appropriate, discussing the operations of fees and gates in more detail.[440] This could

on a fund advertisement or fund sales material, for the term of the agreement. *See* Note to paragraph (b)(4), proposed (Fees & Gates) rule 482(b)(4).

Likewise, if an affiliated person, promoter, or principal underwriter of the fund, or an affiliated person of such person, has entered into an agreement to provide financial support to the fund, and the term of the agreement will extend for at least one year following the effective date of the fund's registration statement, the fund would be permitted to omit this bulleted sentence from the disclosure statement that appears on the fund's registration statement. *See* Instruction to proposed (Fees & Gates) Item 4(b)(1)(ii) of Form N–1A.

[432] *See supra* section II.B.3.

[433] *See supra* notes 316 and 317.

[434] *See supra* notes 429 and 430.

[435] In the questions that follow, we use the term ''disclosure statement'' to mean the new disclosure statement that we propose to require money market funds other than those exempted from the fees and gates requirements to incorporate into their prospectuses and advertisements and sales materials or, alternatively and as appropriate, the new disclosure statement that we propose to require government funds (that choose to rely on the rule 2a–7 exemption from the fees and gates requirements) to incorporate into their prospectuses and advertisements and sales materials.

[436] Such instruction or guidance would supplement current requirements for the presentation of the disclosure statement required by rule 482(b)(4). *See supra* note 429; rule 482(b)(5).

[437] *See* Item 11(c)(1) and Item 23 of Form N–1A.

[438] *See supra* note 351 and accompanying text (discussing the extent to which standby liquidity fees can provide a disincentive for money market fund investors to redeem their shares during times of stress).

[439] *See infra* section III.B.8.d.

[440] Prospectus disclosure regarding any restrictions on redemptions is currently required by Item 11(c)(1) of Form N–1A. However, we believe that funds could determine that more detailed disclosure about the operations of fees and gates, as further discussed in this section, would appropriately appear in a fund's SAI, and that this more detailed disclosure is responsive to Item 23

Continued

include disclosure regarding the following:

- Means of notifying shareholders about the imposition and lifting of fees and/or gates (*e.g.,* press release, Web site announcement);
- Timing of the imposition and lifting of fees and gates, including an explanation that if a fund's weekly liquid assets fall below 15% of its total assets at the end of any business day, the next business day it must impose a 2% liquidity fee on shareholder redemptions unless the fund's board of directors determines otherwise, and an explanation of the 30-day limit for imposing gates;
- Use of fee proceeds by the fund, including any possible return to shareholders in the form of a distribution;
- The tax consequences to the fund and its shareholders of the fund's receipt of liquidity fees; and
- General description of the process of fund liquidation [441] if the fund's weekly liquid assets fall below 15%, and the fund's board of directors determines that the fund would be unable to stay open (or, if gated, re-open) without further harm to the fund.

We request comment on the disclosure that we expect funds to include in their registration statements regarding the operations and effects of liquidity fees and redemption gates.

- Would the disclosure that we discuss above adequately assist money market fund investors in understanding the potential effect of their redemption decisions, and in evaluating the full costs of redeeming fund shares? Should we require funds to include this disclosure in their prospectuses and/or SAIs? Should we require funds to include any additional prospectus and SAI disclosure discussing, in detail, the operations and effects of fees and redemption gates? In particular, should we require funds to include any additional details about the fund's liquidation process? [442] Alternatively, should any of the proposed prospectus and SAI disclosure not be required, and if so, why not?
- Should we require any information about the basic operations and effects of fees and redemption gates to be disclosed in the summary section of the statutory prospectus (and any summary prospectus, if used)?
- Should we require disclosure to investors of the particular risks associated with buying fund shares when the fund or market is stressed, especially when the fund is imposing either a liquidity fee or a gate?
- Should Form N–1A or its instructions be amended to more explicitly require any of the proposed disclosure to be included in a fund's prospectus and/or SAI? If so, how should it be amended?

c. Disclosure of the Imposition of Liquidity Fees and Gates

If we were to adopt a reform alternative involving liquidity fees and gates, we believe that it would be important for money market funds (other than government money market funds that have chosen to rely on the proposed rule 2a–7 exemption from the fees and gates requirements) to inform existing and prospective shareholders when: (i) The fund's weekly liquid assets fall below 15% of its total assets; (ii) the fund's board of directors imposes a liquidity fee pursuant to rule 2a–7; or (iii) the fund's board of directors temporarily suspends the fund's redemptions pursuant to rule 2a–7 or permanently suspends redemptions pursuant to rule 22e–3. This information would be important for shareholders to receive, as it could influence prospective shareholders' decision to purchase shares of the fund, as well as current shareholders' decision or ability to sell fund shares. To this end, we are proposing an amendment to rule 2a–7 that would require a fund to post prominently on its Web site certain information that the fund would be required to report to the Commission on Form N–CR [443] regarding the imposition of liquidity fees, suspension of fund redemptions, and the removal of liquidity fees and/or resumption of fund redemptions.[444] The amendment would require a fund to include this Web site disclosure on the same business day as the fund files an initial report with the Commission in response to any of the events specified in Parts E, F, and G of Form N–CR,[445] and, with respect to any such event, to maintain this disclosure on its Web site for a period of not less than one year following the date on which the fund filed Form N–CR concerning the event.[446]

We believe that this Web site disclosure would provide greater transparency to shareholders regarding occasions on which a fund's weekly liquid assets drop below 15% of the fund's total assets, as well as the imposition of liquidity fees and suspension of fund redemptions, because many investors currently obtain important information about the fund on the fund's Web site.[447] We understand that investors have, in past years, become accustomed to obtaining money market fund information on funds' Web sites.[448] While we believe

of Form N–1A (''Purchase, Redemption, and Pricing of Shares''). In determining whether to include this disclosure in the prospectus or SAI, money market funds should rely on the principle that funds should limit disclosure in prospectuses generally to information that is necessary for an average or typical investor to make an investment decision. Detailed or highly technical discussions, as well as information that may be helpful to more sophisticated investors, dilute the effect of necessary prospectus disclosure and should be placed in the SAI. *See* Registration Form Used by Open-End Management Investment Companies, Investment Company Act Release No. 23064 (Mar. 13, 1998) [63 FR 13916 (Mar. 23, 1998)], at section I. Based on this principle, we anticipate that funds would generally consider the disclosure topics covered by the first two bullets on the above list (means of notifying shareholders of fees and gates and the timing of the imposition and removal of fees and gates) to be appropriate prospectus disclosure.

[441] *See supra* note 408 and accompanying text.

[442] Disclosure about the process of fund liquidation might include, for example, disclosure regarding any fees, including advisory fees, that the adviser will collect during the liquidation process.

[443] *See infra* section III.G.

[444] *See* proposed (Fees & Gates) rule 2a–7(h)(10)(v); proposed (Fees & Gates) Form N–CR Parts E, F, and G; *see also infra* section III.G (discussing the proposed Form N–CR requirements). With respect to the events specified in Part E of Form N–CR (imposition of a liquidity fee) and Part F of Form N–CR (suspension of fund redemptions), a fund would be required to post on its Web site only the preliminary information required to be filed on Form N–CR on the first business day following the triggering event. *See* Instructions to proposed (Fees & Gates) Form N–CR Parts E and F.

[445] A fund must file an initial report on Form N–CR in response to any of the events specified in Parts E, F, or G within one business day after the occurrence of any such event. We believe that funds should disclose these events within one business day following the event because it is particularly important to provide shareholders with information that could directly affect their redemption of fund shares, and that could be a material factor in determining whether to purchase or redeem fund shares, as soon as reasonably possible.

[446] *See* proposed (Fees & Gates) rule 2a–7(h)(10)(v). We believe that the one-year minimum time frame for Web site disclosure is appropriate because this time frame would effectively oblige a fund to post the required information in the interim period until the fund files an annual post-effective amendment updating its registration statement, which update would incorporate the same information. *See infra* notes 450 and 451 and accompanying text. Although a fund would inform prospective investors of any redemption fee or gate currently in place by means of a prospectus supplement (*see infra* note 449 and accompanying text), the prospectus supplement would not inform shareholders of any fees or gates that were imposed, and then were removed, during the previous 12 months.

[447] For example, fund investors may access the fund's proxy voting guidelines, and proxy vote report, as well as the fund's prospectus, SAI, and shareholder reports if the fund uses a summary prospectus, on the fund Web site.

[448] *See, e.g.,* 2010 Adopting Release, *supra* note 92 (adopting amendments to rule 2a-7 requiring money market funds to disclose information about their portfolio holdings each month on their Web sites); SIFMA FSOC Comment Letter, *supra* note 358 (noting that some industry participants now post on their Web sites portfolio holdings-related information beyond that which is required by the

that it is important to have a uniform, central place for investors to access the required disclosure, we note that nothing in this proposal would prevent a fund from supplementing its Form N–CR filing and Web site posting with complementary shareholder communications, such as a press release or social media update disclosing a fee or gate imposed by the fund.

A fund currently must update its registration statement to reflect any material changes by means of a post-effective amendment or a prospectus supplement (or ''sticker'') pursuant to rule 497 under the Securities Act.[449] We would expect that, to meet this requirement, promptly after a money market fund imposes a redemption fee or gate, it would inform prospective investors of any fees or gates currently in place by means of a prospectus supplement.

We request comment on the proposed requirement for money market funds to inform existing and prospective shareholders, on the fund's Web site and in the fund's registration statement, of any present occasion in which the fund's weekly liquid assets fall below 15% of its total assets, the fund's board imposes a liquidity fee, or the fund's board temporarily suspends the fund's redemptions.

• Should any more, any less, or any other information be required to be posted on the fund's Web site than that disclosed on Form N–CR?

• As proposed, should we require this information to be posted ''prominently'' on the fund's Web site? Should we provide any other instruction as to the presentation of this information, in order to highlight the information and/or lead investors efficiently to the information, for example, should we require that the information be posted on the fund's home page or be accessible in no more than two clicks from the fund's home page?

• Should this information be posted on the fund's Web site for a longer or shorter period than one year following the date on which the fund filed Form N–CR to disclose any of the events specified in Part E, F, or G of Form N–CR?

• Besides requiring a money market fund that imposes a liquidity fee or gate to file a prospectus supplement and include related disclosure on the fund's Web site, should we also require the fund to notify shareholders individually about the effects of the fee or gate? Should we require a fund to engage in any other supplemental shareholder communications, such as issuing a press release or disclosing the fee or gate on any form of social media that the fund uses?

• How will the disclosure of the imposition of a fee or gate affect the willingness of current or prospective investors to purchase shares of the fund? How will this disclosure affect investors' purchases and redemptions in other funds? How will it affect other market participants? Will these effects differ based on the number of funds that concurrently impose fees and/or gates?

d. Historical Disclosure of Liquidity Fees and Gates

We also believe that money market funds' current and prospective shareholders should be informed of post-compliance-period historical occasions in which the fund's weekly liquid assets have fallen below 15% or the fund has imposed liquidity fees or redemption gates. While we recognize that historical occurrences are not necessarily indicative of future events, we anticipate that current and prospective fund investors could use this information as one factor to compare the risks and potential costs of investing in different money market funds.

We are therefore proposing an amendment to Form N–1A to require money market funds (other than government money market funds that have chosen to rely on the proposed rule 2a–7 exemption from the fees and gates requirements) to provide disclosure in their SAIs regarding any occasion during the last 10 years (but not before the compliance period) on which the fund's weekly liquid assets have fallen below 15%, and with respect to each such occasion, whether the fund's board of directors determined to impose a liquidity fee and/or suspend the fund's redemptions.[450] With respect to each occasion, we propose requiring funds to disclose: (i) The length of time for which the fund's weekly liquid assets remained below 15%; (ii) the dates and length of time for which the fund's board of directors determined to impose a liquidity fee and/or temporarily suspend the fund's redemptions; and (iii) a short discussion of the board's analysis supporting its decision to impose a liquidity fee (or not to impose a liquidity fee) and/or temporarily suspend the fund's redemptions.[451] We would expect that this disclosure could include (as applicable, and taking into account considerations regarding the confidentiality of board deliberations) a discussion of the following factors relating to the board's decision to impose a liquidity fee and/or suspend redemptions: The fund's shadow price; relevant market indicators of liquidity stress in the markets; changes in spreads for portfolio securities; the fund's future liquidity profile (taking into account predicted redemptions and other expectations); the fund's ability to apply any collected fees quickly to rebuild fund liquidity; and the predicted time for portfolio securities to mature and provide internal liquidity to the fund, and for potentially distressed portfolio securities to mature or recover. The required disclosure would permit current and prospective shareholders to assess, among other things, any patterns of stress experienced by the fund, as well as whether the fund's board has previously imposed fees and/or redemption gates in light of significant drops in portfolio liquidity. This disclosure also would provide investors with historical information about the board's past analytical process in determining how to handle liquidity issues when the fund experiences stress, which could influence an investor's decision to purchase shares of, or remain invested in, the fund. In addition, the required disclosure may encourage portfolio managers to increase the level of daily and weekly liquid assets in the fund, as that would tend to lessen the likelihood of a liquidity fee or gate being needed, and the fund being required to disclose the fee or gate to current and prospective investors.[452]

We request comment on the proposed requirement for money market funds to include SAI disclosure regarding the historical occasions in which the fund's weekly liquid assets have fallen below 15% or the fund has imposed liquidity fees or redemption gates.

• Would the proposed disclosure requirement assist current and prospective fund investors in comparing the risks and potential costs of investing in different money market funds, and would retail investors as well as

money market reforms adopted by the Commission in 2010, as well as daily disclosure of market value per share); *see also infra* note 659 (discussing recent decisions by a number of money market fund firms to begin reporting funds' daily shadow prices on the fund Web site).

[449] *See* 17 CFR 230.497.

[450] *See* proposed (Fees & Gates) Item 16(g)(1) of Form N–1A. We believe that the proposed 10-year look-back period would provide shareholders and the Commission with a historical perspective that would be long enough to provide a useful understanding of past events, and to analyze patterns with respect to fees and gates, but not so long as to include circumstances that may no longer be a relevant reflection of the fund's management or operations.

[451] *See* instructions to proposed (Fees & Gates) Item 16(g)(1) of Form N–1A.

[452] *See supra* note 365.

institutional investors benefit from the proposed disclosure? Would the proposed requirement to include a short discussion of the board's analysis supporting its decision whether to impose a fee or suspend redemptions result in meaningful and succinct disclosure? Should any more, any less, or any other disclosure be required to be included in the fund's SAI? Should the disclosure instead be required in the prospectus?

• Keeping in mind the compliance period we propose,[453] should the ''look-back'' period for this historical disclosure be longer or shorter than 10 years?

• Should the proposed SAI disclosure be permitted to be incorporated by reference in a fund's registration statement, on account of the fact that funds will have previously disclosed the information proposed to be required in this SAI disclosure on Form N–CR? [454]

• Should we require this historical disclosure to be included anywhere else, for example, on the fund's Web site?

e. Prospectus Fee Table

Under the proposed liquidity fees and gates alternative, a liquidity fee would only be imposed when a fund experiences stress (*i.e.,* we believe that shareholders would not pay the liquidity fee in connection with their typical day-to-day transactions with the fund under normal conditions and many funds may never need to impose the fee). Because funds are anticipated to rarely, if at all, impose this fee,[455] we do not believe that the prospectus fee table, which is intended to help shareholders compare the costs of investing in different mutual funds, should include the proposed liquidity fee.[456] Therefore, we propose clarifying in the instructions to Item 3 of Form N–1A (''Risk/Return Summary: Fee Table'') that the term ''redemption fee,'' for purposes of the prospectus fee table, does not include a liquidity fee that may be imposed in accordance with rule 2a–7.[457] As discussed above, we do believe that shareholders should be able to compare the extent to which money market funds have historically imposed liquidity fees, and to this end, we have proposed SAI amendments requiring this disclosure.[458] Also, as previously discussed, funds would disclose in the summary section of the statutory prospectus (and, accordingly, any summary prospectus, if used) that they may impose a liquidity fee, and also would include a detailed description of the size of the fees, and when the fees might be imposed, elsewhere in the statutory prospectus.[459]

We request comment on the proposed Form N–1A instruction that would clarify that, for purposes of the prospectus fee table, the term ''redemption fee'' does not include a liquidity fee imposed in accordance with rule 2a–7.

• Would shareholders find it instructive for funds to disclose the proposed liquidity fee in the prospectus fee table? Why or why not? If we were to require money market funds to include liquidity fees in the fee table, how should the fee table account for the contingent nature of liquidity fees and inform investors that liquidity fees will only be imposed in certain circumstances? Should the possibility of a liquidity fee be disclosed in a footnote of the fee table? Should a cross-reference to the fund's SAI disclosure regarding historical occasions on which the fund has imposed liquidity fees be disclosed in a footnote of the fee table?

• Would the proposed SAI amendments requiring disclosure of the historical occasions on which the fund has imposed liquidity fees be an effective way for shareholders to compare the extent to which money market funds have historically imposed liquidity fees, and analyze the probability that a fund will impose such fees in the future?

f. Economic Analysis

The liquidity fees and gates proposal makes significant changes to the nature of money market funds as an investment vehicle. The proposed disclosure requirements in this section are intended to communicate to shareholders the nature of the risks that follow from the liquidity fees and gates proposal. In section III.B, we discussed why we are unable to estimate how the liquidity fees and gates proposal will affect shareholders' use of money market funds or the resulting effects on the short-term financing markets because we do not have the information necessary to provide a reasonable estimate. For similar reasons, we are unable to estimate the incremental effects that the proposed disclosure requirements will have on either shareholders or the short-term financing markets. However, we believe that the proposed disclosure will better inform shareholders about the changes, which should result in shareholders making investment decisions that better match their investment preferences. We expect that this will have similar effects on efficiency, competition, and capital formation as those outlined in section III.E rather than to introduce new effects. We further believe that the effects of the proposed disclosure requirements will be small relative to the liquidity fees and gates proposal. The Commission staff has not measured the quantitative benefits of these proposed requirements at this time because of uncertainty about how increased transparency may affect different investors' understanding of the risks associated with money market funds.[460] Where it is relevant, we request the data needed to make these calculations below.

We anticipate that money market funds would incur costs to amend their registration statements, and to update their advertising and sales materials (including the fund Web site), to include the proposed disclosure statement. We also anticipate that money market funds (besides government money market funds that have chosen to rely on the proposed rule 2a–7 exemption from the fees and gates requirements) would incur costs to (i) amend their registration statements to incorporate disclosure regarding the effects of fees and gates on redemptions; (ii) include disclosure of the post-compliance-period historical occasions in which the fund's weekly liquid assets have fallen below 15% or the fund has imposed liquidity fees or gates; and (iii) update the prospectus fee table. These funds also would incur costs to disclose current instances of liquidity fees or gates on the fund's Web site. These costs would include initial, one-time costs, as well as ongoing costs. Our staff estimates that the average one-time costs for a money market fund (except government money market funds that have chosen to rely on the proposed rule 2a–7 exemption from the fees and

[453] *See infra* section III.N.

[454] *See* proposed (Fees & Gates) Form N–CR Parts E, F, and G.

[455] *See supra* text following note 383.

[456] Instruction 2(b) to Item 3 of Form N–1A currently defines ''redemption fee'' to include any fee charged for any redemption of the Fund's shares, but does not include a deferred sales charge (load) imposed upon redemption.

[457] *See* instruction 2(b) to proposed (Fees & Gates) Item 3 of Form N–1A.

[458] *See supra* notes 450 and 451 and accompanying text.

[459] *See supra* notes 429, 431 and 440 and accompanying text.

[460] Likewise, uncertainty regarding how the proposed disclosure may affect different investors' behavior makes it difficult for the SEC staff to measure the quantitative benefits of the proposed requirements. With respect to the proposed disclosure statement, there are many possible permutations on specific wording that would convey the specific concerns identified in this Release, and the breadth of these permutations makes it difficult for SEC staff to test how investors would respond to each wording variation.

gates requirements) to comply with these proposed disclosure amendments would be approximately $1,480, and that the average one-time compliance costs for a government money market fund that has chosen to rely on the proposed rule 2a–7 exemption from the fees and gates requirements would be approximately $592.[461]

Ongoing compliance costs include the costs for money market funds periodically to update disclosure in their registration statements regarding historical occasions in which the fund's weekly liquid assets have fallen below 15% or the fund has imposed fees or gates, and also to disclose current instances of any of these events on the fund's Web site. Because the required registration statement and Web site disclosure overlaps with the information that a fund must disclose on Form N–CR when the fund's weekly liquid assets fall below 15%, or the fund imposes or removes a fee or gate,[462] we anticipate that the costs a fund will incur to draft and finalize the disclosure that will appear in its registration statement and on its Web site will largely be incurred when the fund files Form N–CR, as discussed below in section III.G.3. In addition, we estimate that a fund (besides a government money market fund that has chosen to rely on the proposed rule 2a–7 exemption from the fees and gates requirements) would incur average annual costs of $296 [463] to review and update the historical disclosure in its registration statement (plus printing costs), and costs of $207 [464] each time that it updates its Web site to include the required disclosure.

We request comment on this economic analysis:

- Are any of the proposed disclosure requirements unduly burdensome, or would they impose any unnecessary costs?
- We request comment on the staff's estimates of the operational costs associated with the proposed disclosure requirements.
- We request comment on our analysis of potential effects of these proposed disclosure requirements on efficiency, competition, and capital formation.

9. Alternative Redemption Restrictions

a. Stand-Alone Liquidity Fees or Stand-Alone Gates

We are proposing that money market fund boards of directors be permitted to institute liquidity fees or gates (and potentially one followed by the other). This proposal is designed to provide money market funds with multiple tools to manage heightened redemptions in the best interest of the fund and to mitigate potential contagion effects on the short-term financing markets for issuers.

We also have considered whether we should permit these money market funds to institute only liquidity fees or only gates. As discussed above, fees and gates can accomplish somewhat different objectives and have somewhat different tradeoffs and effects on shareholders and the short-term financing markets for issuers. For shareholders valuing principal preservation in their evaluation of money market fund investments, a gate may be preferable to a liquidity fee particularly if the fund expects to rebuild liquidity through maturing assets. In contrast, shareholders preferring liquidity over principal preservation may prefer a liquidity fee because it allows full liquidity of that investor's money market fund shareholdings—it just imposes a greater cost for that liquidity if the fund is under stress.[465]

Because fees and gates can accomplish somewhat different objectives and one may be better suited to one set of market circumstances than the other, we preliminarily believe that providing funds with the ability to use either tool, as the board determines is in the best interest of the fund, is a better approach to preserve the benefits of money market funds for investors and the short-term financing markets for issuers, enhance investor protection, and improve money market funds' ability to manage and mitigate high levels of redemptions. It also may better allow funds to tailor the redemption restrictions they employ to their experience with the preferences and behavior of their particular shareholder base and to adapt the restriction they institute as they or the industry gains experience over time employing such restrictions. We request comment on stand-alone liquidity fees or stand-alone gates.

- Should we adopt rule amendments that would just permit money market funds to institute liquidity fees or just permit these money market funds to institute a gate? Why might it be preferable to allow only a fee or only a gate? If we allowed only a fee or only a gate, should there be different parameters or restrictions around when the fee or gate could be imposed or lifted than what we have proposed? If so, what should they be and why?

b. Partial Gates

We are proposing to permit money market funds to institute a complete gate in certain circumstances—a temporary suspension of redemptions. Some have suggested that we allow money market funds to impose partial gates in times of stress.[466] For example, once the money market fund had crossed the 15% weekly liquid asset threshold, we could permit the board of directors (including a majority of its independent directors) to limit redemptions by any particular shareholder to a certain percentage of their shareholdings, to a certain percentage of the fund's outstanding shares, or to a certain dollar amount per day. Those limited redemptions would not be charged a liquidity fee.

A partial gate can operate to prevent ''fire sales'' of assets in the fund and provide some liquidity to investors while allowing time for the fund to satisfy the remaining portion of redemptions requests under better market conditions or with internally generated liquidity. It can act as a gradual brake on redemptions, reducing

[461] Staff estimates that these costs would be attributable to amending the fund's disclosure statement and updating the fund's advertising and sales materials. *See supra* note 245 (discussing the bases of our staff's estimates of operational and related costs). The costs associated with these activities are all paperwork-related costs and are discussed in more detail in *infra* section IV.B.7.

We expect the new required disclosure would add minimal length to the current required registration statement disclosure, and thus would not increase the number of pages in, or change the printing costs of, a fund's registration statement. Based on conversations with fund representatives, the Commission understands that, in general, unless the page count of a registration statement is changed by at least four pages, printing costs would remain the same.

[462] *See* proposed (Fees & Gates) Form N–CR Parts E, F, and G.

[463] The costs associated with updating the fund's registration statement are paperwork-related costs and are discussed in more detail in *infra* section IV.B.7.

[464] The costs associated with updating the fund's Web site are paperwork-related costs and are discussed in more detail in *infra* section IV.B.1.g.iv.

[465] *See, e.g.,* Comment Letter of BlackRock, Inc. on the IOSCO Consultation Report on Money Market Fund Systemic Risk Analysis and Reform Options (May 28, 2012), *available at http://www.iosco.org/library/pubdocs/pdf/IOSCOPD392.pdf.* (stating their preference for liquidity fees over gates ''because clients with an extreme need for liquidity can choose to pay for that liquidity in a crisis''); BNP Paribas IOSCO Comment Letter, *supra* note 357 (stating that it ''would not make sense to restrict the redeemer willing to pay the price of liquidity'').

[466] *See, e.g.,* HSBC EC Letter, *supra* note 156 (stating that a money market fund should be able to limit the total number of shares that the fund is required to redeem on any trading day to 10% of the shares in issue, that any such gate be applied pro rata to redemption requests, and that any redemption requests not met be carried over to the next business day and so forth until all redemption requests have been met).

them to the extent that they no longer impact the fund's value or liquidity. In doing so, they can have a less severe impact on fund shareholders because they know they will be able to redeem without cost at least a certain portion of their investment on any particular day, even in times of stress. A partial gate could be imposed in lieu of a liquidity fee or could be combined with a liquidity fee (*e.g.,* once the fund imposed a partial gate, a shareholder could redeem 10% of their shareholdings at no cost and the rest of their shareholdings by paying a liquidity fee). Similarly, we could consider adopting a partial gate in lieu of our full gate proposal or as an additional tool that would be available to fund boards on the same terms as a full gate is available.

On the other hand, a partial gate may not impose a substantial enough deterrent on redemption activity in times of stress to effectively reduce the contagion impact of heavy redemptions on remaining investors and the short-term financing markets. For example, in 2007 when a Florida local government investment pool suspended redemptions in response to a run, it re-opened with a combined partial gate and liquidity fee—local governments could take out the greater of 15% of their holdings or $2 million without penalty, and the remainder of any redemptions were subject to a 2% redemption fee.[467] We understand that only a few investors redeemed more than what was allowed without a fee, but that investors redeemed most of what was allowed under the partial gate without triggering the redemption fee.[468] We also are concerned that a partial gate would operate in substantially the same manner as an exemption from the fee or gate requirement for small withdrawals, discussed above in section III.B.5, and thus may be subject to many of the same drawbacks in terms of operational costs and added complexity compared to our liquidity fees and gates proposal.

We request comment on whether we should require or permit partial gates in certain circumstances.

- Should we allow partial gates? If so, why? Under what conditions and of what nature? Should they limit each shareholder's redemptions to a certain percentage of his or her shareholdings (*e.g.,* 10% or 25%), to a certain percentage of the fund's outstanding shares (*e.g.,* 1% or 5%), or to a certain dollar amount per day (*e.g.,* $10,000 or $50,000)? If so, what percentage or dollar amount and why?
- How would partial gates affect shareholder redemption decisions compared to our proposal of liquidity fees and full gates? Would they achieve our goals of preserving the benefits of money market funds for investors and the short-term financing markets for issuers, while mitigating the risk of runs, enhancing investor protection and improving money market funds' ability to manage and mitigate high levels of redemptions to the same extent as our proposed liquidity fees and gates? Why or why not?
- If we allowed partial gates, should they be allowed in addition to liquidity fees and full gates or in lieu of fees or full gates? What operational and other costs would be involved if we allowed partial gates in addition to or in lieu of fees and/or full gates?

c. In-Kind Redemptions

In 2009, we requested comment on requiring that funds satisfy redemption requests in excess of a certain size through in-kind redemptions.[469] We also requested comment on this type of redemption restriction when we requested comment on the PWG Report.[470] In-kind redemptions might lessen the effect of large redemptions on remaining money market fund shareholders, and they would ensure that the redeeming investors bear part of the cost of their liquidity needs. During the 2008 financial crisis, one money market fund stated that it would honor certain large redemptions in-kind in an attempt to decrease the level of redemptions in that fund.[471]

In both instances, almost all commenters addressing this potential reform option opposed it.[472] Most commenters believed that requiring in-kind redemptions would be technically unworkable due to the complex valuation and operational issues that would be imposed on both the fund and on investors receiving portfolio securities.[473] They also asserted that required in-kind redemptions could result in disrupting, rather than stabilizing, markets if redeeming shareholders needing liquidity were forced to sell into declining markets.[474] Several commenters stated that investors would dislike the prospect of receiving redemptions in-kind and would structure their holdings to avoid the requirement, but would nevertheless still collectively engage in redemptions if the money market funds were to come

[467] *See* David Evans and Darrell Preston, *Florida Investment Chief Quits; Fund Rescue Approved,* Bloomberg (Dec. 4, 2007).

[468] *See, e.g.,* Neil Weinberg, *Florida Fund Meltdown: Bad to Worse,* Forbes (Dec. 6, 2007) (noting that investors withdrew $1.2 billion from the $14 billion pool after it re-opened, while depositing only $7 million, but that only 3 out of about 1,700 participants in the pool chose to pay the redemption fee to withdraw additional assets).

[469] *See* 2009 Proposing Release, *supra* note 31, at section III.B. An in-kind redemption occurs when a shareholder's redemption request to a fund is satisfied by distributing to that shareholder portfolio assets of that fund instead of cash.

[470] *See* PWG Report, *supra* note 111, at section 3.c (discussing requiring that money market funds satisfy certain redemptions in-kind).

[471] *See* 2009 Proposing Release, *supra* note 31, at n.309.

[472] *But see* Comment Letter of Forward Management (Aug. 21, 2009) (available in File No. S7–11–09) (supporting in-kind redemption requirement); Comment Letter of the American Bar Association (Committee on Federal Regulation of Securities) (Sept. 9, 2009) (available in File No. S7–11–09) (same). In addition, two PWG Report commenters expressed concern that redemptions in-kind would be technically unworkable, but were open to further examination of this option. *See* Comment Letter of Invesco Advisers, Inc. (Jan. 10, 2011) (available in File No. 4–619) (''We have previously expressed our concern that requiring money market funds to satisfy redemptions in-kind under certain circumstances would likely be technically unworkable and could result in disrupting, rather than stabilizing, markets. While we continue to harbor these concerns, we would be supportive in principle of a mandatory in-kind redemption requirement if these technical challenges could be addressed successfully in a partnership with regulatory authorities.''); Comment Letter of Federated Investors, Inc. (Jan. 7, 2011) (available in File No. 4–619) (''Federated Jan 2011 PWG Comment Letter'') (''we have identified some of the major problems associated with redemption in-kind and included these in our comment letter to the Commission on the recent money market fund reforms. . . . At the appropriate time, we would be willing to meet with the Commission or its staff to review our analysis of the issues raised in responding to such events and to discuss approaches to resolving these issues.'').

[473] *See, e.g.,* Comment Letter of BlackRock Inc. (Jan. 10, 2011) (available in File No. 4–619) (''BlackRock PWG Comment Letter''); Comment Letter of The Dreyfus Corporation (Jan. 10, 2011) (available in File No. 4–619) (''Dreyfus PWG Comment Letter''); Comment Letter of Investment Company Institute (Jan. 10, 2011) (available in File No. 4–619) (''ICI Jan 2011 PWG Comment Letter''); Comment Letter of Fidelity Investments (Jan. 10, 2011) (available in File No. 4–619) (''Fidelity Jan 2011 PWG Comment Letter''). For example, the BlackRock PWG Comment Letter stated that some shareholders cannot receive and hold direct investments in money market assets and some portfolio securities, such as repurchase agreements and Eurodollar time deposits, are OTC contracts and cannot be transferred to retail or to multiple investors. The Fidelity Jan 2011 PWG Comment Letter added that advisers may only be able to transfer the most liquid securities, leaving a less liquid portfolio for non-redeeming shareholders and with odd-lot positions that are more difficult and expensive to trade.

[474] *See, e.g.,* Comment Letter of Goldman Sachs Asset Management, L.P. (Jan. 10, 2011) (available in File No. 4–619) (''a potential result of forced in-kind redemptions is simply to transfer the selling responsibility from presumably sophisticated and experienced asset managers to a disparate group of investors who do not necessarily have any reason to know how to dispose of these securities effectively''); Comment Letter of SVB Asset Management (Jan. 10, 2011) (available in File No. 4–619); Comment Letter of T. Rowe Price Associates, Inc. (Jan. 10, 2011) (available in File No. 4–619).

under stress with similar adverse consequences for the funds and the short-term financing markets.[475]

These comments led us to believe that requiring in-kind redemptions would create operational difficulties that could prevent funds from operating fairly to investors in practice and that it would not necessarily mitigate money market funds' susceptibility to runs and related adverse effects on the short-term financing markets and capital formation. Thus, we expect that the liquidity fees and gates approach described above would better achieve our goals of preserving the benefits of money market funds for investors and the short-term financing markets for issuers while enhancing investor protection and improving money market funds' ability to manage and mitigate potential contagion from high levels of redemptions. Liquidity fees and gates also may be easier to implement than required in-kind redemptions. We request comment on whether we are correct in our analysis of the relative merits and costs of in-kind redemptions as compared to the other forms of redemption restrictions described in this Release as well as any others that money market funds could seek to impose.

We also request comment on all the redemption restriction alternatives discussed in this Release.

- Are there other alternatives that we should consider? Do commenters agree with our discussion about the advantages and disadvantages of the various alternatives? Do commenters agree with our discussion of their potential benefits and costs and other economic effects?

*C. Potential Combination of Standby Liquidity Fees and Gates and Floating Net Asset Value*

Today, we are proposing two alternative methods of reforming money market funds. Although these two proposals are designed to achieve many of the same goals, by their nature they would do so to different degrees and with different tradeoffs. As discussed above, our first alternative would require money market funds (other than government and retail funds) to adopt floating NAVs. This proposal is designed primarily to address the incentive for shareholders to redeem shares ahead of other investors in times of fund and market stress. It also is intended to improve the transparency of funds' investment risks through more transparent valuation and pricing methods. It makes explicit the risk and reward relation for money market funds. We recognize, however, that the proposal does not necessarily address shareholders' incentive to redeem from money market funds due to their liquidity risk or for other reasons as discussed below. In times of severe market stress when the secondary markets for funds' assets become illiquid, investors may still have incentives to redeem shares before their fund's liquidity dries up. It also may not alter money market fund shareholders' incentive to redeem in times of market stress when investors are engaging in flights to quality, liquidity, and transparency and the related contagion effects from such high levels of redemptions.

Our second proposal, which requires funds to impose liquidity fees unless the fund's board determines that it would not be in the best interest of the fund and permits them to impose gates in certain circumstances, is primarily focused on helping money market funds manage heightened redemptions and reducing shareholders' incentive to redeem under stress. It also could improve the transparency of funds' liquidity risks through a more transparent and systematic allocation of liquidity costs. In doing so, it addresses a principal drawback of our floating NAV proposal by imposing a cost on redemptions in times of market stress that may incorporate not just investment risk but also liquidity risk. The prospect of facing liquidity fees and gates will give the additional benefit of better informing and sensitizing investors to the risks of investing in money market funds. We recognize, however, that our liquidity fees and gates proposal does not entirely eliminate the incentive of shareholders to redeem when the fund's shadow price falls below a dollar. Moreover, it does not eliminate the lack of valuation transparency in the pricing of money market funds and any corresponding lack of shareholder appreciation of money market fund valuation risks.

We are considering addressing the limitations of the two proposals by combining them into a single reform package; that is, requiring money market funds (other than government money market funds and, regarding the floating NAV, retail money market funds) to both use a floating NAV and potentially impose liquidity fees or gates in times of fund and market stress.[476] Doing so would address some of the drawbacks of each proposal individually, but would present other tradeoffs, as further discussed below.

1. Potential Benefits of a Combination

A combined reform approach could reduce investors' incentive to quickly redeem assets from money market funds in a crisis, improve the transparency of funds' investment and liquidity risks, and enhance money market funds' ability to manage and mitigate potential contagion from high levels of redemptions relative to either proposal alone. Under a combined approach, the floating NAV should reduce investors' incentive to redeem early to avoid a market-based loss embedded in the fund's portfolio because the fund would be transacting at the fair value of its portfolio at all times. Doing so should reduce the likelihood that investors engage in preemptive redemptions that could trigger the imposition of fees and gates.[477] Requiring a fund to operate with a floating NAV with potential imposition of fees and gates in times of fund or market stress should thus reduce the risk that funds would face heavy redemptions. Early redeeming shareholders would be less likely to be able to exit the fund without bearing the cost of their redemptions, and thereby it will be less likely to concentrate losses for the remaining shareholders. At the same time, requiring a floating NAV fund to consider imposing liquidity fees or impose gates when the fund's liquidity buffer comes under strain should enhance its ability to manage its liquidity risk before it results in portfolio losses.

The combination would provide a broader range of tools to a floating NAV money market fund to manage redemptions in a crisis, thereby avoiding ''fire sales'' of assets that would affect all shareholders and potentially the short-term financing markets for issuers. The combined approach also should further enhance the ability of money market funds to treat shareholders equitably, and could allow better management of funds' portfolios in a crisis to minimize shareholder losses.

Requiring funds that can impose liquidity fees and gates to have a floating NAV provides fuller transparency of fund valuation and

[475] *See, e.g.,* ICI Jan 2011 PWG Comment Letter, *supra* note 473; Richmond Fed PWG Comment Letter, *supra* note 139; Comment Letter of Wells Fargo Funds Management, LLC (Jan. 10, 2011) (available in File No. 4–619) (''Wells Fargo PWG Comment Letter'').

[476] As discussed in *supra* section III.A.4, retail money market funds would also be exempt from our proposed floating NAV requirement.

[477] *See supra* section III.B.1 (discussing shareholders' potential incentive to engage in preemptive redemptions in a stable price money market fund that can impose fees or gates).

liquidity risk. This enhanced transparency may better inform investors to the risk profile of their money market fund investment, and may make investors less sensitive to fluctuations in a money market fund's NAV. As a result of this familiarity with money market fund NAV fluctuations, investors may be less likely to redeem shares in times of fund and market stress because of the possibility that a fund's NAV might change, and correspondingly reducing the chances that fees or gates may be triggered.[478] Liquidity fees also can encourage funds to better and more systematically manage liquidity and redemption activity and encourage shareholders to monitor and exert market discipline over the fund to reduce the likelihood that the imposition of fees or gates will become necessary in that fund.

We request comment on the potential benefits of combining our two alternatives into a single proposal.

- Would combining the floating NAV alternative with the liquidity fees and gates alternative have the benefits we discuss above? Are there any other benefits that we have not discussed? If so, what would they be?
- Would combining the floating NAV alternative with only liquidity fees or only gates provide different benefits?

2. Potential Drawbacks of a Combination

Some drawbacks may result from combining the two proposals.[479] One potential drawback is that combining a floating NAV with liquidity fees and gates does not preserve the benefits of stable price money market funds for investors as our liquidity fees and gates alternative does. Although any combination likely would include an exemption to the floating NAV requirement for government and retail money market funds,[480] most other money market funds would have a floating NAV, thereby incurring the costs and operational issues associated with that proposal. As discussed more fully in the section on that alternative, some investors may be deterred from investing in a floating NAV fund for a variety of reasons. We have designed our liquidity fees and gates alternative in large part to preserve the benefits of stable price funds for those investors while enhancing investor protection and improving money market funds' ability to manage and mitigate potential contagion from high levels of redemptions. Combining the proposals thus may not fully accomplish our goal of preserving the current benefits of money market funds.

Another drawback of combining the two proposals is that if a floating NAV significantly changes investor expectations regarding money market fund risk and their prospect of suffering losses, requiring funds with a floating NAV to also be able to impose standby liquidity fees and gates may be unnecessary to manage the risks of heavy redemptions in times of crisis. Because of the unique features of stable price money market funds, liquidity fees and gates may be necessary for a fund to ensure that all of its shareholders are treated the same, while also managing the risks of contagion from heavy redemptions. A fund with a floating NAV may not face these same risks and thus providing those funds with the ability to impose fees or gates may not be justified, particularly in light of the Investment Company Act's expressed preference for full redeemability of open-end fund shares.[481]

A last potential drawback is that although some investors may be comfortable investing in a money market fund that has *either* a floating NAV or liquidity fees and gates, some investors may not wish to invest in a fund that has *both* features because a fund that does not have a stable price and also may restrict redemptions may not be suitable as a cash management tool for such investors. The combination of our proposals may result in these investors looking to other investment alternatives that offer principal stability or that do not also have potential restrictions on redemptions. We discuss the potential effects of such a shift in section III.E below.

We request comment on the potential drawbacks of combining our two alternatives into a single proposal.

- Would combining the floating NAV alternative with the liquidity fees and gates alternative have the drawbacks we discuss above? Are there any other drawbacks that we have not discussed? If so, what would they be?
- Would combining the floating NAV alternative with only liquidity fees or only gates impose different costs?

3. Effect of Combination

As discussed above, each of the alternatives that we are proposing today achieves similar goals, in different ways, but they bear distinct costs. Accordingly, if we were to combine the two proposals, while there is the likelihood that a combination may in some ways improve on each alternative standing alone, the combination would impose two separate sets of costs on funds, investors, and the markets. We request comment on whether the benefit of combining the two alternatives into a single reform would justify the drawbacks of imposing two distinct sets of costs and economic impacts.

- Should we combine the two alternatives as a single reform? What would be the advantages and drawbacks of such a combination? Would the benefits of combining the proposals justify requiring the two individual sets of costs associated with implementing the combined alternatives? Would the imposition of two sets of costs materially impact the decisions of money market fund sponsors on whether or not they would continue to offer the product?

4. Operational Issues

Combining the two alternatives into a single approach could pose certain operational issues and raise questions about how we should structure such a reform. These issues are discussed below.

a. Fee Structure

Under our liquidity fees and gates proposal, the board of directors of a money market fund would be required to impose a liquidity fee (unless they find that not doing so would be in the best interest of the fund) if the fund's weekly liquid assets fell below 15% of its total assets. The default liquidity fee would be 2% unless the board determined that a lesser fee would be in the best interest of fund shareholders.

The liquidity fees imposed by a floating NAV fund may serve different purposes than those of a stable price fund. A stable price fund board, for example, might use liquidity fees to recoup the costs associated with selling assets at distressed prices in an illiquid market to meet redemptions, as well as to help repair the fund's NAV. In contrast, a floating NAV fund board might choose to impose liquidity fees only to recoup the costs associated with selling assets at distressed prices. This difference in the purpose served by liquidity fees raises questions about the appropriate default size of a liquidity fee for the combined proposal, the

[478] *See supra* section III.A.1.

[479] One commenter noted their opposition to combining redemption gates with a floating NAV, arguing that such a combination "acknowledges that the floating NAV does not resolve such first mover advantage." *See* Dreyfus FSOC Comment Letter, *supra* note 174.

[480] *See supra* sections III.A.3 and III.A.4. In any combination, retail funds would likely be subject to fees and gates, although exempt from the floating NAV, and thus would not be exempt from both provisions as government funds likely would.

[481] *See* 15 U.S.C. 80a–2(a)(32) and 80a–22(e); *see also supra* note 395.

appropriate thresholds for triggering imposition of the fee, and the thresholds for removing it.

We request comment on the structure of the default liquidity fee if applied to a floating NAV money market fund.

• Should we alter the default liquidity fee for the combined proposal? Should we specify a default fee for the combined proposal or merely require that a fee be based on the costs incurred by the fund selling assets to meet redemptions? We previously noted issues that can arise with variable liquidity fees.[482] Would these issues be of concern in the context of a floating NAV fund?

• Should we contemplate different percentages for funds to consider before applying liquidity fees or gates to a floating NAV money market fund than weekly liquid assets falling below 15%? If so, what percentages should we consider. Should we consider a different threshold for automatic removal of liquidity fees other than recovery of a fund's liquidity to 30% weekly liquid assets? If so, what should the threshold for removal be?

• Should a liquidity fee in a floating NAV fund be triggered by a different factor other than weekly liquid assets falling below 15%, such as a change in NAV? If so, should such a trigger be based on a relative percentage change in NAV over some time period or on an absolute change since a fund's inception? For example, should a liquidity fee be triggered if a fund's NAV falls by more than ¼ of 1% in a week? Alternatively, should a liquidity fee be triggered if a fund's NAV falls by more than a certain number of basis points? If based on an absolute number, what should the number be? A drop in NAV of more than 25 basis points from its initial starting price or another number? What types of issues do the two options present? What other types of thresholds should be considered? What issues would arise from using other thresholds?

b. Redemption gates

Under our liquidity fees and gates alternative, a fund would have the option of imposing temporary redemption gates if liquidity falls below the same threshold that it imposes liquidity fees. These redemption gates are designed to act as ''circuit breakers'' to halt redemptions, thereby allowing funds to minimize losses to all shareholders and reducing any associated contagion risks. Most of the concerns that redemption gates are designed to address in a stable price money market fund also apply to a floating NAV money market fund, and gates should be similarly useful in addressing them. Much like a stable price fund, a floating NAV fund may also face difficulties managing heavy redemptions in times of stress, and redemption gates may work to mitigate these difficulties. Gates, by halting redemptions, would provide ''breathing room'' for investors to take better stock of a situation. Conversely, redemption gates may not be in the interest of investors who rationally wish to redeem at the time, or who want immediate liquidity.

• Do redemption gates on a floating NAV fund pose any particular issues or provide any specific benefits different than those associated with gates in a stable price fund? If so, what are they?

• If we were to combine the two alternatives and permit redemption gates on a floating NAV fund, should the thresholds be the same as for imposing liquidity fees? If not, what should they be? Should they be tied to redemption activity? Drops in NAV?

• Should the length of time permitted for redemption gates in a floating NAV fund be the same as that permitted under the standalone alternative? Should floating NAV funds be permitted to gate redemptions for a longer or shorter time? If so, why?

• If the proposals were combined, would a partial gate be appropriate?

c. Floating NAV Combined with only Liquidity Fees or only Gates

If we were to combine the alternatives, we could also do so in a partial manner, requiring money markets to maintain a floating NAV and combining it with standby liquidity fees standing alone. Similarly, we could instead require that a floating NAV fund be able to impose gates, but not liquidity fees. Combining a floating NAV with just liquidity fees or gates may simplify operational implementation of the combination and make money market funds more attractive to investors. On the other hand, such a limited combination may not achieve the goals of the proposed reform to the same extent as a full combination. We request comment on whether, if we were to combine the two alternatives, we should require a floating NAV fund to only have standby liquidity fees or gates, but not both.

• What advantages and disadvantages would result from such a limited combination?

• If we were to pursue a limited combination, which measure should we combine with the floating NAV? Liquidity fees or gates? Why?

d. Choice of Floating NAV or Liquidity Fees and Gates

Another way of combining the floating NAV and fees and gates alternatives discussed in this Release would be to require that money market funds (other than government money market funds) choose to either transact with a floating NAV or be able to impose liquidity fees and gates in times of stress—in other words, each non-government money market fund would have to choose to apply either the floating NAV alternative or the liquidity fees and gates alternative. Providing such a choice may allow each money market fund to choose the reform alternative that is most efficient, cost-effective, and preferable to shareholders. This could enhance the efficiency of our reforms and minimize costs and competitive impacts. On the other hand, allowing such a choice may not achieve the goals of the proposed reform to the same extent as a full combination or mandating one alternative versus another. In addition, in making such a choice, the money market fund industry may not necessarily be incentivized to take into consideration the full likely effects of their decisions on the short-term financing markets, and thus capital formation, or the broader systemic effects of their choices. Funds would need to clearly communicate their choice of approaches to shareholders. We request comment on whether we should permit non-government money market funds to choose to apply either the floating NAV alternative or the fees and gates alternative.

• What advantages and disadvantages would result from permitting such a choice?

• Would permitting such a choice achieve our reform goals to the same extent as either our floating NAV proposal or our fees and gates proposal?

• Would this cause investor confusion because of a fragmentation in the market?

• How should a fund elect to make such a choice? At inception of the fund? Should a fund be permitted to switch elections?

e. Other Issues

The combination of the two alternatives could create other operational issues. For example, we have previously discussed our understanding that a floating NAV fund would meet the definition of a cash equivalent for accounting purposes, because it is unlikely to experience significant fluctuations in value.[483] We

[482] *See supra* section III.B.2.c.

[483] *See supra* section III.A.6.

would expect a fund that combines liquidity fees and gates with a floating NAV should not experience any additional volatility compared to a floating NAV fund alone. That said, in some circumstances, liquidity fees could effectively lower share value, by requiring the payment of fees upon redemption. It is also important to note that gates would potentially compromise liquidity. Nevertheless, we expect the value of floating NAV funds with liquidity fees and gates would be substantially stable and should continue to be treated as a cash equivalent under GAAP.[484] We also do not expect that a combination of the two approaches would result in any novel tax issues that we have not previously discussed in the relevant sections above. We request comment on the implications of combining fees and gates with a floating NAV on tax and accounting issues.

- Would a money market fund that combines a floating NAV with liquidity fees and gates continue to be treated as a cash equivalent under GAAP? If not, why not?
- Would a combination of the alternatives create any additional accounting or any novel tax issues? If so, what would they be?

Under our floating NAV proposal we are proposing that a fund would be required to price to the fourth decimal place if they price their shares at one dollar (*e.g.,* $1.0000), or to an equivalent level of precision if the fund uses another price level. We would require such a level of pricing precision, in part, to ensure that any fluctuations in a fund's NAV are visible to investors.[485] We would expect that the value of such transparency would be unchanged under a combined approach.

- Would such a level of pricing precision be appropriate for a fund that combines liquidity fees and gates with a floating NAV? If not, why not, and what level of pricing precision should be required instead?

As discussed above, we are proposing exemptions under each alternative. Under the floating NAV alternative, we are proposing an exemption for government and retail money market funds. Under the liquidity fees and gates alternative, we are proposing an exemption for government money market funds, but not retail funds. We would expect that a combined approach would also include these exemptions, considering that the reasons we are proposing the exemptions to the floating NAV remain the same in the context of a combined approach. However, our liquidity fees and gates proposal treats government and retail funds differently, and provides an exemption to the liquidity fees and gates proposal for government money market funds, but not for retail funds. For the reasons discussed in the sections where we propose the exemptions, if we were to combine the proposals, we would expect to continue to offer the exemptions provided under each alternative, but would not extend them. Accordingly, a combined approach would likely provide an exemption to the floating NAV *and* to fees and gates for government money market funds, but would provide only an exemption to the floating NAV for retail funds, and *not* an exemption to fees and gates.

- If we were to combine the two alternatives, should we retain the proposed exemptions to the floating NAV requirement for government and retail money market funds? If not, why not?
- Under a combined approach, should we also exempt retail funds from not only the floating NAV but also from the fees and gates requirements? If so, why?

We are also proposing to retain rules 17a–9 and 22e–3 under both of the alternatives we are proposing today, with certain amendments to account for operational differences to rule 22e–3's triggering mechanism.[486] If we were to combine the two alternatives into a single approach, we would expect to make the amendments to the triggering mechanisms of rule 22e–3 we are proposing today (which are the same under each alternative) and retain rule 17a–9 unchanged. As discussed above, we believe that funds would continue to find the ability to sell securities to affiliated persons under rule 17a–9 useful under both alternatives, as well as under a combined approach. We also expect that the amendments we are making to the triggering mechanism permitting a suspension of redemptions in preparation for a fund's liquidation under rule 22e–3 would continue to be appropriate under a combined approach as well.

- Would a combined approach have any significant effects on our proposed treatment of rules 17a–9 and 22e–3? Would we need to make any other changes to those rules to accommodate such a combination?

Our floating NAV alternative includes a compliance period of 2 years to allow for funds to transition to a floating NAV without imposing unnecessary costs.[487] We would expect that any combined approach would include a similar compliance period because funds would likely need a significant amount of time to implement a floating NAV. At the same time, we do not expect that implementing both alternatives would add substantially to the amount of time it would take to implement a floating NAV alone, and accordingly would expect to provide the same compliance period if we were to combine the approaches.

- Should we provide the same compliance period under a combined approach? If not, should the compliance period be longer or shorter? Should we consider a grandfathering approach instead of or in addition to a compliance period?

Under both of the alternatives that we are proposing today, we are also including a variety of proposed disclosure improvements designed to improve transparency of fund risks and risk management, with the relevant disclosure tailored to each alternative. If we were to combine the two approaches, we would likely merge the disclosure reforms, and revise the disclosure requirements to take such a merger into account. We would not expect that a combined approach would require significant additional disclosure reforms not discussed under the two alternatives.

- Would a combined approach pose any new disclosure issues that are not currently contemplated in the discussion of disclosure reforms for each of the two alternatives? If so, what would those issues be? Would a combined approach result in any new or changed risks that investors should be informed of?

We do not expect that there would be any significant additional costs from combining the two approaches that are not previously discussed in the sections discussing the costs of the two alternatives above. It is likely that implementing a combined approach would likely save some percentage over the costs of implementing each alterative separately as a result of synergies and the ability to make a variety of changes to systems at a single time. We do not expect that combining the approaches would create any new costs as a result of the combination itself. Accordingly, we estimate that the costs of implementing a combined approach would at most be the sum of the costs of each alternative, but may likely be less.

[484] *Id.*

[485] *See supra* section III.A.2.

[486] We are proposing to change the trigger for use of rule 22e–3 under both alternatives to a reduction in a fund's weekly liquid assets below 15%. *See supra* section III.A.5.b.

[487] *See supra* section III.A.9.

We request comment on the costs of combining the two approaches.

• Would there be any new costs associated with combining the two approaches that are not already discussed separately under each alternative? If so, what would they be?

• Would there be a reduction in costs as a result of implementing both alternatives at the same time? If so, how much savings would there be?

*D. Certain Alternatives Considered*

In addition to the proposed reforms and alternatives described elsewhere in this Release, it is important to note that in coming to this proposal, we and our staff considered a number of additional alternative options for regulatory reform in this area. For example, we considered each option discussed in the PWG Report and the FSOC Proposed Recommendations. We currently are not pursuing certain of these other options because we believe, after considering the comments we received on the PWG Report and that FSOC received on the FSOC Proposed Recommendations and the economic analysis set forth in this Release, that they would not achieve our regulatory goals as well as what we propose today. We discuss below these options, and our principal reasons for not pursuing them further at this time.

1. Alternatives in the FSOC Proposed Recommendations

As discussed in section II.D.3 above, in November 2012, FSOC proposed to recommend that we undertake structural reforms of money market funds. FSOC proposed three alternatives for consideration, which, it stated, could be implemented individually or in combination. The first option [488]—requiring that money market funds use a floating NAV—is part of our proposal. The other two options in the FSOC Proposed Recommendations each would require that money market funds maintain a NAV buffer. One option would require that most money market funds have a risk-based NAV buffer of up to 1% to absorb day-to-day fluctuations in the value of the funds' portfolio securities and allow the funds to maintain a stable NAV and that this NAV buffer be combined with a ''minimum balance at risk.'' [489] The required minimum size of a fund's NAV buffer would be determined based on the composition of the money market fund's portfolio according to the following formula:

• No buffer requirement for cash, Treasury securities, and repos collateralized solely by cash and Treasury securities (''Treasury repo'');

• A 0.75% buffer requirement for other daily liquid assets (or weekly liquid assets, in the case of tax-exempt money market funds); and

• A 1% buffer requirement for all other assets.

A fund whose NAV buffer fell below the required minimum amount would be required to limit its new investments to cash, Treasury securities, and Treasury repos until its NAV buffer was restored. A fund that completely exhausted its NAV buffer would be required to suspend redemptions and liquidate or could continue to operate with a floating NAV indefinitely or until it restored its NAV buffer.

A money market fund could use any funding method or combination of methods to build the NAV buffer, and could vary these methods over time. The FSOC Proposed Recommendations identified three funding methods that would be possible with Commission relief from certain provisions of the Investment Company Act: (1) An escrow account that a money market fund's sponsor established and funded and that was pledged to support the fund's stable share price; (2) the money market fund's issuance of a class of subordinated, non-redeemable equity securities (''buffer shares'') that would absorb first losses in the funds' portfolios; and (3) the money market fund's retention of some earnings that it would otherwise distribute to shareholders (subject to certain tax limitations).[490] We believe that the first funding method would be the most likely approach for funding the buffer given the complexity of a fund offering a new class of buffer shares (and the uncertainty of an active, liquid market for buffer shares developing) and the tax limitations on the third method.[491] We note, however, that we believe this funding method is the most expensive of the three because of the opportunity costs the fund's sponsor will bear to the extent that the firms redirect this funding from other essential activities, as further discussed below.[492]

The minimum balance at risk (''MBR'') would require that the last 3% of a shareholder's highest account value in excess of $100,000 during the previous 30 days (the shareholder's MBR or ''holdback shares'') be redeemable only with a 30-day delay.[493] All shareholders may redeem 97% of their holdings immediately without being restricted by the MBR. If the money market fund suffers losses that exceed its NAV buffer, the losses would be borne first by the MBRs of shareholders who have recently redeemed (*i.e.,* their MBRs would be ''subordinated''). The extent of subordination of a shareholder's MBR would be approximately proportionate to the shareholder's cumulative net redemptions during the prior 30 days—in other words, the more the shareholder redeems, the more their holdback shares become ''subordinated holdback shares.''

The last option in the FSOC Proposed Recommendations would require money market funds to have a risk-based NAV buffer of up to 3% (which otherwise would have the same structure as discussed above), and this larger NAV buffer could be combined with other measures.[494] The alternative measures discussed in the FSOC Proposed Recommendations include more stringent investment diversification requirements (which are proposed or discussed in section III.J below), increased minimum liquidity levels

[488] *See* FSOC Proposed Recommendations, *supra* note 114, at section V.A.

[489] Under the FSOC Proposed Recommendations, Treasury money market funds would not be subject to a NAV buffer or a minimum balance at risk. *See* FSOC Proposed Recommendations, *supra* note 114, at sections V.B and V.C for a full discussion of these two alternatives. This section of the Release provides a summary based on those sections of the FSOC Proposed Recommendation.

[490] *See* FSOC Proposed Recommendations, *supra* note 114, at section V.B.

[491] Under the Internal Revenue Code, each year, mutual funds, including money market funds, must distribute to shareholders at least 90% of their annual earnings or lose the ability to deduct dividends paid to their shareholders. *See, e.g.,* Comment Letter of the Investment Company Institute (May 16, 2012) (available in File No. 4–619). We note that the retained earnings method is similar to how some money market funds paid for insurance that was provided by ICI Mutual Insurance Company from 1993 to 2003. This insurance covered losses on money market fund portfolio assets due to defaults and insolvencies but not from events such as a security downgrade or a rise in interest rates. Coverage was limited to $50 million per fund, with a deductible of the first 10 to 40 basis points of any loss. Premiums ranged from 1 to 3 basis points. *See* PWG Report, *supra* note 111, at n.24 and accompanying text. Because of the tax disadvantages of this funding method, it would take a long time for a NAV buffer of any size to build, particularly in the current low interest rate environment.

[492] This funding method also could have the greatest competitive impacts on the money market fund industry, as larger bank-affiliated sponsors would have less costly access to funding for the NAV buffer than independent asset management firm sponsors. *See, e.g.,* Systemic Risk Council FSOC Comment Letter, *supra* note 363 (''Capital requirements would likely encourage money market fund consolidation—particularly toward larger bank-affiliated sponsors (who traditionally have, and can access, more capital than traditional, independent asset managers). If so, this could further concentrate systemic risk from these institutions, and create conflicts of interest in the short-term financing markets (as fewer money funds would control a larger share of the short-term lending markets).'').

[493] *See* FSOC Proposed Recommendations, *supra* note 114, at section V.C.

[494] *See id,* at section V.C.

(which we have not proposed), and more robust disclosure requirements (which are generally proposed in sections III.F and III.G below).[495]

In the sections that follow, we discuss our evaluation of a NAV buffer requirement and an MBR requirement for money market funds. We also discuss comments FSOC received on these recommendations. For the reasons discussed below, the Commission is not pursuing these alternatives because we presently believe that the imposition of either a NAV buffer combined with a minimum balance at risk or a stand-alone NAV buffer, while advancing some of our goals for money market fund reform, might prove costly for money market fund shareholders and could result in a contraction in the money market fund industry that could harm the short-term financing markets and capital formation to a greater degree than the proposals under consideration.

a. NAV Buffer

In considering a NAV buffer such as those recommended by FSOC as a potential reform option for money market funds, we considered the benefits that such a buffer could provide, as well as its costs. Our evaluation of what could be a reasonable size for a NAV buffer also factored into our analysis of the advantages and disadvantages of these options. A buffer can be designed to satisfy different potential objectives. A large buffer could protect shareholders from losses related to defaults, such as the one experienced by the Reserve Primary Fund following the Lehman Brothers bankruptcy. However, if complete loss absorption is the objective, a substantial buffer would be required, particularly given that money market funds can hold up to 5% of their assets in a single security.[496]

Alternatively, if a buffer were not intended for complete loss absorption, but rather designed primarily to absorb day-to-day variations in the market-based value of money market funds' portfolio holdings under normal market conditions, this would allow a fund to hold a significantly smaller buffer. Accordingly, the relatively larger buffers contemplated in the FSOC Proposed Recommendations[497] must have been designed to absorb daily price fluctuations as well as relatively large security defaults.[498] In fact, a 3% buffer would accommodate all but extremely large losses, such as those experienced during the crisis. However, a buffer that was designed to absorb such large losses may be too high and too costly because the opportunity cost of this capital would be borne at all times even though it was likely to be drawn upon to any degree only rarely. Accordingly, a buffer of the size contemplated by either alternative in the FSOC Proposed Recommendations appears to be too costly to be practicable.[499]

i. Benefits of a NAV Buffer

The FSOC Proposed Recommendations discusses a number of potential benefits that a NAV buffer could provide to money market funds and their investors, many of which we discuss below.[500] It would preserve money market funds' stable share price and potentially increase the stability of the funds, but would likely reduce the yields (and in the option that combines a 1% NAV buffer with an MBR, the liquidity) that money market funds currently offer to investors. Like our proposed reforms, the NAV buffer presents trade-offs between stability, yield, and liquidity.

In effect, depending on the size of the buffer, a buffer could provide various levels of coverage of losses due to both the illiquidity and credit deterioration of portfolio securities. Money market funds that are supported by a NAV buffer would be more resilient to redemptions and credit or liquidity changes in their portfolios than stable value money market funds without a buffer (the current baseline).[501] As long as the NAV buffer is funded at necessary levels, each $1.00 in money market fund shares is backed by $1.00 in fund assets, eliminating the incentive of shareholders to redeem at $1.00 when the market-based value of their shares is worth less. This reduces shareholders' incentive to redeem shares quickly in response to small losses or concerns about the quality and liquidity of the money market fund portfolio, discussed in section II.B above, particularly during

[495] The FSOC Proposed Recommendations asked the Commission to consider increasing minimum weekly liquidity requirements from 30% of total assets to 40% of total assets. The justification provided by FSOC was that most funds already have weekly liquidity in excess of this 40% minimum level. We do not consider this alternative for two reasons. There is no evidence that current liquidity requirements are inadequate. For example, the RSFI Study notes that the heightened redemption activity in the summer of 2011 did not place undue burdens on MMFs when they sold assets to meet redemption requests. No fund lost more than 50 basis points during this period nor did their shadow NAVs deviate significantly from amortized cost. *See* RSFI Study, *supra* note 21. Based on these considerations, we have preliminarily determined not to address additional minimum liquidity requirements.

[496] Even commenters in favor of a buffer showed concern that FSOC's proposed buffer size of 1% or 3% may be inadequate. *See, e.g.,* Federal Reserve Bank Presidents FSOC Comment Letter, *supra* note 38, at 5 (''For a poorly diversified fund with portfolio assets that carry relatively more credit risk, a 3% (maximum) NAV buffer may not be sufficient.''); Harvard Business School FSOC Comment Letter, *supra* note 24 (''For a well-diversified portfolio, we estimate that MMFs should hold 3 to 4% capital against unsecured paper issued by financial institutions, the primary asset held by MMFs. For more concentrated portfolios, we estimate that the amount of capital should be considerably higher.''); Better Markets FSOC Comment Letter, *supra* note 67 (''The primary shortcoming of [FSOC's proposed buffer] is its low level of 1 or 3 percent. . . . [Any buffer] must be set at a level that is sufficient to cover all of these factors: Projected and historical losses; additional costs in the form of liquidity damages or government backstops; and investor psychology in the face of possible financial shocks or crises. [. . . .] Historical examples alone . . . indicate that MMF losses have risen as high as 3.9 percent. This serves only as a floor regarding actual potential losses, clearly indicating that the necessary buffer must be substantially higher than 3.9 percent.''); Occupy the SEC FSOC Comment Letter, *supra* note 42 (arguing that FSOC's proposed buffer does not go far enough in accounting for potential risks in a fund's portfolio. Instead, the approach should be a two-layer buffer, with a first layer of up to 3% depending on the portfolio's credit rating and a second layer to be sized according to the concentration of the portfolio).

[497] While the second alternative in the FSOC Proposed Recommendation only includes a NAV buffer of up to 1%, it was combined with a 3% MBR, which would effectively provide the fund with a 4% buffer before non-redeeming shareholders in the fund suffered losses.

[498] For example, beginning in September 2008, money market funds that chose to participate in the Treasury Temporary Guarantee Program were required to file with the Treasury their weekly shadow price if it was below $0.9975. Our staff has reviewed the data, and found that through October 17, 2008, only three funds carried losses larger than four percent, and only five funds carried losses larger than three percent. Reported shadow prices excluded the value of any capital support agreements in place at the time, but in some cases included sponsor-provided capital contributions to the fund. Not every money market fund that applied to participate in the program reported shadow price data for every day during the period between September 1, 2008 and October 17, 2008. *See also* Patrick E. McCabe et al., *The Minimum Balance at Risk: A Proposal to Mitigate the Systemic Risks Posed by Money Market Funds,* at 31, Table 2 Federal Reserve Bank of New York Staff Report No. 564, July 2012 (providing additional statistical analysis of shadow price information reported by money market funds filing under the Treasury Temporary Guarantee Program). During that period there were over 800 money market funds based on Form N–SAR data.

[499] There is another potential adverse effect of requiring large NAV buffers for money market funds to address risk from systemic events. According to the FSOC Proposed Recommendations, outflows from institutional prime money market funds following the Lehman Brothers bankruptcy tended to be larger among money market funds with sponsors that were themselves under stress, indicating that investors redeemed shares when concerned about sponsors' potential inability to support ailing funds. But these sponsors were the ones most likely to need funding dedicated to the buffer for other purposes. As a result, larger buffers may negatively affect other important activities of money market fund sponsors and cause them to fail faster.

[500] *See* FSOC Proposed Recommendations, *supra* note 114, at section V.B.

[501] *See, e.g.,* Occupy the SEC FSOC Comment Letter, *supra* note 42.

periods when the underlying portfolio has significant unrealized capital losses and the fund has not broken the buck. As long as the expected effect on the portfolio from potential losses is smaller than the NAV buffer, investors would be protected—they would continue to receive a stable value for their shares.

A second benefit is that a NAV buffer would force money market funds to provide explicit capital support rather than the implicit and uncertain support that is permitted under the current regulatory baseline. This would require funds to internalize some of the cost of the discretionary capital support sometimes provided to money market funds, and to define in advance how losses will be allocated. In addition, a NAV buffer could reduce fund managers' incentives to take risk beyond what is desired by fund shareholders because investing in less risky securities reduces the probability of buffer depletion.[502]

Another potential benefit is that a NAV buffer might provide counter-cyclical capital to the money market fund industry. This is because once a buffer is funded it remains in place regardless of redemption activity. With a buffer, redemptions increase the relative size of the buffer because the same dollar buffer now supports fewer assets.[503] As an example, consider a fund with a 1% NAV buffer that experiences a 25 basis point portfolio loss, which then triggers redemptions of 20% of its assets. The NAV buffer, as a proportion of fund assets and prior to any replenishment, will increase from 75 basis points after the loss to 93.75 basis points after the redemptions. This illustrates how the NAV buffer strengthens the ability of the fund to absorb further losses, reducing investors' incentive to redeem shares. This result contrasts to the current regulatory baseline under rule 2a–7 where redemptions amplify the impact of losses by distributing them over a smaller investor base. For example, suppose a fund with a shadow price of $1.00 (*i.e.,* no embedded losses) experiences a 25 basis point loss, which causes its shadow price to fall to $0.9975. If 20% of the fund's shares are then redeemed at $1.00, its shadow price will fall to $0.9969, reflecting a loss which is 24% greater than the loss precipitating the redemptions.

Finally, by allowing money market funds to absorb small losses in portfolio securities without affecting their ability to transact at a stable price per share, a NAV buffer may facilitate and protect capital formation in short-term financing markets during periods of modest stress. Currently, money market fund portfolio managers are limited in their ability to sell portfolio securities when markets are under stress because they have little ability to absorb losses without causing a fund's shadow NAV to drop below $1.00 (or embed losses in the fund's market-based NAV per share). As a result, managers tend to avoid trading when markets are strained, contributing to further illiquidity in the short-term financing markets in such circumstances. A NAV buffer should enable funds to absorb small losses and thus could reduce this tendency. Thus, by adding resiliency to money market funds and enhancing their ability to absorb losses, a NAV buffer may benefit capital formation in the long term. A more stable money market fund industry may produce more stable short-term financing markets, which would provide more reliability as to the demand for short-term credit to the economy.

ii. Costs of a NAV Buffer

There are significant ongoing costs associated with a NAV buffer. They can be divided into direct costs that affect money market fund sponsors or investors and indirect costs that impact capital formation. In addition, a NAV buffer does not protect shareholders completely from the possibility of heightened rapid redemption activity during periods of market stress, particularly in periods where the buffer is at risk of depletion. As the buffer becomes impaired (or if shareholders believe the fund may suffer a loss that exceeds the size of its NAV buffer), shareholders have an incentive to redeem shares quickly because, once the buffer fails, the fund will no longer be able to maintain a stable value and shareholders will suddenly lose money on their investment.[504] Such rapid severe redemptions could impair the fund's business model and viability.

Another possible implication of this facet of NAV buffers is that money market funds with buffers may avoid holding riskier short-term debt securities (like commercial paper) and instead hold a higher amount of low yielding investments like cash, Treasury securities, or Treasury repos. This could lead money market funds to hold more conservative portfolios than investors may prefer, given tradeoffs between principal stability, liquidity, and yield.[505]

The most significant direct cost of a NAV buffer is the opportunity cost associated with maintaining a NAV buffer. Those contributing to the buffer essentially deploy valuable scarce resources to maintain a NAV buffer rather than being able to use the funds elsewhere. The cost of diverting funds for this purpose represents a significant incremental cost of doing business for those providing the buffer funding. We cannot provide estimates of these opportunity costs because the relevant data is not currently available to the Commission.[506]

The second direct cost of a NAV buffer is the equilibrium rate of return that a provider of funding for a NAV buffer would demand. An entity that

[502] *See, e.g.,* Harvard Business School FSOC Comment Letter, *supra* note 24 (''Capital buffers also mean that there is an investor class that explicitly bears losses and has incentives to curb ex ante risk taking.'').

[503] *See, e.g.,* J.P. Morgan FSOC Comment Letter, *supra* note 342 ([W]here capital support is utilized as a first loss position upon liquidation, the level of capital can be tied to a MMF's highest asset levels. This can result in a structure whereby, as redemptions accelerate and cause the unrealized loss per share to increase further, the amount of capital support available per share increases accordingly, providing further capital support to the remaining shareholders that do not redeem their shares.'').

[504] *See, e.g.,* Systemic Risk Council FSOC Comment Letter, *supra* note 363 (stating that capital is difficult to set and is imperfect, that ''[g]iven the lack of data and impossibility of modeling future events, even [a 3% NAV buffer] runs the risk of being too high, or too low to protect the system in the future'' and that ''too little capital could provide a false sense of security in a crisis''). *See also infra* note 512 and accompanying discussion.

[505] *But see, e.g.,* U.S. Chamber Jan. 23, 2013 FSOC Comment Letter, *supra* note 248 (arguing that ''a NAV buffer is likely to incentivize sponsors to reach for yield.''); Vanguard FSOC Comment Letter, *supra* note 172 (''Capital buffers are also likely to carry unintended consequences, as some funds may purchase riskier, higher-yielding securities to compensate for the reduction in yield. As a result, capital buffers are likely to provide investors with a false sense of security.''); Comment Letter of Federated Investors, Inc. (Re: Alternative 3) (Jan. 25. 2013) (available in File No. FSOC–2012–0003) (''If anything, creating a junior class of equity puts earnings pressure on an MMF to alter its balance sheet to decrease near-term liquid assets to generate investment returns available from longer-term, higher risk investments in order to either build capital through retained earnings or to compensate investors who have invested in the new class of subordinated equity capital of the MMF.'').

[506] The opportunity costs would represent the net present value of these forgone opportunities, an amount that cannot be estimated without relevant data about each firm's productive opportunities.

However, a number of FSOC commenters have already cautioned that a NAV buffer could make money market funds unprofitable. *See, e.g.,* Angel FSOC Comment Letter, *supra* note 60 (stating that ''in today's low yield environment, even five basis points [of cost associated with a NAV buffer] would push most money market funds into negative yield territory.''); BlackRock FSOC Comment Letter, *supra* note 204 (''[A]ny capital over 0.75% will make the MMF product uneconomical for sponsors to offer.''); Federated Investors Feb. 15 FSOC Comment Letter, *supra* note 192 (calculating that ''prime MMFs would no longer be economically viable products'' based on cost estimates provided by the ICI.).

provides such funding, possibly the fund sponsor, would expect to be paid a return that sets the market value of the buffer equal to the amount of the capital contribution. Since a NAV buffer is designed to absorb the same amount of risk regardless of its size, the promised yield increases with the relative amount of risk it is expected to absorb. This is a well-known leverage effect.[507]

One could analogize a NAV buffer to bank capital by considering the similarities between money market funds with a NAV buffer and banks with capital. A traditional bank generally finances long-term assets (customer loans) with short-term liabilities (demand deposits). The Federal Reserve Board, as part of its prudential regulation, requires banks to adhere to certain minimum capital requirements.[508] Bank capital, among other functions, provides a buffer that allows banks to withstand a certain amount of sudden demands for liquidity and losses without becoming insolvent and thus needing to draw upon federal deposit insurance or other aspects of the regulatory safety net for banks.[509] The fact that the bank assets have a long maturity and are illiquid compared to the bank's liabilities results in a maturity and liquidity mismatch problem that creates the possibility of a depositor run during periods of stress.[510] Capital is one part of a prudential regulatory framework employed to deter runs in banks and generally protect the safety and soundness of the banking system. A money market fund with a NAV buffer has been described as essentially a ''special purpose bank'' where fund shareholders' equity is equivalent to demand deposits and a NAV buffer is analogous to the bank's capital.[511] Since a NAV buffer is effectively a leveraged position in the underlying assets of the fund that is designed to absorb interest rate risk and mitigate default risk, a provider of buffer funding should demand a return that reflects the fund's aggregate cost of capital plus compensation for the fraction of default risk it is capable of absorbing.

The effectiveness of a NAV buffer to protect against large-scale redemptions during periods of stress is predicated upon whether shareholders expect the decline in the value of the fund's portfolio to be less than the value of the NAV buffer. Once investors anticipate that the buffer will be depleted, they have an incentive to redeem before it is completely depleted.[512] In this sense, a NAV buffer that is not sufficiently large is incapable of fully mitigating the possibility of a liquidity run. The drawback with increasing buffer size to address this risk, however, is that the opportunity costs of operating a buffer increase as the size of the buffer increases. Due to the correlated nature of portfolio holdings across money market funds, this could amplify market-wide run risk if NAV buffer impairment also is highly correlated across money market funds. The incentive to redeem could be further amplified if, as contemplated in the FSOC Proposed Recommendations, a NAV buffer failure would require a money market fund to either liquidate or convert to a floating NAV. If investors anticipate this occurring, some investors that value principal stability and liquidity may no longer view money market funds as viable investments.

As noted above, substantial NAV buffers may be able to absorb much, if not all, of the default risk in the underlying portfolio of a money market fund. This implies that any compensation for bearing default risk will be transferred from current money market fund shareholders to those financing the NAV buffer, effectively converting a prime money market fund into a fund that mimics the return of a Treasury fund for current money market fund shareholders. If fund managers are unable to pass through the yield associated with holding risky securities, like commercial paper, to money market fund shareholders, it is likely that they will reduce their investment in risky securities, such as commercial paper or short-term municipal securities.[513] While lower yields would reduce, but not necessarily eliminate, the utility of the product to investors, it could have a negative impact on capital formation. Since the probability of breaking the buck is higher for a money market fund with riskier securities (*e.g.,* a fund with a WAM of 90 days rather than one with a WAM of 60 days)[514] and fund managers cannot pass through the higher associated yields, it is likely that managers will reduce investments in commercial paper because they cannot differentiate their funds on the basis of yield.

In addition, many investors are attracted to money market funds because they provide a stable value but have higher rates of return than Treasury securities. These higher rates of return are intended to compensate for exposure to greater credit risk and potential volatility than Treasury securities. As a result of funding the buffer, the returns to money market fund shareholders are likely to decline, potentially reducing demand from investors who are attracted to money market funds for their higher yield than alternative stable value investments.[515]

[507] The leverage effect reflects the concept that higher leverage levels induce an equity holder to demand higher returns to compensate for the higher risk levels.

[508] *See* the Federal Reserve Board's Web site on Capital Guidelines and Adequacy, *available at http://www.federalreserve.gov/bankinforeg/topics/capital.htm,* for an overview of minimum capital requirements.

[509] *See, e.g.,* Allen N. Berger et al., *The Role of Capital in Financial Institutions,* 19 J. of Banking and Fin. 393 (1995) (''Berger'') (''Regulators require capital for almost all the same reasons that other uninsured creditors of banks 'require' capital—to protect themselves against the costs of financial distress, agency problems, and the reduction in market discipline caused by the safety net.'').

[510] More generally, banks are structured to satisfy depositors' preference for access to their money on demand with businesses' preference for a source of longer-term capital. However, the maturity and liquidity transformation provided by banks can also lead to runs. Deposit insurance, access to a lender of last resort, and other bank regulatory tools are designed to lessen the incentive of depositors to run. *See, e.g.,* Douglas W. Diamond & Philip H. Dybvig, *Bank Runs, Deposit Insurance, and Liquidity,* 91 J. Pol. Econ 401 (June 1983) (''Diamond & Dybvig''); Mark J. Flannery, *Financial Crises, Payment System Problems, and Discount Window Lending,* 28 Journal of Money, Credit and Banking 804 (1996); Jeffrey A. Miron, *Financial Panics, the Seasonality of the Nominal Interest Rate, and the Founding of the Fed,* 76 American Economic Review 125 (1986); S. Bhattacharya & D. Gale, *Preference Shocks, Liquidity, and Central Bank Policy,* in New Approaches to Monetary Economics (eds., W. Barnnett and K. Singleton, 1987).

[511] *See, e.g.,* Gary Gorton & George Pennacchi, *Money Market Funds and Finance Companies: Are They the Banks of the Future?,* in Structural Change in Banking (Michael Klausner & Lawrence J. White, eds. 1993), at 173–214.

[512] *See, e.g.,* Federal Reserve Bank Presidents FSOC Comment Letter, *supra* note 38 (''The [FSOC] Proposal notes that a fund depleting its NAV buffer would be required to suspend redemptions and liquidate under rule 22e–3 or continue operating as a floating NAV fund. However, this sequence of events could be destabilizing. Investors in 3% NAV buffer funds may be quite risk averse, even more so than floating NAV MMF investors might be, given their revealed preference for stable NAV shares. If they foresee a possible conversion to floating NAV once the buffer is depleted, these risk-averse investors would have an incentive to redeem prior to conversion. If, on the other hand, investors foresee a suspension of redemptions, they would presumably have an even stronger incentive to redeem before facing a liquidity freeze when the NAV buffer is completely depleted.'').

[513] *But see supra* note 505.

[514] *See* RSFI Study, *supra* note 21, at 28–31.

[515] *See, e.g.,* Invesco FSOC Comment Letter, *supra* note 192 (''As a result of the ongoing ultra-low interest rate environment, MMF yields remain at historic lows. . . . A requirement to divert a portion of a MMF's earnings in order to build a NAV buffer would result in prime MMF yields essentially equaling those of Treasury MMFs (which would not be required to maintain a buffer under the Proposal). Faced with the choice of equivalent yields but asymmetrical risks, logical investors would abandon prime funds for Treasury funds, potentially triggering the very instability that reforms are intended to prevent and vastly reducing corporate borrowers' access to short-term financing.'').

Taken together, the demand by investors for some yield and the incentives for fund managers to reduce portfolio risk may impact competition and capital formation in two ways. First, investors seeking higher yield may move their funds to other alternative investment vehicles resulting in a contraction in the money market fund industry. In addition, fund managers may have an incentive to reduce the funds' investment in commercial paper or short-term municipal securities in order to reduce the volatility of cash flows and increase the resilience of the NAV buffer. In both of these cases, there may be an effect on the short-term financing markets if the decrease in demand for short-term securities from money market funds results in an increase in the cost of capital for issuers of commercial paper and other securities.

b. Minimum Balance at Risk

As discussed above, under the second alternative in the FSOC Proposed Recommendations, a 1% capital buffer is paired with an MBR or a holdback of a certain portion of a shareholder's money market fund shares.[516] In the event of fund losses, this alternative effectively would create a ''waterfall'' with the NAV buffer bearing first losses, subordinated holdback shares bearing second losses, followed by non-subordinated holdback shares, and finally by the remaining shares in the fund (and then only if the loss exceeded the aggregate value of the holdback shares). This allocation of losses, in effect, would impose a ''liquidity fee'' on redeeming shareholders if the fund experiences a loss that exceeds the NAV buffer. The value of the holdback shares effectively provides the non-redeeming shareholders with an additional buffer cushion when the NAV buffer is exhausted.

i. Benefits of a Minimum Balance at Risk

An MBR requirement could provide some benefits to money market funds. First, it would force redeeming shareholders to pay for the cost of their liquidity during periods of severe market stress when liquidity is particularly costly. Such a requirement could create an incentive against shareholders participating in a run on a fund facing potential losses of certain sizes because shareholders will incur greater losses if they redeem.[517] It thus may reduce the amount of less liquid securities that funds would need to sell in the secondary markets at unfavorable prices to satisfy redemptions and therefore may increase stability in the short-term financing markets.

Second, it would allocate liquidity costs to investors demanding liquidity when the fund itself is under severe stress. This would be accomplished primarily by making redeeming shareholders bear first losses when the fund first depletes its buffer and then the fund's value falls below its stable share price within 30 days after their redemption. Redeeming shareholders subject to the holdback are the ones whose redemptions may have contributed to fund losses if securities are sold at fire sale prices to satisfy those redemptions. If the fund sells assets to meet redemptions, the costs of doing so would be incurred while the redeeming investor is still in the fund because of the delay in redeeming his or her holdback shares. Essentially, investors would face a choice between redeeming to preserve liquidity and remaining invested in the fund to protect their principal.

Third, an MBR would provide the fund with 30 days to obtain cash to satisfy the holdback portion of a shareholder's redemption. This may give the fund time for distressed securities to recover when, for example, the market has acquired additional information about the ability of the issuer to make payment upon maturity. As of February 28, 2013, 43% of prime money market fund assets had a maturity of 30 days or less.[518] Thus, an MBR would provide time for potential losses in fund portfolios to be avoided since distressed securities could trade at a heavy discount in the market but may ultimately pay in full at maturity. This added resiliency could not only benefit the fund and its investors, but it also could reduce the contagion risk that a run on a single fund can cause when assets are correlated across the money market fund industry.

ii. Costs of a Minimum Balance at Risk

There are a number of drawbacks to an MBR requirement. It forces shareholders that redeem more than 97% of their assets to pay for any losses, if incurred, on the entire portfolio on a ratable basis. Rather than simply delaying redemption requests, the contingent nature of the way losses are distributed among shareholders forces early redeeming investors to bear the losses they are trying to avoid.

As discussed in section II.B.2 above, there is a tendency for a money market fund to meet redemptions by selling assets that are the most liquid and have the smallest capital losses. Liquid assets are sold first because managers can trade at close to their non-distressed valuations—they do not reflect large liquidity discounts. Managers also tend to sell assets whose market-based values are close to or exceed amortized cost because realized capital gains and losses will be reflected in a fund's shadow price. Assets that are highly liquid will not be sold at significant discounts to fair value. Since the liquidity discount associated with the sale of liquid assets is smaller than that for illiquid assets, shareholders can continue to immediately redeem shares at $1.00 per share under an MBR provided the fund is capable of selling liquid assets. Once a fund exhausts its supply of liquid assets, it will sell less liquid assets to meet redemption requests, possibly at a loss. If in fact, assets are sold at a loss, the stable value of the fund's shares could be impaired, motivating shareholders to be the first to leave. Therefore, even with a NAV buffer and an MBR there continues to be an incentive to redeem in times of fund and market stress.[519]

The MBR, which applies to all redemptions without regard to the fund's circumstances at the time of redemption, constantly restricts some portion of an investor's holdings. Under the resulting continuous impairment of full liquidity, many current investors who value liquidity in money market funds may shift their investment to other short-term investments that offer higher yields or fewer restrictions on redemptions. A reduction in the number of money market funds and/or the amount of money market fund assets under management as a result of any further money market fund reforms would have a greater negative impact on money market fund sponsors whose fund groups consist primarily of money market funds, as opposed to sponsors that offer a more diversified range of mutual funds or engage in other financial activities (*e.g.,* brokerage).

[516] *See* FSOC Proposed Recommendations, *supra* note 114, at section V.B.

[517] *See, e.g.,* Gordon FSOC Comment Letter, *supra* note 159 (''[T]he Minimum Balance at Risk feature is a novel way to reduce MMF run risk by imposing some of the run costs on the users of MMFs.'').

[518] Based on Form N–MFP data, with maturity determined in the same manner as it is for purposes of computing the fund's weighted average life.

[519] *See, e.g.,* Comment Letter of Federated Investors, Inc. (Dec. 17, 2012) (available in File No. FSOC–2012–0003) (''The data, analyses, surveys and other commentary in the SEC's docket show convincingly that the MBR/capital proposal's impact in reducing runs is speculative and unproven and in fact could and likely would precipitate runs under certain circumstances.''); Schwab FSOC Comment Letter, *supra* note 171 (''[I]t is not clear to us that holding back a certain percentage of a client's funds would reduce run risk.'')

Given that money market funds' largest commercial paper exposure is to issuances by financial institutions,[520] a reduction in the demand of money market instruments may have an impact on the ability of financial institutions to issue commercial paper.[521]

The MBR will introduce additional complexity to what to-date has been a relatively simple product for investors to understand. For example, requiring shareholders that redeem more than 97% of their balances to bear the first loss creates a cash flow waterfall that is complex and that may be difficult for retail investors to understand fully.[522]

Implementing an MBR could involve significant operational costs. These would include costs to convert existing shares or issue new holdback and subordinated holdback shares and changes to systems that would allow recordkeepers to account for and track the MBR and allocation of unrestricted, holdback or subordinated holdback shares in shareholder accounts. We expect that these costs would vary significantly among funds depending on a variety of factors. In addition, funds subject to an MBR may have to amend or adopt new governing documents to issue different classes of shares with quite different rights: Unrestricted shares, holdback shares, and subordinated holdback shares.[523] The costs to amend governing documents would vary based on the jurisdiction in which the fund is organized and the amendment processes enumerated in the fund's governing documents, including whether board or shareholder approval is necessary.[524] The costs of obtaining shareholder approval, amending governing documents or changing domicile would depend on a number of factors, including the size and the number of shareholders of the fund.[525]

Overall, the complexity of an MBR may be more costly for unsophisticated investors because they may not fully appreciate the implications. In addition, money market funds and their intermediaries (and money market fund shareholders that have in place cash management systems) could incur potentially significant operational costs to modify their systems to reflect a MBR requirement. We believe that an MBR coupled with a NAV buffer would turn money market funds into a more complex instrument whose valuation may become more difficult for investors to understand.

2. Alternatives in the PWG Report

a. Private Emergency Liquidity Facility

One option outlined in the PWG Report is a private emergency liquidity facility (''LF'') for money market funds.[526] One comment letter on the PWG Report proposed a structure for such a facility in some detail.[527] Under this proposal, the LF would be organized as a state-chartered bank or trust company. Sponsors of prime money market funds would be required to provide initial capital to the LF in an amount based on their assets under management up to 4.9% of the LF's total initial equity, but with a minimum investment amount. The LF also would charge participating funds commitment fees of 3 basis points per year on fund assets under management. Finally, at the end of its third year, the LF would issue to third parties time deposits paying a rate approximately equal to the 3-month bank CD rate. The LF would be designed to provide initially $7 billion in backup redemption liquidity to prime money market funds, $12.3 billion at the end of the first year, $30 billion at the end of five years, and $50–55 billion at the end of year 10 (these figures take into account the LF's ability to expand its capacity by borrowing through the Federal Reserve's discount window). The LF would be leveraged at inception, but would seek to achieve and maintain a minimum leverage ratio of 5%. Each fund would be able to obtain a maximum amount of cash from the LF. The LF would not provide credit support. It would not provide liquidity to a fund that had broken the buck or would ''break the buck'' after using the LF. There also would be eligibility requirements for money market fund access to the LF.

Participating funds would elect a board of directors that would oversee the LF, with representation from large, medium, and smaller money market fund complexes. The LF would have restrictions on the securities that it could purchase from funds seeking liquidity and on the LF's investment portfolio. The LF would be able to pledge approved securities (less a haircut) to the Federal Reserve discount window. We note that the interaction with the Federal Reserve discount window (as well as the bank structure of the LF) means that the Commission does not have regulatory authority to create the LF.

An LF could lessen and internalize some of the liquidity risk of money market funds that contributes to their vulnerability to runs by acting as a purchaser of last resort if a liquidity event is triggered. It also could create efficiency gains by pooling this liquidity risk within the money market fund industry.[528]

Commenters on the PWG Report addressing this option generally supported the concept of the LF, stating that it would facilitate money market funds internalizing the costs of liquidity and other risks associated with their operations through the cost of participation. In addition, such a facility could reduce contagion effects by limiting the need for fire sales of money market fund assets to satisfy redemption pressures.[529]

[520] *See supra* Panel A in section III.E.

[521] *See, e.g.,* Wells Fargo FSOC Comment Letter, *supra* note 342 (''the MBR requirement would have the anticipated impact of driving investors and sponsors out of money market funds. We expect that the resulting contraction of assets in the money market fund industry would, in turn, have disruptive effects on the short-term money markets, decrease the supply of capital and/or raise the cost of borrowing for businesses, states, municipalities and other local governments that rely on money market funds, and jeopardize the fragile state of the economy and its long-term growth prospects.'').

[522] Several commenters have noted that the MBR would be confusing to retail investors. *See, e.g.,* Fidelity FSOC Comment Letter, *supra* note 295; T. Rowe Price FSOC Comment Letter, *supra* note 290.

[523] One commenter on the PWG Report suggested that the MBR framework may be achieved by issuing different classes of shares with conversion features triggered by shareholder activity. *See* Comment Letter of Federated Investors, Inc. (Mar. 16, 2012) (available in File No. 4–619) (''Federated March 2012 PWG Comment Letter''). Multiple class structures are common among funds offering different arrangements for the payment of distribution costs and related shareholder services. Funds have also developed the operational capacity to track and convert certain share classes to others based on the redemption activity of the shareholder. *See* Mutual Fund Distribution Fees; Confirmations, Investment Company Act Release No. 29367 (July 21, 2010) [75 FR 47064 (Aug. 4, 2010)], at section III.D.1.b.

[524] *See* Federated Alternative 2 FSOC Comment Letter, *supra* note 254 and Federated March 2012 PWG Comment Letter, *supra* note 523 (discussing certain applicable state law requirements).

[525] Other factors may include the concentration of fund shares among certain shareholders, the number of objecting beneficial owners and non-objecting beneficial owners of street name shareholders, whether certain costs can be shared among funds in the same family, whether the fund employs a proxy solicitor and the services the proxy solicitor may provide, and whether the fund, in connection with sending a proxy statement to shareholders, uses the opportunity to have shareholders vote on other matters. Other matters that may be set forth in the proxy materials include the election of directors, a change in investment objectives or fundamental investment restrictions, and fund reorganization or re-domicile.

[526] *See* PWG Report, *supra* note 111, at 23–25.

[527] *See* ICI Jan 2011 PWG Comment Letter, *supra* note 473.

[528] The liquidity facility would function in a fashion similar to private deposit insurance for banks. For the economics of using a liquidity facility to stop runs, *see* Diamond & Dybvig, *supra* note 510.

[529] *See, e.g.,* ICI Jan 2011 PWG Comment Letter, *supra* note 473; Dreyfus PWG Comment Letter, *supra* note 473; Federated Jan 2011 PWG Comment Letter, *supra* note 472.

However, several commenters expressed reservations regarding this reform option. For example, one commenter supported ''the idea'' of such a facility ''in that it could provide an incremental liquidity cushion for the industry,'' but noted that ''it is difficult to ensure that [a liquidity facility] with finite purchasing capacity is fairly administered in a crisis. . . . [which] could lead to [money market funds] attempting to optimize the outcome for themselves, rather than working cooperatively to solve a systemic crisis.'' [530] This commenter also stated that shared capital ''poses the danger of increased risk-taking by industry participants who believe that they have access to a large collective pool of capital.'' [531] Another commenter, while ''receptive to a private liquidity facility,'' expressed concern that the facility itself might be vulnerable to runs if the facility raises funding through the short-term financing markets.[532] This commenter also noted other challenges in designing such a facility, including governance issues and ''the fact that because of its size, the liquidity facility would only be able to address the liquidity needs of a very limited number of funds and would not be able to meet the needs of the entire industry in the event of a run.'' [533] Another commenter expressed concerns that ''the costs, infrastructure and complications associated with private liquidity facilities are not worth the minimal liquidity that would be provided.'' [534] Finally, another commenter echoed this concern, stating:

[a private liquidity facility] cannot possibly eliminate completely the risk of breaking the buck without in effect eliminating maturity transformation, for instance through the imposition of capital and liquidity standards on the private facilities. Thus, in the case of a pervasive financial shock to asset values, [money market fund] shareholders will almost certainly view the presence of private facilities as a weak reed and widespread runs are likely to develop. In turn, government aid is likely to flow. Because shareholders will expect government aid in a pervasive financial crisis, shareholder and [money market fund] investment decisions will be distorted. Therefore, we view emergency facilities as perhaps a valuable enhancement, but not a reliable overall solution either to the problem of runs or to the broader problem of distorted investment decisions.[535]

A private liquidity facility was also discussed at the 2011 Roundtable, where many participants made points and expressed concerns similar to those discussed above.[536]

We have considered these comments, and our staff has spent considerable time evaluating whether an LF would successfully mitigate the risk of runs in money market funds and change the economic incentives of market participants. We have determined not to pursue this option further for a number of reasons, foremost because we are concerned that a private liquidity facility would not have sufficient purchasing capacity in the event of a widespread run without access to the Federal Reserve's discount window and we do not have legal authority to grant discount window access to an LF. Access to the discount window would raise complicated policy considerations and likely would require legislation.[537] In addition, such a facility would not protect money market funds from capital losses triggered by credit events as the facility would purchase securities at the prevailing market price. Thus, we are concerned that such a facility without additional loss protection would not sufficiently prevent widespread runs on money market funds.

We also are concerned about the conflicts of interest inherent in any such facility given that it would be managed by a diverse money market fund industry, not all of whom may have the same interests at all times. Participating money market funds would be of different sizes and the governance arrangements would represent some fund complexes and not others. There may be conflicts relating to money market funds whose nature or portfolio makes them more or less likely to ever need to access the LF. The LF may face conflicts allocating limited liquidity resources during a crisis, and choosing which funds gain access and which do not. To be successful, an LF would need to be managed such that it sustains its credibility, particularly in a crisis, and does not distort incentives in the market to favor certain business models or types of funds.

These potential issues collectively created a concern that such a facility may not prove effective in a crisis and thus we would not be able to achieve our regulatory goals of reducing money market funds' susceptibility to runs and the corresponding impacts on investor protection and capital formation. Combined with our lack of authority to create an LF bank with access to the Federal Reserve's discount window, these concerns ultimately have led us to not pursue this alternative.

b. Insurance

We also considered whether money market funds should be required to carry some form of public or private insurance, similar to bank accounts that carry Federal Deposit Insurance Corporation deposit insurance, which has played a central role in mitigating the risk of runs on banks.[538] The Treasury's Temporary Guarantee Program helped slow the run on money market funds in September 2008, and thus we naturally considered whether some form of insurance for money market fund shareholders might mitigate the risk of runs in money market funds and their detrimental impacts on investors and capital formation.[539] Insurance might replace

[530] BlackRock PWG Comment Letter, *supra* note 473.

[531] *Id.* In the case of deposit insurance, bank capital is used to overcome the moral hazard problem of excessive risk taking. *See, e.g.,* Berger, *supra* note 509; Michael C. Keeley & Frederick T. Furlong, *A Reexamination of Mean-Variance Analysis of Bank Capital Regulation,* 14 J. of Banking and Fin. 69 (1990).

[532] Wells Fargo PWG Comment Letter, *supra* note 475.

[533] *Id.*

[534] Fidelity Jan 2011 PWG Comment Letter, *supra* note 473.

[535] Richmond Fed PWG Comment Letter, *supra* note 139.

[536] *See, e.g.,* Roundtable Transcript, *supra* note 43 (Brian Reid, Investment Company Institute) (discussing the basic concept for a private liquidity facility as proposed by the Investment Company Institute and its potential advantages providing additional liquidity to money market funds when market makers were unwilling or unable to do so); (Paul Tucker, Bank of England) (discussing the potential policy issues involved in the Federal Reserve extending discount window access to such a facility); (Daniel K. Tarullo, Federal Reserve Board) (discussing the potential policy issues involved in the Federal Reserve extending discount window access to such a facility); (Jeffrey A. Goldstein, Department of Treasury) (questioning whether there were potential capacity issues with such a facility); (Sheila C. Bair, Federal Deposit Insurance Corporation) (stating her belief that ''the better approach would be to try to reduce or eliminate the systemic risk, as opposed to just kind of acknowledge it'' and institutionalize a ''bailout facility'' in a way that would exacerbate moral hazard).

[537] *See, e.g., id.* (Paul Tucker, Bank of England) (''As I understand it, this is a bank whose sole purpose is to stand between the Federal Reserve and the money market mutual fund industry. If I think about that as a central banker, I think 'So, I'm lending to the money market mutual fund industry.' What do I think about the regulation of the money market mutual fund industry? . . . And the other thought I think I would have is . . . 'If the money market mutual fund industry can do this, what's to stop other parts of our economy doing this and tapping into the special ability of the central bank to create liquidity' . . . It's almost to bring out the enormity of the idea that you have floated . . . it's posing very big questions indeed, about who should have direct access and to the nature of the monetary economy.'')

[538] *See generally* Charles W. Calomiris, *Is Deposit Insurance Necessary? A Historical Perspective,* 50 J. Econ. Hist. 283 (1990); Rita Carisano, Deposit Insurance: Theory, Policy and Evidence (1992); Diamond & Dybvig, *supra* note 510.

[539] Authority for a guarantee program like the Temporary Guarantee Program for Money Market Funds has since been removed. *See* Emergency

Continued

money market funds' historical reliance on discretionary sponsor support, which has covered capital losses in money market funds in the past but, as discussed above, also contributes to these funds' vulnerability to runs.

While a few commenters expressed some support for a system of insurance for money market funds,[540] most commenters opposed this potential reform option.[541] Commenters expressed concern that government insurance would create moral hazard and encourage excessive risk taking by funds.[542] They also asserted that such insurance could distort capital flows from bank deposits or government money market funds into prime money market funds, and that this disintermediation could and likely would cause significant disruption to the banking system and the money market.[543] For example, one commenter stated that:

''If the insurance program were partial (for example, capped at $250,000 per account), many institutional investors likely would invest in this partially insured product rather than directly in the market or in other cash pools because the insured funds would offer liquidity, portfolios that were somewhat less risky than other pools, and yields only slightly lower than alternative cash pools. Without insurance covering the full value of investors' account balances, however, there would still be an incentive for these investors to withdraw the uninsured portion of their assets from these funds during periods of severe market stress.'' [544]

Commenters stated that with respect to private insurance, it has been made available in the past but the product proved unsuccessful due to its cost and in the future would be too costly.[545] They also stated that they did not believe any private insurance coverage would have sufficient capacity.[546]

Given these comments, combined with our staff's analysis of this option, and considering that we do not have regulatory authority to create a public insurance scheme for money market funds, we are not pursuing this option as it does not appear that it would achieve our goal, among others, of materially reducing the contagion effects from heavy redemptions at money market funds without undue costs. We have made this determination based on money market fund insurance's potential for creating moral hazard and encouraging excessive risk-taking by money market funds, given the difficulties and costs involved in creating effective risk-based pricing for insurance and additional regulatory structure to offset this incentive.[547] If insurance actually increases moral hazard and decreases corresponding market discipline, it may in fact increase rather than decrease money market funds' susceptibility to runs. If the only way to counter these incentives was by imposing a very costly regulatory structure and risk-based pricing system our proposed alternatives potentially offer a better ratio of benefits to associated costs. Finally, we were concerned with the difficulty of creating private insurance at an appropriate cost and of sufficient capacity for a several trillion-dollar industry that tends to have highly correlated tail risk. All of these considerations have led us to not pursue this option further.

c. Special Purpose Bank

We also evaluated whether money market funds should be regulated as special purpose banks. Stable net asset value money market fund shares can bear some similarity to bank deposits.[548] Some aspects of bank regulation could be used to mitigate some of the risks described in section II above.[549] Money market funds could benefit from access to the special purpose bank's capital, government deposit insurance and emergency liquidity facilities from the Federal Reserve on terms codified and well understood in advance, and thus with a clearer allocation of risks among market participants.

As the PWG Report noted, and as commenters reinforced, there are a number of drawbacks to regulating money market funds as special purpose banks. While a few commenters expressed some support for this option,[550] almost all commenters on the PWG Report addressing this possible reform option opposed it.[551] Some commenters stated that the costs of converting money market funds to special purpose banks would likely be large relative to the costs of simply allowing more of this type of cash management activity to be absorbed into the existing banking sector.[552] Others expressed concern that regulating money market funds as special purpose banks would radically change the product, make it less attractive to investors and thereby have unintended consequences potentially worse than the mitigated risk, such as leading sophisticated investors to move their funds to unregulated or offshore money market fund substitutes and thereby limiting the applicability of the current money market fund regulatory regime and creating additional systemic risk.[553] For example, one of these commenters

Economic Stabilization Act of 2008 § 131(b), 12 U.S.C. § 5236 (2008) (prohibiting the Secretary of Treasury from using the Exchange Stabilization Fund for the establishment of any future guaranty programs for the U.S. money market fund industry).

[540] *See, e.g.,* Richmond Fed PWG Comment Letter, *supra* note 139 (stating that insurance would be a second best solution for mitigating the risk of runs in money market funds after a floating net asset value because insurance premiums and regulation are difficult to calibrate correctly, so distortions would likely remain); Comment Letter of Paul A. Volcker (Feb. 11, 2011) (available in File No. 4–619) (''Volcker PWG Comment Letter'') (stating that money market funds wishing to retain a stable net asset value should reorganize as special purpose banks or ''submit themselves to capital and supervisory requirements and FDIC-type insurance on the funds under deposit'').

[541] *See, e.g.,* Comment Letter of the American Bankers Association (Jan. 10, 2011) (available in File No. 4–619) (''American Bankers PWG Comment Letter''); BlackRock PWG Comment Letter, *supra* note 473; Dreyfus PWG Comment Letter, *supra* note 473; Fidelity Jan 2011 PWG Comment Letter, *supra* note 473; Wells Fargo PWG Comment Letter, *supra* note 475; ''); Comment Letter of John M. Winters (Jan. 5, 2011) (available in File No. 4–619) (''Winters PWG Comment Letter'').

[542] *See, e.g.,* American Bankers PWG Comment Letter, *supra* note 541; BlackRock PWG Comment Letter, *supra* note 473; ICI Jan 2011 PWG Comment Letter, *supra* note 473; Wells Fargo PWG Comment Letter, *supra* note 475.

[543] *See, e.g.,* ICI Jan 2011 PWG Comment Letter, *supra* note 473; Wells Fargo PWG Comment Letter, *supra* note 475.

[544] ICI Jan 2011 PWG Comment Letter, *supra* note 473.

[545] *See, e.g.,* BlackRock PWG Comment Letter, *supra* note 473; Fidelity Jan 2011 PWG Comment Letter, *supra* note 473; Dreyfus PWG Comment Letter, *supra* note 473; Wells Fargo PWG Comment Letter, *supra* note 475; Winters PWG Comment Letter, *supra* note 541.

[546] *See, e.g.,* BlackRock PWG Comment Letter, *supra* note 473; Fidelity Jan 2011 PWG Comment Letter, *supra* note 473; Wells Fargo PWG Comment Letter, *supra* note 475; Winters PWG Comment Letter, *supra* note 541.

[547] *See, e.g.,* Yuk-Shee Chan et al., *Is Fairly Priced Deposit Insurance Possible?,* 47 J. Fin. 227 (1992).

[548] *See supra* note 511 and accompanying text.

[549] *Id.*

[550] *See* Volcker PWG Comment Letter, *supra* note 540 (''MMMFs that desire to offer their clients bank-like transaction services . . . and promises of maintaining a constant or stable net asset value (NAV), should either be required to organize themselves as special purpose banks or submit themselves to capital and supervisory requirements and FDIC-type insurance on funds under deposit.''); Winters PWG Comment Letter, *supra* note 541 (supporting it as the third best option, stating that ''[a]s long as the federal government continues to be the only viable source of large scale back-up liquidity for MMFs, it is intellectually dishonest to pretend that MMFs are not the functional equivalent of deposit-taking banks. Thus, inclusion in the federal banking system is warranted.'').

[551] *See, e.g.,* BlackRock PWG Comment Letter, *supra* note 473; Fidelity Jan. 2011 PWG Comment Letter, *supra* note 473; ICI Jan. 2011 PWG Comment Letter, *supra* note 473; Comment Letter of the Institutional Money Market Funds Association (Jan. 10, 2011) (available in File No. 4–619).

[552] *See, e.g.,* Richmond Fed PWG Comment Letter, *supra* note 139; ICI Jan. 2011 PWG Comment Letter, *supra* note 473.

[553] *See, e.g.,* Comment Letter of the Mutual Fund Directors Forum (Jan. 10, 2011) (available in File No. 4–619); Fidelity Jan. 2011 PWG Comment Letter, *supra* note 473; ICI Jan. 2011 PWG Comment Letter, *supra* note 473.

stated that transforming money market funds into special purpose banks would create homogeneity in the financial regulatory scheme by relying on the bank business model for all short-term cash investments and that ''[g]iven the unprecedented difficulties the banking industry has experienced recently, it seems bizarre to propose that [money market funds] operate more like banks, which have absorbed hundreds of billions of dollars in government loans and handouts.'' [554] Some pointed to the differences between banks and money market funds as justifying different regulatory treatment, and expressed concern that concentrating investors' cash management activity in the banking sector could increase systemic risk.[555]

The potential costs involved in creating a new special purpose bank regulatory framework to govern money market funds do not seem justified. In addition, given our view that money market funds have some features similar to banks but other aspects quite different from banks, applying substantial parts of the bank regulatory regime to money market funds does not seem as well tailored to the structure of and risks involved in money market funds compared to the reforms we are proposing in this Release. After considering our lack of regulatory authority to transform money market funds into special purpose banks as well as the views expressed in these comment letters and our staff's analysis of these matters and for the reasons set forth above, we are not pursuing a reform option of transforming money market funds into special purpose banks.

d. Dual Systems of Money Market Funds

We evaluated options that would institute a dual system of money market funds, where either institutional money market funds or money market funds using a stable share price would be subject to more stringent regulation than others. As discussed in the PWG Report,[556] money market fund reforms could focus on providing enhanced regulation solely for money market funds that seek to maintain a stable net asset value, rather than a floating NAV. Enhanced regulations could include any of the regulatory reform options discussed above such as mandatory insurance, a private liquidity facility, or special purpose bank regulation. Money market funds that did not comply with these enhanced constraints would have a floating NAV (though they would still be subject to the other risk limiting conditions contained in rule 2a–7).

There also may be other enhanced forms of regulation or other types of dual systems. For example, an alternative formulation of this regulatory regime would apply the enhanced regulatory constraints discussed above (*e.g.,* a private liquidity facility or insurance) only to ''institutional'' money market funds, and ''retail'' money market funds would continue to be subject to rule 2a–7 as it exists today. We note that our proposals to exempt retail and government money market funds from any floating NAV requirement and to exempt government money market funds from any fees and gates requirement in effect creates a dual system.

These dual system regulatory regimes for money market funds could provide several important benefits. They attempt to apply the enhanced regulatory constraints on those aspects of money market funds that most contribute to their susceptibility to runs—whether it is institutional investors that have shown a tendency to run or a stable net asset value created through the use of amortized cost valuation that can create a first mover advantage for those investors that redeem at the first signs of potential stress. A dual system that imposes enhanced constraints on stable net asset value money market funds would allow investors to choose their preferred mixture of stability, risk, and return.

Because insurance, special purpose banks, and the private liquidity facility generally are beyond our regulatory authority to create, these particular dual options, which would impose one of these regulatory constraints on a subset of money market funds, could not be created under our current regulatory authority. Other options, such as requiring a floating NAV or liquidity fees and gates only for some types of money market funds, however, could be imposed under our current authority and are indeed proposed.

Each of these dual systems generally has the same advantages and disadvantages as the potential enhanced regulatory constraints that would be applied, described above. In addition, for any two-tier system of money market fund regulation to be effective in reducing the risk of contagion effects from heavy redemptions, investors would need to fully understand the difference between the two types of funds and their associated risks. If they did not, they may indiscriminately flee both types of money market funds even if only one type experiences difficulty.[557]

A dual system approach also would allow the Commission to tailor its reforms to the particular areas of the money market fund industry that are of most concern (*e.g.,* funds operating with a stable NAV or institutional funds or accounts). Given the difficulties, drawbacks, and limitations on our regulatory authority associated with dual systems involving a special purpose bank, private liquidity facility and insurance, we are not pursuing creating a dual system of money market fund regulation involving these enhanced regulatory constraints at this time. However, as noted above, our current proposal would to some extent create a dual system of money market funds, and we request comment on other potential dual systems that are within our regulatory authority.

*E. Macroeconomic Effects of the Proposals*

In this section, we analyze the macroeconomic consequences of our floating NAV and liquidity fees and gates proposals, as well as some of their effects on efficiency, competition, and capital formation. We also examine the potential implications of these proposals on current investments in money market funds and on the short-term financing markets.[558] The baseline for these analyses (and all of our economic analysis in this Release) is money market fund investment and the short-term financing markets, as they exist today.[559]

Our proposals should provide a number of benefits and positive effects on competition, efficiency, and capital formation. As discussed in detail earlier in this Release, we have designed both

[554] Fidelity Jan. 2011 PWG Comment Letter, *supra* note 473.

[555] *See, e.g.,* Fidelity Jan. 2011 PWG Comment Letter, *supra* note 473; ICI Jan. 2011 PWG Comment Letter, *supra* note 473.

[556] *See* PWG Report, *supra* note 111, at 29–32.

[557] For example, when The Reserve Primary Fund broke the buck in September 2008, all money market funds managed by Reserve Management Company, Inc. experienced runs, even the Reserve U.S. Government Fund, despite the fact that the Reserve U.S. Government Fund had a quite different risk profile. *See* Press Release, A Statement Regarding The Reserve Primary and U.S. Government Funds (Sept. 19, 2008) *available at http://www.primary-yieldplus-inliquidation.com/pdf/PressReleasePrimGovt2008_0919.pdf* (''The U.S. Government Fund, which had approximately $10 billion in assets under management at the opening of business on September 15, 2008, has received redemption requests this week of approximately $6 billion.'').

[558] In *supra* sections III.A and III.B we discuss the specific benefits and costs associated with the two alternative reform proposals, and we discuss later in this Release the specific economic analysis of other aspects of our proposals. The specific operational costs of implementing the reform proposals are discussed in each respective section.

[559] *See* Panels A, B and C later in this section for certain recent data regarding money market fund investment and the short-term financing markets.

of our proposals to improve the transparency of money market funds' risks and lessen the incentives for investors to redeem shares in times of fund or market stress. The floating NAV proposal is designed to address the incentive created today by money market funds' stable values for shareholders to redeem fund shares when the funds' market-based NAVs are below their intended stable price. That proposal is also designed to reduce the likelihood that funds would experience heavy redemptions in times of stress, by acclimatizing investors to expect small fluctuations in the fund's share price over time, which could reduce the chances that investors will redeem in the face of market stress or stress on the money market fund. However, for those funds that do not qualify for the proposed retail or government exemptions to the floating NAV, this alternative would come at the cost of removing many of the benefits to investors that are the result of a fund being able to maintain a stable share price through the rounding conventions of rule 2a–7. A floating NAV also may not deter heavy redemptions from certain types of money market funds (*e.g.,* prime money market funds) in times of stress if shareholders engage in a flight to quality, liquidity or transparency.

The liquidity fees and gates alternative would preserve the benefits of the stable price per share that shareholders currently enjoy, but it would do so at the cost of potentially reducing (or making more costly) shareholder liquidity in certain circumstances. The liquidity fees and gates proposal is designed to protect fund shareholders that remain invested in a fund from bearing the liquidity costs of shareholders that exit a fund when the funds' liquidity is under stress. Redeeming fund shareholders receive the benefits of a fund's liquidity, which in times of stress may have the effect of imposing costs on the shareholders remaining in the fund. The liquidity fees and gates proposal would address this risk. The proposal also is designed to better position a money market fund to withstand heavy redemptions. A fund's board would be permitted to impose a gate when the fund is under stress, which would provide time for a panic to subside; for the fund's portfolio securities to mature and provide internal liquidity to meet redemptions; and for fund managers to assess the appropriate strategy to meet redemptions. Liquidity fees also could lessen investors' incentives to redeem and require investors to evaluate and price their liquidity needs. The fees and gates proposal, however, would not fully eliminate the incentive to quickly redeem in times of stress, because redeeming shareholders would retain an economic advantage over shareholders that remain in a fund if they redeem when the costs of liquidity are high, but the fund has not yet imposed a fee or gate. Also, by their nature, liquidity fees and redemption gates, if imposed, increase costs on shareholders who seek to redeem fund shares.

Both of these proposals are intended, in different ways, to stabilize funds in times of stress. Thus, the proposals are designed to reduce the likelihood and associated costs of any contagion effects from heavy redemptions in money market funds to other money market funds, the short-term financing markets, and other parts of the economy. Nevertheless, we recognize that the expected benefits of the proposals may be accompanied by some adverse effects on the short-term financing markets for issuers, and may affect the level of investment in money market funds that would be subject to the proposals. The magnitude of these effects, including any effects on competition, efficiency, and capital formation, would depend on the extent to which investors reallocate their investments within the money market fund industry and on the extent to which investors reallocate their investments between money market funds and alternatives outside the money market fund industry. We anticipate that the adverse effects on investment in money market funds and the short-term financing markets for debt issuers would be small if either relatively little money is reallocated, or if the alternatives to which investors reallocate their cash invest in securities similar to those previously held by the money market funds. Conversely, the effects on investment in money market funds and the short-term financing markets would be larger if a substantial amount of money is reallocated to alternatives and those alternatives invest in securities of a different type from those previously held by money market funds.

1. Effect on Current Investment in Money Market Funds

The popularity of money market funds today indicates they compete favorably with other investment alternatives. As of February 28, 2013, all money market funds had approximately $2.9 trillion in assets under management while government money market funds had approximately $929 billion under management.[560] Money market funds that self-report as retail prime money market funds held approximately $497 billion in assets under management and tax-exempt money market funds held approximately $277 billion in assets under management. We do not know how many of these funds would qualify for our proposed retail exemption from the floating NAV requirement.[561]

If we were to adopt either of the alternatives we are proposing today, current money market fund investors would likely consider the tradeoffs involved of investing in a money market fund subject to our proposals. Investors may decide to remain invested in money market funds subject to either a floating NAV or liquidity fees and gates, or they may choose to invest in a money market fund that is exempt from our proposed reforms (such as a government money market fund, or for the floating NAV proposal, a retail fund), invest directly in short-term debt instruments, hold cash in a bank deposit account, invest in one of the few alternative diversified investments products that maintains a stable value (such as certain unregistered private funds), or invest in other products that fluctuate in value, such as ultra-short bond funds.

Money market funds under either of our proposals, like money market funds today, would compete against many investment alternatives for investors' assets. Our proposals, by increasing transparency and reducing the incentive for investors to redeem shares ahead of other investors in times of stress, could increase the attractiveness of money market funds in the long term for investors who value this aspect of our reforms, potentially offsetting the loss of some money market fund investors that may occur in the short term if we were to adopt either proposal, and enhancing competition. The proposals could also increase competition as investors become more aware of certain aspects of the industry and funds respond to meet investors' preferences. Our proposals also could increase allocative efficiency[562] by not only increasing transparency of the underlying risks of money market fund investing, but also by making it harder for one group of investors to impose disproportionate costs on another group.[563] In particular,

[560] Based on Form N–MFP data.

[561] Based on iMoneyNet data as of April 16, 2013.

[562] Allocative efficiency refers to investors allocating their funds to the most suitable investments on efficient terms, taking all relevant factors into account.

[563] Some commenters have noted the potential for inequitable treatment of shareholders under the stable NAV model. *See, e.g.,* Better Markets FSOC

the floating NAV proposal requires investors to bear day-to-day losses and gains, and the liquidity fees and gates proposal requires investors to bear their liquidity costs when liquidity is particularly costly. Today, money market funds' day-to-day market-based losses and gains and any liquidity costs generally are not borne by redeeming investors because investors buy and sell money market fund shares at their stable $1.00 share price absent a break-the-buck event. In addition, as discussed in section III.F below, our proposal would require that money market fund sponsors disclose their support of funds, which also would advance investor understanding of the risk of loss in money market funds and thus may advance allocative efficiency if investors make better investment decisions as a result.

If we were to adopt reforms to money market funds, investors may withdraw some of their assets from affected money market funds. We believe that investors may withdraw more assets under the floating NAV proposal than they would under the liquidity fees and gates alternative because the floating NAV proposal may have a more significant effect on investors' day-to-day experience with and use of money market funds than the liquidity fees and gates alternative and because many investors place great value on principal stability in a money market fund.[564] It is important to note, however, that investors that hold shares of money market funds not subject to our proposed reform alternatives (such as government money market funds, or under our floating NAV proposal, retail money market funds) may not experience outflows if we were to adopt the proposed reforms to money market funds because those funds would continue to be able to maintain a stable price under our floating NAV proposal. These exempt funds may even experience inflows of assets if investors reallocate their investments to such stable price funds.

We understand that many money market fund investors value both price stability and share liquidity.[565] Because of the exemptions to the alternatives that we are proposing, under either the floating NAV or liquidity fees and gates proposal, investors will still be able to invest in certain money market funds that can continue to offer both price stability and unrestricted liquidity. Investors that value yield over these two features will be able to invest in prime money market funds, or if they are able to accept the daily redemption limits, retail money market funds. The key change under this proposal is that investors will have to prioritize their preference for these characteristics as they make their investment decisions because under our proposal, money market funds not subject to an exemption will, depending on the alternative adopted, suffer some diminution in principal stability, liquidity, or yield.

For those money market funds that would be required to use floating NAVs or to consider imposing liquidity fees and gates, there may be shifts in asset allocations not only among funds in the money market fund industry but also into alternative investment vehicles. We currently do not have a basis for estimating under either reform alternative the number of investors that might reallocate assets, the magnitude of the assets that might shift, or the likely investment alternatives because we do not know how investors will weigh the tradeoffs involved in reallocating their investments to alternatives. We request comment on these issues below.

As discussed in sections III.A and III.B above, we anticipate some institutional investors would not or could not invest in a money market fund that does not offer principal stability or that has restrictions on redemptions. We do expect that more institutional investors would be unwilling to invest in a floating NAV money market fund than a money market fund that might impose a fee or gate because a floating NAV would have a persistent effect on investors' experience in a money market fund. These investors also may be unwilling to incur the operational and other costs and burdens discussed above that would be necessary to use floating NAV money market funds. One survey concluded, among other things, that if the Commission were to require money market funds to use floating NAVs, 79% of the 203 corporate, government, and institutional investors that responded to the survey would decrease their money market fund investments or stop using the funds.[566] Similarly, a 2012 liquidity survey found that up to 77% of the 391 organizations that responded to the survey would be less willing to invest in floating NAV money market funds, and/or would reduce or eliminate their money market fund holdings if the Commission were to require the funds to use floating NAVs.[567] We also

Comment Letter, *supra* note 67 (stating that ''an investor that succeeds in redeeming early in a downward spiral may receive more than they deserve in the sense that they liquidate at $1.00 per share even though the underlying assets are actually worth less. Without a sponsor contribution or other rescue, that differential in share value is paid by the shareholders remaining in the fund, who receive less not only due to declining asset values but also because early redeemers received more than their fair share of asset value.''); Comment Letter of Wisconsin Bankers Association (Feb. 15. 2013) (available in File No. FSOC–2012–0003) (stating that ''[a] floating NAV has the benefits of . . . reducing the possibilities for transaction activity that results in non-equitable treatment across all shareholders''). *See also supra* section II.B.1.

[564] *See, e.g., infra* note 565 and accompanying discussion.

[565] Many of the comments received by FSOC stressed the importance of price stability and liquidity to many investors. *See, e.g.,* Steve Morgan FSOC Comment Letter, *supra* note 290 (''The stable share price and liquid access to investors' money are key features of MMFs.''); Comment Letter of James White (Jan. 11, 2013) (available in File No. FSOC–2012–0003) (''Stability, convenience, and liquidity—including the stable share price and ability to access 100 percent of their money—are what draw investors to MMFs.''); Comment Letter of The SPARK Institute (Jan. 18, 2013) (available in File No. FSOC–2012–0003) (''Money market funds with a stable [NAV] serve important functions in the operation and administration of defined contribution retirement plans (*e.g.,* 401(k) plans) as convenient, cost-effective, simple, stable and liquid cash management tools.''); Comment Letter of Association for Financial Professionals (Jan. 22, 2013) (available in File No. FSOC–2012–0003) (''For a large number of institutional investors, the potential of principal loss would preclude investing in floating NAV MMFs''); Comment Letter of Independent Directors Council (Jan. 23, 2013) (available in File No. FSOC–2012–0003); Invesco FSOC Comment Letter, *supra* note 192.

[566] *See* ICI Apr 2012 PWG Comment Letter, *supra* note 62. According to this survey, if the Commission were to require money market funds to use floating NAVs: (i) 21% of the surveyed respondents would continue using funds at the same level; and (ii) 79% would either decrease use or discontinue altogether. Treasury Strategies, which conducted the survey, estimates that ''money market fund assets held by corporate, government and institutional investors would see a net decrease of 61%'' based on its assessment of the survey responses.

[567] *See* 2012 AFP Liquidity Survey, *supra* note 73, at 3 (201 corporate practitioner members of the Association for Financial Professionals and 190 corporate practitioners who are not members responded to the survey). *See also, e.g.,* ICI Feb 2012 PWG Comment Letter, *supra* note 259 (describing a survey conducted by Treasury Strategies Inc., a survey conducted by Harris Interactive (commissioned by T. Rowe Price), and a survey conducted by Fidelity); Dreyfus 2009 Comment Letter, *supra* note 350 (opposing a floating NAV and stating that, after surveying 37 of its largest institutional money market fund shareholders (representing over $60 billion in assets) regarding a floating NAV, 67% responded that their business could not continue to invest in a floating NAV product and that they would have to seek an alternative investment option); Comment Letter of National Association of State Treasurers (Dec. 21, 2010) (available in File No. 4–619) (''Nat. Assoc. of State Treasurers PWG Comment Letter'') (opposing a floating NAV because, among other reasons, ''a floating NAV would push investors to less regulated or non-regulated markets''); Comment Letter of the Association for Financial Professionals (Jan. 10, 2011) (available in File No. 4–619) (''AFP Jan. 2011 PWG Comment Letter'') (reporting results of a survey of its members reflecting that four out of five organizations would likely move at least some of their assets out of money market funds if the funds were required to use floating NAVs and

Continued

understand that some institutional investors currently are prohibited by board-approved guidelines or internal policies from investing certain assets in money market funds that do not have a stable value per share.[568] Other investors, including state and local governments, may be subject to statutory or regulatory requirements that permit them to invest certain assets only in funds that seek to maintain a stable value per share.[569] In these instances, we anticipate monies would flow out of prime money market funds and into government money market funds or alternate investment vehicles. This would result in a contraction in the prime money market fund industry, thereby reducing the type and amount of money market fund investments available to investors and potentially harming the ability of money market funds to compete in several respects affected by our proposal. The net effect of this contraction would depend upon the ability of investors to replicate the pre-reform characteristics of money market funds in alternative investments.

As of February 28, 2013, institutional prime money market funds manage approximately $974 billion in assets.[570] As with government and retail funds, however, we do not have a basis for estimating the number of institutions that might reallocate assets, the amount of assets that might shift, or the likely alternatives under either of our proposals, because we do not know how many of these investors face statutory or other requirements that mandate investment in a stable value product or a product that will not restrict redemptions or how these investors would weigh the tradeoffs involved in switching their investment to various alternative products. We request comment on these issues below.

Investors that are unable or unwilling to invest in a money market fund subject to our proposed reforms would have a range of investment options, each offering a different combination of price stability, risk exposure, return, investor protections, and disclosure. For example, some current money market fund investors may manage their cash themselves and, based on our understanding of institutional investor cash management practices, many of these investors would invest directly in securities similar to those held by money market funds today. If so, our proposal would not have a large negative effect on capital formation. Any desire to self-manage cash, however, would likely be tempered by the expertise required to invest in a diversified portfolio of money market securities directly and the costs of investing in those securities given the economies of scale that would be lost when each investor has to conduct credit analysis itself for each investment (in contrast to money market funds which could spread their credit analysis costs for each security across their entire shareholder base).[571] Additionally, these investors might find it difficult to find appropriate investments that match their specific cash flows available for investment.

Shifts from reformed money market funds to other investment alternatives that could result from our proposals likely would transfer certain risks from money market funds to other markets and institutions. Commenters have cited to the fact that a shift of assets from money market funds to bank deposits, for example, would increase investors' reliance on FDIC deposit insurance and increase the size of the banking sector, possibly increasing the concentration of risk in banks.[572] As discussed in the RSFI Study, individual and business holdings in checking deposits and currency are large and have significantly increased in recent years relative to their holdings of money market fund shares.[573] The 2012 AFP Liquidity Survey of corporate treasurers indicates that bank deposits accounted for 51% of the surveyed organizations' short-term investments in 2012, which is up from 25% in 2008.[574] Money market funds accounted for 19% of these organizations' short-term investments in 2012, down from 30% just a year earlier, and down from almost 40% in 2008.[575] This shift was likely motivated by the availability of unlimited FDIC insurance on non-interest bearing accounts between the end of 2010 and January 2013.[576] A further shift in assets from money market funds to bank deposits would increase this concentration.

As discussed in the RSFI Study, there are a range of investment alternatives that currently compete with money market funds. If we adopt either of our proposals, investors could choose from among at least the following alternatives: Money market funds that are exempt from the proposed reforms; under the liquidity fees and gates proposal, money market funds that invest only in weekly liquid assets; bank deposit accounts; bank certificates of deposit; bank collective trust funds; local government investment pools (''LGIPs''); U.S. private funds; offshore money market funds; short-term investment funds (''STIFs''); separately managed accounts; ultra-short bond funds; short-duration exchange-traded funds; and direct investments in money market instruments.[577] Each of these choices involves different tradeoffs, and money market fund investors that are unwilling or unable to invest in a money market fund under either of our proposals would need to analyze the various tradeoffs associated with each alternative.

The following table, taken from the RSFI Study, outlines the principal

providing details as to the likely destinations); Comment Letter of Federated Investors, Inc. (Feb. 24, 2012) (available in File No. 4–619) (stating that many state laws would preclude trust investments in money market funds with a floating NAV); Roundtable Transcript, *supra* note 43 (Carol A DeNale, (CVS Caremark) (''I will not invest in a floating NAV product. [. . . .] We will pull out of money market funds, and I think that is the consensus of the treasurers that I have talked to in different meetings that I've been in, in group panels.'').

[568] *See, e.g.,* ICI Jan. 24 FSOC Comment Letter, *supra* note 25; Wells Fargo FSOC Comment Letter, *supra* note 342; Comment Letter of County Commissioners Assoc. of Ohio (Dec. 21, 2012) (available in File No. FSOC–2012–0003); Comment Letter of the American Bankers Association (Sept. 8, 2009) (available in File No. S7–11–09); Fidelity 2009 Comment Letter, *supra* note 208; Comment Letter of Goldman Sachs Asset Management, L.P. (Sept. 8, 2009) (available in File No. S7–11–09); Comment Letter of Treasury Strategies, Inc. (Sept. 8, 2009) (available in File No. S7–11–09).

[569] *Id.*

[570] Based on iMoneyNet data.

[571] *See, e.g.,* U.S. Chamber Jan. 23, 2013 FSOC Comment Letter, *supra* note 248 (''Quite simply, it is more efficient and economical to pay the management fee for a MMMF than to hire the internal staff to manage the investment of cash.'').

[572] *See, e.g.,* Angel FSOC Comment Letter, *supra* note 60 (stating that ''[m]any of the proposed reforms would seriously reduce the attractiveness of MMMFs,'' which ''could increase, not decrease, systemic risk as assets move to too-big-to-fail banks.''); Comment Letter of Jonathan Macey (Nov. 27, 2012) (available in File No. FSOC–2012–0003) (stating that a ''reduced MMF industry may lead to the flow of large amounts of cash into [the banking system], especially through the largest banks, and increase pressure on the FDIC.''); Federated Investors Alternative 1 FSOC Comment Letter, *supra* note 161 (''A floating NAV would accelerate the flow of assets to ''Too Big to Fail'' banks, further concentrating risk in that sector.'').

[573] *See* RSFI Study, *supra* note 21, at figure 18.

[574] *See* 2012 AFP Liquidity Survey, *supra* note 73.

[575] *See id.,* 2008 AFP Liquidity Survey, *supra* note 73.

[576] As of December 31, 2012, the amount in domestic noninterest-bearing transaction accounts over the normal $250,000 limit was $1.5 trillion. *See* Federal Deposit Insurance Corporation Quarterly Banking Profile, Fourth Quarter 2012, at 16, *available at http://www2.fdic.gov/qbp/2012dec/qbp.pdf.* At December 31, 2008, the amount in domestic noninterest-bearing transaction accounts over the normal $250,000 limit was $814 billion. *See* Federal Deposit Insurance Corporation Quarterly Banking Profile, Fourth Quarter 2008, at 20, *available at http://www2.fdic.gov/qbp/2008dec/qbp.pdf.*

[577] *See, e.g.,* ICI Feb 2012 PWG Comment Letter, *supra* note 259; Comment Letter of the Association for Financial Professionals et al. (Apr. 4, 2012) (available in File No. 4–619).

features of various cash alternatives to money market funds that exist today.

TABLE 2—CASH INVESTMENT ALTERNATIVES

| Product | Valuation | Investment risks [a] | Redemption restrictions | Yield [b] | Regulated | Restrictions on investor base |
|---|---|---|---|---|---|---|
| Bank demand deposits | Stable | Below benchmark up to depository insurance ("DI") limit; above benchmark above DI limit [c]. | No | Below benchmark. | Yes | No. |
| Time deposits (CDs) | Stable | Bank counterparty risk above DI limit. | Yes [d] | Below benchmark. | Yes | No. |
| Offshore money funds (European short-term MMFs) [e]. | Stable or Floating NAV. | Comparable to benchmark | Some [f] | Comparable to benchmark. | Yes | Yes.[g] |
| Offshore money funds (European MMFs) [h]. | Floating NAV | Above benchmark | Some | Above benchmark. | Yes | Yes. |
| Enhanced cash funds (private funds). | Stable NAV (generally). | Above benchmark | By contract | Above benchmark. | No [i] | Yes.[j] |
| Ultra-short bond funds | Floating NAV | Above benchmark | Some | Above benchmark. | Yes | No. |
| Collective investment funds [k] | Not stable | Above benchmark | No | Above benchmark. | Yes | Tax-exempt bank clients.[l] |
| Short-term investment funds ("STIFs"). | Stable | Above benchmark | No | Above benchmark. | Yes [m] | Tax-exempt bank clients. |
| Local government investment pools ("LGIPs"). | Stable (generally) [n]. | Benchmark | No | Benchmark | Yes | Local government and public entities. |
| Short-duration ETFs | Floating NAV; Market price [o]. | Above benchmark | No | Above benchmark. | Yes | No. |
| Separately managed accounts (including wrap accounts). | Not stable | Above benchmark | No | Above benchmark. | No | Investment minimum.[p] |
| Direct investment in MMF instruments. | Not stable | Comparable to benchmark but may vary depending on investment mix [q]. | No | Comparable to benchmark but may vary depending on investment mix. | No | Some.[r] |

[a] For purposes of this table, investment risks include exposure to interest rate and credit risks. The column also indicates the general level of investment risk for the product compared with the baseline of prime money market funds and is generally a premium above the risk-free or Treasury rate.

[b] The table entries reflect average yields in a normal interest rate environment. Certain cash management products, such as certificates of deposits ("CDs") and demand deposits, may be able to offer rates above the baseline in a low interest rate environment.

[c] The current DI limit is $250,000 per owner for interest-bearing accounts. *See* Deposit Insurance Summary, Federal Deposit Insurance Corporation ("FDIC"), *available at http://www.fdic.gov/deposit/deposits/dis/.*

[d] Time deposits, or CDs, are subject to minimum early withdrawal penalties if funds are withdrawn within six days of the date of deposit or within six days of the immediately preceding partial withdrawal. *See* 12 CFR 204.2(c)(1)(i). Many CDs are also subject to early withdrawal penalties if withdrawn before maturity, although market forces, rather than federal regulation, impose such penalties. CDs generally have specific fixed terms (*e.g.,* one-, three-, or six-month terms), although some banks offer customized CDs (*e.g.,* with terms of seven days).

[e] The vast majority of money market fund assets are held in U.S. and European money market funds. *See* Consultation Report of the IOSCO Standing Committee 5 (Apr. 27, 2012) ("IOSCO SC5 Report"), at App. B, §§ 2.1–2.36 (in 2011, of the assets invested in money market funds in IOSCO countries, approximately 61% were invested in U.S. money market funds and 32% were invested in European money market funds). Consequently, dollar-denominated European money market funds may provide a limited offshore money market fund alternative to U.S. money market funds. Most European stable value money market funds are a member of the Institutional Money Market Funds Association ("IMMFA"). According to IMMFA, as of March 1, 2013, there were approximately $286 billion U.S. dollar-denominated IMMFA money market funds. *See www.immfa.org* (this figure excludes accumulating NAV U.S. dollar-denominated money market funds). Like U.S. money market funds, European short-term money market funds must have a dollar-weighted average maturity of no more than 60 days and a dollar-weighted average life maturity of no more than 120 days, and their portfolio securities must hold one of the two highest short-term credit ratings and have a maturity of no more than 397 days. However, unlike U.S. money market funds, European short-term money market funds may either have a floating or fixed NAV. *Compare* Common Definition of European Money Market Funds (Ref. CESR/10–049) *with* rule 2a–7.

[f] Most European money market funds are subject to legislation governing Undertakings for Collective Investment in Transferable Securities ("UCITS"), which also covers other collective investments. *See, e.g.,* UCITS IV Directive, Article 84 (permitting a UCITS to, in accordance with applicable national law and its instruments of incorporation, temporarily suspend redemption of its units); Articles L. 214–19 and L. 214–30 of the French Monetary and Financial Code (providing that under exceptional circumstances and if the interests of the UCITS units holders so demand, UCITs may temporarily suspend redemptions).

[g] Section 7(d) of the Investment Company Act requires that any non-U.S. investment company that wishes to register as an investment company in order to publicly offer its securities in the U.S. must first obtain an order from the SEC. To issue such an order, the SEC must find that "by reason of special circumstances or arrangements, it is both legally and practically feasible to enforce the provisions of [the Act against the non-U.S. fund,] and that the issuance of [the] order is otherwise consistent with the public interest and the protection of investors." No European money market fund has received such an order. European money market funds could be offered to U.S. investors privately on a very limited basis subject to certain exclusions from investment company regulation under the Investment Company Act and certain exemptions from registration under the Securities Act. U.S. investors purchasing non-U.S. funds in private offerings, however, may be subject to potentially significant adverse tax implications. *See, e.g.,* Internal Revenue Code of 1986 §§ 1291 through 1297. Moreover, as a practical matter, and in view of the severe consequences of violating the Securities Act registration and offering requirements, most European money market funds currently prohibit investment by U.S. Persons.

[h] European money market funds may have a dollar-weighted average portfolio maturity of up to six months and a dollar-weighted average life maturity of up to 12 months that are significantly greater than are permitted for U.S. money market funds. *Compare* Common Definition of European Money Market Funds (Ref. CESR/10–049) *with* rule 2a–7.

[i] Private funds generally rely on one of two exclusions from investment company regulation by the Commission. Section 3(c)(1) of the Investment Company Act, in general, excludes from the definition of ''investment company'' funds whose shares are beneficially owned by not more than 100 persons where the issuer does not make or propose to make a public offering. Section 3(c)(7) of the Act places no limit on the number of holders of securities, as long as each is a ''qualified purchaser'' (as that term is defined in section 2(a)(51) of the Act) when the securities are acquired and the issuer does not make or propose to make a public offering. Most retail investors would not fall within the definition of ''qualified purchaser.'' Moreover, such private funds also generally rely on the private offering exemption in section 4(2) of the Securities Act or Securities Act rule 506 to avoid the registration and prospectus delivery requirements of Section 5 of the Securities Act. Rule 506 establishes ''safe harbor'' criteria to meet the private offering exemption. The provision most often relied upon by private funds under rule 506 exempts offerings made exclusively to ''accredited investors'' (as that term is defined in rule 501(a) under the Securities Act). Most retail investors would not fall within the definition of ''accredited investor.'' Offshore private funds also generally rely on one of the two non-exclusive safe harbors of Regulation S, an issuer safe harbor and an offshore resale safe harbor. If one of the two is satisfied, an offshore private fund will not have to register the offer and sale of its securities under the Securities Act. Specifically, rules 903(a) and 904(a) of Regulation S provide that offers and sales must be made in ''offshore transactions'' and rule 902(h) provides that an offer or sale is made in an ''offshore transaction'' if, among other conditions, the offer is not made to a person in the United States. Regulation S is not available to offers and sales of securities issued by investment companies required to be registered, but not registered, under the Investment Company Act. *See* Regulation S Preliminary Notes 3 and 4.

[j] *See id.*

[k] Collective investment funds include collective trust funds and common trust funds managed by banks or their trust departments, both of which are a subset of short-term investment funds. For purposes of this table, short-term investment funds are separately addressed.

[l] Collective trust funds are generally limited to tax-qualified plans and government plans, while common trust funds are generally limited to tax-qualified personal trusts and estates and trusts established by institutions.

[m] STIFs are generally regulated by 12 CFR 9.18. The Office of the Comptroller of the Currency recently reformed the rules governing STIFs subject to their jurisdiction to impose similar requirements to those governing money market funds. *See* Office of the Comptroller of Currency, Treasury, Short-Term Investment Funds [77 FR 61229 (Oct. 9, 2012)].

[n] Regarding all items in this row of the table, LGIPs generally are structured to meet a particular investment objective. In most cases, they are designed to serve as short-term investments for funds that may be needed by participants on a day-to-day or near-term basis. These local government investment pools tend to emulate typical money market mutual funds in many respects, particularly by maintaining a stable net asset value of $1.00 through investments in short-term securities. A few local government investment pools are designed to provide the potential for greater returns through investment in longer-term securities for participants' funds that may not be needed on a near-term basis. The value of shares in these local government investment pools fluctuates depending upon the value of the underlying investments. Local government investment pools limit the nature of underlying investments to those in which its participants are permitted to invest under applicable state law. *See http://www.msrb.org/Municipal-Bond-Market/About-Municipal-Securities/Local-Government-Investment-Pools.aspx.* Investors in local government investment pools may include counties, cities, public schools, and similar public entities. *See, e.g.,* The South Carolina Local Government Investment Pool Participant Procedures Manual, *available at http://www.treasurer.sc.gov/Investments/The%20South%20Carolina%20Local%20Government%20Investment%20Pool%20Participant%20Procedures%20Manual.pdf.*

[o] Although the performance of an exchange traded fund (''ETF'') is measured by its NAV, the price of an ETF for most shareholders is not determined solely by its NAV, but by buyers and sellers on the open market, who may take into account the ETF's NAV as well as other factors.

[p] Many separately managed accounts have investment minimums of $100,000 or more.

[q] Depending on the nature and scope of their investments, these investors may also face risks stemming from a lack of portfolio diversification.

[r] Some money market fund instruments are only sold in large denominations or are only available to qualified institutional buyers. *See generally* rule 144A under the Securities Act (17 CFR 230.144A(7)(a)(1)).

If we adopt the floating NAV proposal, investors that value principal stability would likely consider shifting investments to government money market funds (or retail money market funds), which would be permitted to continue to maintain stable prices under that proposal. Similarly, if we adopt the alternative fees and gates proposal, investors that are unwilling to invest in a money market fund that might impose a liquidity fee or gate when liquidity is particularly costly might shift their investments to government money market funds. Investors that shifted their assets from prime money market funds to government money market funds would likely sacrifice yield under both proposals, but they would maintain the principal stability and liquidity of their assets. Investors in exempt retail money market funds would not have to face the same tradeoff. Alternatively, money market fund investors could reallocate assets to various bank products such as demand deposits or short-maturity certificates of deposit. FDIC insurance would provide principal stability and liquidity irrespective of market conditions for bank accounts whose deposits are within the insurance limits.

Today, interest-bearing accounts and non-interest-bearing transaction accounts at depository institutions are insured up to $250,000. Accordingly, institutions would be deterred from moving their investments from money market funds to banks because their assets would probably be above the current depository insurance limits which would expose them to substantial counterparty risk.[578] Nevertheless, these investors could gain full insurance coverage if they are willing and able to break their cash holdings into sufficiently small pieces and spread them across enough banks.[579]

Investors in reformed money market funds that value principal stability would find most other investment alternatives unattractive, including floating value enhanced cash funds, ultra-short bond funds, short-duration ETFs, and collective investment funds. These alternatives typically do not offer principal stability. These investments, however, might be attractive to investors that value yield over principal stability and the lowest investment risk. To our knowledge, none of these alternative investment products (except potentially enhanced cash funds) may restrict redemptions in times of stress without obtaining relief from regulatory restrictions.

One practical constraint for many money market fund investors is that they may be precluded from investing in certain alternatives, such as STIFs, offshore money market funds, LGIPs, separately managed accounts, and direct investments in money market instruments, due to significant

[578] *See, e.g.,* Comment Letter of Crawford and Company (Jan. 14, 2013) (available in File No. FSOC–2012–0003) (''Bank demand deposits . . . lack the diversification of MMFs and carry inherent counterparty risk.''); ICI Jan 2011 PWG Comment Letter, *supra* note 473 (''The Report suggests that requiring money market funds to float their NAVs could encourage investors to shift their liquid balances to bank deposits. We believe that this effect is overstated, particularly for institutional investors. Corporate cash managers and other institutional investors would not view an undiversified holding in an uninsured (or underinsured) bank account as having the same risk profile as an investment in a diversified short-term money market fund. Such investors would continue to seek out diversified investment pools, which may or may not include bank time deposits.'').

[579] Certain third party service providers offer such services. *See, e.g.,* Nathaniel Popper and Jessica Silver-Greenberg, *Big Depositors Seek New Safety Net*, N.Y. Times (Dec. 30, 2012).

restrictions on participation. For example, STIFs are only available to accounts for personal trusts, estates, and employee benefit plans that are exempt from taxation under the U.S. Internal Revenue Code.[580] STIFs subject to regulation by the Office of the Comptroller of the Currency also are subject to less stringent regulatory restrictions than rule 2a–7 imposes, and STIFs under the jurisdiction of other banking regulators may be subject to no restrictions at all equivalent to rule 2a–7.[581] Accordingly, these funds pose greater risk than money market funds and thus may not be attractive alternatives to investors that highly value principal stability. Offshore money market funds, which are investment pools domiciled and authorized outside the United States, can only sell shares to U.S. investors in private offerings. Few offshore money market funds offer their shares to U.S. investors in part because doing so could create adverse tax consequences.[582] In addition, European money market funds can take on more risk than U.S. money market funds as they are not currently subject to regulatory restrictions on their credit quality, liquidity, maturity, and diversification as stringent as those imposed under rule 2a–7, among other differences in regulation.[583]

Some current money market fund investors may have self-imposed restrictions or fiduciary duties that limit the risks they can assume or that preclude them from investing in certain alternatives. They might be prohibited from investing in, for example, enhanced cash funds that are privately offered to institutions, wealthy clients, and certain types of trusts due to greater investment risk, limitations on investor base, or the lack of disclosure and legal protections of the type afforded them by U.S. securities regulations.[584] Likewise, money market fund investors that can only invest in SEC-registered investment vehicles could not invest in LGIPs, which are not registered with the SEC (as states and local state agencies are excluded from regulation under the Investment Company Act). Many unregistered and offshore alternatives to money market funds—unlike registered money market funds in the United States today—are not prohibited from imposing gates or suspending redemptions.[585] Other investment alternatives, such as bank CDs, also impose redemption restrictions. Investors placing a high value on liquidity would likely find the potential imposition of these restrictions unacceptable and thus not invest in them.

Both retail and institutional investors' assessments of money market funds as reformed under our proposals and their attractiveness relative to alternatives may be influenced by investors' views on the degree to which funds' NAVs will change from day to day under our floating NAV proposal or the frequency with which fees and gates will be imposed under our liquidity fees and gates proposal. For example, managers of floating NAV funds could invest a large percentage of their holdings in very short-term or Treasury securities to minimize fluctuations in the funds' NAVs. Additionally, under our liquidity fees and gates proposal, we expect that funds would attempt to manage their liquidity levels in order to avoid crossing the threshold for applying liquidity fees or gates. One possible effect of each of these actions may be to lower the expected yield of the fund. Thus, we believe that, under our proposals, fund managers would be incentivized to mitigate the potential direct costs of the proposals for investors, and we further believe that they would be successful in so doing in all but the most extreme circumstances, but that this mitigation may come at a cost to fund yield and profitability as managers shift to shorter dated or more liquid securities.

Investors' demand for stability in the value of the money market fund investment could provide an incentive for sponsors to support their money market funds in the event a particular portfolio security would negatively affect the NAV of the fund (*i.e.,* to prevent a fund's NAV from declining below a value the fund seeks to maintain under either our floating NAV proposal or our liquidity fees and gates proposal). Under our floating NAV proposal, sponsor support could permit prime money market funds (or other non-exempt money market funds) to continue to maintain a stable price. Under our liquidity fees and gates proposal, a sponsor could prevent the money market fund's weekly liquid assets from falling below the 15% threshold for applying liquidity fees and gates by giving the fund cash (for example, the sponsor could lift out some of the fund's non-weekly liquid assets or the sponsor could directly purchase fund shares) to invest in weekly liquid assets. We are proposing a number of new disclosure requirements regarding sponsor support to help shareholders understand whether a fund's stable price or liquidity was the result of careful portfolio management or sponsor support. Among other things, money market funds would be required to provide real-time notifications to both investors and the Commission of new instances of sponsor support, a description of the nature of support, and the date and amount of support provided.[586]

As this analysis reflects, the economic implications of our floating NAV and liquidity fees and gates proposals depend on investors' preferences, and the attractiveness of investment alternatives.[587] For these and the other reasons discussed below, we believe that the survey data submitted by commenters reflecting that certain investors expect to reduce or eliminate their money market fund investments under the floating NAV alternative may

[580] *See* Testimony of Paul Schott Stevens, President and CEO of the Investment Company Institute, before the Committee on Banking, Housing, and Urban Affairs, United States Senate, on ''Perspectives on Money Market Mutual Fund Reforms,'' June 21, 2012.

[581] For a discussion of the regulation of STIFs by the Office of the Comptroller of the Currency (OCC), *see supra* Table 2, note M. The OCC's rule 9.18 governs STIFs managed by national banks and federal savings associations. Other types of banks may or may not follow the requirements of OCC rule 9.18, depending, for example, on state law requirements and federal tax laws. *See* Office of the Comptroller of Currency, Treasury, Short-Term Investment Funds, at n.6 and accompanying text [77 FR 61229 (Oct. 9, 2012)].

[582] *See supra* this section, Table 2, explanatory notes G and I.

[583] For a discussion of the regulation of European money market funds, *see supra* Table 2, notes E and H; Common Definition of European Money Market Funds (Ref. CESR/10–049).

[584] According to the 2012 AFP Liquidity Survey, *supra* note 73, only 21% of respondents stated that enhanced cash funds were permissible investment vehicles under the organization's short-term investment policy. In contrast, 44% stated that prime money market funds were a permissible investment and 56% stated that Treasury money market funds were a permissible investment.

[585] *See, e.g., supra* this section, Table 2, explanatory note F.

[586] *See infra* section III.G; proposed (FNAV and Fees & Gates) Form N–CR, Part C (Provision of Financial Support to Fund).

[587] *See, e.g.,* Better Markets FSOC Comment Letter, *supra* note 67 (in response to industry survey data reflecting intolerance for the floating NAV, stating that ''it is difficult to predict the level of contraction that would actually result from instituting a floating NAV. [. . . .] The move to a floating NAV does not alter the fundamental attributes of MMFs with respect to the type, quality, and liquidity of the investments in the fund. [. . . .] It is therefore unrealistic to think that MMFs . . . will become extinct solely as a result of a move to a more accurate and transparent valuation methodology.''); Winters FSOC Comment Letter, *supra* note 190 (''[T]he feared migration to unregulated funds has not been quantified and is probably overstated.''); U.S. Chamber Jan. 23, 2013 FSOC Comment Letter, *supra* note 248 (''No alternatives with the same multiple benefits are available to replace money market mutual funds.'').

not definitively indicate how investors might actually behave.[588]

None of the surveys discussed above considered the exemptions we are proposing that would permit both government money market funds (under both proposals) and retail money market funds (under the floating NAV proposal) to continue to maintain a stable price without restrictions. In addition, none of the surveys addressed how investors would respond to our specific liquidity fees and gates proposal. Finally, the surveys did not consider how available alternatives to floating NAV money market funds might satisfy money market fund investors' expressed desires for stable, liquid, and safe investments. Indeed, some commenters have suggested that the mass exodus from money market funds as a result of further reforms is unlikely and that money market fund investors may not necessarily seek out investment alternatives.[589] Some alternatives to money market funds, commenters explain, would carry greater risks than the effect of our proposals on money market funds, would not be able to accommodate a sizeable portion of money market fund assets, or both.[590] We also understand that at least one money market fund sponsor converted its non-U.S. stable value money market funds to funds with floating NAVs and found that its concern in advance of the conversion that the funds' mostly retail investors would redeem and reject the floating NAV funds proved to be unjustified.[591]

We request comment on what effects our floating NAV or liquidity fees and gates proposals would have on current money market fund investments.

- Do commenters believe that the likely effect of either our floating NAV proposal or our liquidity fees and gates proposal would be to cause some investors to shift their money market fund investments to alternative products and thus reduce the amount of money market fund assets under management? If so, to what extent and why? To what extent would these shifts vary depending on whether the investor was retail or institutional and why?
- Would either of our proposals result in any reduction in the number of money market funds and/or consolidation of the money market industry? How many funds and what types of money market funds would leave the industry? What would be the effect on assets under management of different types of money market funds if we adopt either our floating NAV or liquidity fees and gates proposal?
- To what extent under each alternative would retail and institutional money market fund investors shift to investment alternatives, including managing their cash themselves?
- Would certain investment alternatives that have significant restrictions on their investor base be unavailable for current money market fund investors? If so, which alternatives and to what extent?
- Do commenters agree with our analysis of the likelihood that certain shareholders would seek out particular investment alternatives in the event we adopted either of our floating NAV or liquidity fees and gates proposals? For example, would institutional investors be unlikely to shift assets to bank deposits (because of depository insurance limits) or local government investment pools, short-term investment funds, or offshore money market funds (because of the significant investment restrictions)? Do commenters agree with our analysis with respect to some or all of these alternatives? Why or why not?
- Are there aspects of any investment alternatives other than operational costs discussed in sections III.A.7 and III.B.6 above or the factors we have identified in this section that would affect whether money market fund investors would be likely to use other investment alternatives in lieu of money market funds under either of our proposals? We request that commenters differentiate between short-term effects that would occur as the industry transitions to one in which money market funds use floating NAVs or liquidity fees and gates and the long-term effects that would persist thereafter.
- Under each of the two proposals, what fraction of prime money market fund assets might be moved to government money market funds, retail funds, or to other alternatives (and to which alternatives)? How would these answers differ for retail investors and institutional investors?
- What would be the net effect of our proposal on competition in the money market fund industry?

As noted above, we understand that some institutional investors may be prohibited by board-approved guidelines or internal policies from investing certain assets in money market funds unless they have a stable value per share or do not have redemption restrictions, and we understand that other investors, including state and local governments, may be subject to statutory or regulatory requirements that permit them to invest certain assets only in funds that seek to maintain a stable value per share or that do not have any redemption restrictions.

- How would these guidelines and other constraints affect investors' use of floating NAV money market funds or those that could impose fees or gates?
- Could institutional investors change their guidelines or policies to invest in either floating NAV money market funds or funds that could impose fees or gates, if appropriate? If not, why not? If so, what costs might institutional investors incur to change these guidelines and policies?
- Do the guidelines or statutory or regulatory constraints precluding investment in floating NAV money market funds permit investments in investment products that can fluctuate in value, such as direct investments in money market instruments or Treasury securities?

2. Effect on Current Issuers and the Short-Term Financing Markets

Although we currently do not have estimates of the amount of assets money market fund investors might migrate to investment alternatives, we recognize that shifts from money market funds into other choices could affect issuers of short-term debt securities and the short-term financing markets. The effects of these shifts, including any effect on efficiency, competition, and capital formation, would depend on the size of reallocations to investment alternatives and the nature of the alternatives,

[588] *See supra* notes 566 and 567, and *infra* note 803 and accompanying text.

[589] *See, e.g.,* Winters FSOC Comment Letter, *supra* note 190 (stating that, with respect to the feared migration to unregulated funds, ''the capacity for existing unregulated funds to take inflows is relatively small and the operators of such funds may not welcome a flood of hot money with riskless expectations.''); ICI Jan 2011 PWG Comment Letter, *supra* note 473 (''The Report suggests that requiring money market funds to float their NAVs could encourage investors to shift their liquid balances to bank deposits. We believe that this effect is overstated, particularly for institutional investors. Corporate cash managers and other institutional investors would not view an undiversified holding in an uninsured (or underinsured) bank account as having the same risk profile as an investment in a diversified short-term money market fund. Such investors would continue to seek out diversified investment pools, which may or may not include bank time deposits.'').

[590] *See, e.g.,* Thrivent FSOC Comment Letter, *supra* note 396 (''Arguments for massive movements into vehicles such as cash enhanced funds, offshore money market funds and the like seem to assume that investors will behave irrationally. There would be no logical reason to move from highly regulated money market funds with a history of maintaining a close proximity to $1.00 per share net asset value to cash enhanced funds, which are much less regulated and likely to have a much more widely fluctuating NAV, nor to offshore money funds which have materially different guidelines, nor to stable value vehicles, the growth of which is limited by available supply of insured product with commensurate credit ratings.'').

[591] UBS IOSCO Comment Letter, *supra* note 357.

including whether the alternatives invest in the short-term financing markets or otherwise provide similar credit. We discuss these effects in detail and seek comment on them, including the effects of the proposal on the commercial paper markets and municipal financing.

The extent to which money market fund investors might choose to reallocate their assets to investment alternatives as a result of money market fund reforms would likely drive the effect on issuers and the short-term financing markets. As discussed in the RSFI Study, prime money market funds managed approximately $1.7 trillion as of March 31, 2012, holding approximately 57% of the total assets of all registered money market funds. The chart below provides information about prime (and other) money market funds as of December 31, 2012. Even a modest shift could represent a sizeable increase in other investments.

HOLDINGS OF MONEY MARKET FUNDS

| | Treasury debt | Treasury repo | Govmt agency debt | Govmt agency repo | VRDNs | Other municipal debt | Financial Co CP | ABCP | Non-financial Co CP | CDs | Other |
|---|---|---|---|---|---|---|---|---|---|---|---|
| **Panel A. MMF Holdings in $B, December 31, 2012** | | | | | | | | | | | |
| Prime | 143.39 | 53.46 | 155.90 | 143.92 | 55.33 | 4.30 | 221.64 | 121.98 | 77.13 | 524.14 | 250.95 |
| Treasury | 303.54 | 118.56 | 0.01 | 1.38 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.02 |
| Other | 63.38 | 41.81 | 251.26 | 149.06 | 220.43 | 60.50 | 0.65 | 2.94 | 6.63 | 0.72 | 10.37 |
| *All MMF* | *510.31* | *213.83* | *407.17* | *294.36* | *275.77* | *64.80* | *222.29* | *124.92* | *83.76* | *524.86* | *261.33* |

| | Treasury debt | Treasury repo | Govmt agency debt | Govmt agency repo | VRDNs | Other municipal debt | Financial Co CP | ABCP | Non-financial Co CP | CDs | Other |
|---|---|---|---|---|---|---|---|---|---|---|---|
| **Panel B. MMF Holdings as Percentage of Total Amortized Cost of MMFs by Type of Fund, December 31, 2012** | | | | | | | | | | | |
| Prime | 8.18 | 3.05 | 8.90 | 8.21 | 3.16 | 0.25 | 12.65 | 6.96 | 4.40 | 29.91 | 14.32 |
| Treasury | 71.67 | 27.99 | 0.00 | 0.33 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| Other | 7.85 | 5.18 | 31.11 | 18.45 | 27.29 | 7.49 | 0.08 | 0.36 | 0.82 | 0.09 | 1.28 |
| *All MMF* | *17.11* | *7.17* | *13.65* | *9.87* | *9.24* | *2.17* | *7.45* | *4.19* | *2.81* | *17.59* | *8.76* |

| | Treas debt as % treas bills outstnd | (Treas debt + repos) as % treas bills outstnd | Govmt agency debt as % of govmt agency sec outstnd | (Govmt agency debt + repos) as % of govmt agency sec outstnd | VRDN as % of muni secs outstnd | (VRDN+ other muni) as % of muni secs outstnd | Fncl Co CP as % of Fncl Co CP outstnd | ABCP as % of ABCP outstnd | Non-Fncl Co CP as % of non-Fncl Co CP outstnd | CDs as % of savings and time deposit outstnd | CDs as % of large savings and time deposit outstnd |
|---|---|---|---|---|---|---|---|---|---|---|---|
| **Panel C. MMF Holdings as Percentage of Amounts Outstanding, December 31, 2012** | | | | | | | | | | | |
| Prime | 8.82 | 12.10 | 2.07 | 3.97 | 1.49 | 1.61 | 46.43 | 40.17 | 45.16 | 5.63 | 34.74 |
| Treasury | 18.66 | 25.95 | 0.00 | 0.02 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| Other | 3.90 | 6.47 | 3.33 | 5.31 | 5.93 | 7.56 | 0.14 | 0.97 | 3.88 | 0.01 | 0.05 |
| *All MMF* | *31.37* | *44.52* | *5.40* | *9.30* | *7.42* | *9.17* | *46.56* | *41.13* | *49.04* | *5.64* | *34.78* |

Sources: Data on money market fund holdings is derived from Form N–MFP as of December 31, 2012. Data on outstanding Treasury debt, government agency debt, certificates of deposit and municipal debt comes from the Federal Reserve Board's Flow of Funds Accounts of the U.S. for Q4, 2012. Data on commercial paper (not seasonally adjusted) is derived from the Federal Reserve Board's Commercial Paper release for December 2012. VRDNs are Variable Rate Demand Notes; Fncl Co CP is Financial Company Commercial Paper; and ABCP is Asset-Backed Commercial Paper.

Because prime money market funds' holdings are large and their investment strategies differ from some investment alternatives, a shift by investors from prime money market funds to investment alternatives could affect the markets for short-term securities. The magnitude of the effect will depend on not only the size of the shift but also the extent to which there are portfolio investment differences between prime money market funds and the chosen investment alternatives. If, for example, investors in prime money market funds were to choose to manage their cash directly rather than invest in alternative cash management products, they might invest in securities that are similar to those currently held by prime funds. In this case, the effects on issuers and the short-term financing markets would likely be minimal.[592]

If, however, capital flowed from money market funds, which traditionally have been large suppliers of short-term capital, to bank deposits, which tend to fund longer-term lending and capital investments, issuers and the short-term financing markets may be affected to a greater extent. Similarly, if capital flowed from prime money market funds to government money market funds because government money market funds are exempt from further reforms, issuers that primarily issue to prime funds (and thus the short-term financing markets) would be affected. To put these potential shifts in context, on December 31, 2012, prime money market funds held approximately 46% of financial-company commercial paper outstanding and approximately 9% of Treasury bills outstanding, whereas Treasury money market funds held approximately 19% of Treasury bills outstanding but no financial company commercial paper.[593] A shift, therefore, from prime money market funds to Treasury money market funds could decrease demand for commercial paper and adversely

[592] The preference for this alternative, however, may be tempered by the cost to investors of managing cash on their own. *See, e.g., supra* note 571 and accompanying text.

[593] See *supra* Panel C.

affect financial commercial-paper issuers (in terms of the rate they must offer on their short-term debt securities), and could increase demand (thus lowering borrowing costs) in the market for government securities.

Historically, money market funds have been a significant source of financing for issuers of commercial paper, especially financial commercial paper, and for issuers of short-term municipal debt.[594] A shift by investors from prime money market funds to investment alternatives could cause a decline in demand for financial commercial paper and municipal debt, reducing these firms' and municipalities' access to capital from money market funds and potentially creating shortages of short-term financing for such firms and municipalities.[595] If, however, money market fund investors shift capital to investment alternatives that demand the same assets as prime money market funds, the net effect on the short-term financing markets would be small.

As discussed in the RSFI Study, the 2008–2012 increase in bank deposits coupled with the contraction of the money market funds presents an opportunity to examine how capital formation can be affected by a reallocation of capital among different funding sources. According to Federal Reserve Board flow of funds data, money market funds' investments in commercial paper declined by 45% or $277.7 billion from the end of 2008 to the end of 2012. Contemporaneously, funding corporations reduced their holdings of commercial paper by 99% or $357.7 billion.[596] The end result was a contraction of more than 40% or $647.5 billion in the amount of commercial paper outstanding. Analysis of Form N–MFP data from November 2010 through March 2013 indicates that financial company commercial paper and asset-backed commercial paper comprise most of money market funds' commercial paper holdings.[597]

Although the decline in funds' commercial paper holdings was large, it is important to place commercial paper borrowing by financial institutions into perspective by considering its size compared with other funding sources. As with non-financial businesses, financial company commercial paper is a small fraction (3.2%) of all credit market instruments.[598] We have also witnessed the ability of issuers, especially financial institutions, to adjust to changes in markets. Financial institutions, for example, dramatically reduced their use of commercial paper from $1,125.8 billion at the end of 2008 to $449.2 billion at the end of 2012 after regulators encouraged them to curtail their reliance on short-term wholesale financing.[599] As such, we believe that financial institutions, as well as other firms, would be able to identify over time alternate short-term financing sources if the amount of capital available for financial commercial paper declined in response to money market fund rule changes. Alternatively, commercial paper issuers may have to offer higher yields in order to attract alternate investors, potentially hampering capital formation for issuers. The increase in yield, however, may increase demand for these investments which may mitigate, to some extent, the potential adverse capital formation effects on the commercial paper market.

Municipalities also could be affected if our proposals caused the money market fund industry to contract. As shown in Panel C of the table immediately above, money market funds held approximately 9% of outstanding municipal debt securities as of December 31, 2012. Between the end of 2008 and the end of 2012, money market funds decreased their holdings of municipal debt by 34% or $172.8 billion.[600] Despite this reduction in holdings by money market funds, municipal issuers increased aggregate borrowings by over 4% between the end of 2008 and the end of 2012. Municipalities were able to fill the gap by attracting other investor types. Other types of mutual funds, for example, increased their municipal securities holdings by 61% or $238.6 billion. Depository institutions have also increased their funding of municipal issuers during this time period by $141.2 billion as investors have shifted their assets away from money market funds into bank deposit accounts. Life insurance companies almost tripled their municipal securities holdings from $47.1 billion at the end of 2008 to $121 billion at the end of 2012. It would have been difficult to model in 2008 which investors would step into the municipal debt market to take the place of withdrawing money market funds and, for the same reasons, it is difficult now to predict what may happen to the municipal debt markets as a result of our proposal.

To make their issues attractive to alternative lenders, municipalities lengthened the terms of some of their debt securities. Most municipal debt securities held by money market funds are variable rate demand notes (''VRDNs''), in which long-term

[594] Based on Form N–MFP data, non-financial company commercial paper, which includes corporate and non-financial business commercial paper, is a small fraction of overall money market holdings. In addition, commercial paper financing by non-financial businesses is a small portion (one percent) of their overall credit market instruments. According to Federal Reserve Board flow of funds data, as of December 31, 2012 non-financial company commercial paper totaled $130.5 billion compared with $12,694.2 billion of total credit market instruments outstanding for these entities. As such, we do not anticipate a significant effect on the market for non-financial corporate fund raising. Federal Reserve Board flow of funds data is available at *http://www.federalreserve.gov/releases/z1/Current/z1.pdf*.

[595] *See, e.g.,* Comment Letter of Associated Oregon Industries (Jan. 18, 2013) (available in File No. FSOC–2012–0003) (stating that if the proposed reforms ''drive investors out of money market funds, the flow of short-term capital to businesses will be significantly disrupted.''); U.S. Chamber Jan. 23, 2013 FSOC Comment Letter, *supra* note 248 (stating that ''any changes [that make MMFs] a less attractive investment will impact the overall costs for issuers in the commercial paper market resulting from a reduced demand in commercial paper.''); Comment Letter of N.J. Municipal League (Jan. 23, 2013) (available in File No. FSOC–2012–0003) (stating that ''money market funds hold more than half of the short-term debt that finances state and municipal governments for public projects,'' which could force local governments to ''limit projects and staffing, spend more on financing . . . or increase taxes'' if such financing was no longer available.); Comment Letter of Government Finance Officers Association, et al. (Feb. 13, 2013) (available in File No. FSOC–2012–0003) (stating that with respect to FSOC's floating NAV proposal, ''changing the fundamental feature of MMMFs . . . would dampen investor demand for municipal securities and therefore could deprive state and local governments and other borrowers of much-needed capital.'').

[596] The Federal Reserve flow of funds data defines funding corporations as ''funding subsidiaries, custodial accounts for reinvested collateral of securities lending operations, Federal Reserve lending facilities, and funds associated with the Public-Private Investment Program (PPIP).''

[597] In addition, according to the RSFI Study, *supra* note 21, ''as of March 31, 2012, money market funds held $1.4 trillion in Treasury debt, Treasury repo, Government agency debt, and Government agency repo as its largest sector exposure, followed by $659 billion in financial company commercial paper and CDs, its next largest sector exposure.''

[598] According to the Federal Reserve Flow of Funds data as of December 31, 2012, commercial paper outstanding was $449.2 billion compared with $13,852.2 billion of total credit market instruments outstanding for financial institutions.

[599] The statistics in this paragraph are based on the Federal Reserve Board's Flow of Funds data. *See also* 2012 FSOC Annual Report, *available at http://www.treasury.gov/initiatives/fsoc/Documents/2012%20Annual%20Report.pdf,* at 55–56, 66 (showing substantial declines in domestic banking firm's reliance on short-term wholesale funding compared with deposit funding). The Basel III liquidity framework also proposes requirements aimed at limiting banks' reliance on short-term wholesale funding. *See* 2011 FSOC Annual Report, *available at http://www.treasury.gov/initiatives/fsoc/Documents/FSOCAR2011.pdf,* at 90 (describing Basel III's proposed liquidity coverage ratio and the net stable funding ratio); Basel Committee on Banking Supervision: Basel III: The Liquidity Coverage Ratio and liquidity risk monitoring tools (Jan. 2013), *available at http://www.bis.org/publ/bcbs238.pdf* (describing revisions to the liquidity coverage ratio).

[600] The statistics in this paragraph are based on the Federal Reserve Board's Flow of Funds data.

municipal bonds are transformed into short-term instruments through the use of third-party credit and/or liquidity enhancements, such as letters of credit and standby bond purchase agreements from financial institutions. Declines in the creditworthiness of these credit and liquidity enhancement providers have reduced the amount of VRDNs outstanding from approximately $371 billion in December 2010 to approximately $264 billion in December 2012.[601] We believe that this downward trend is likely to continue irrespective of changes in the money market fund industry because of potential downgrades to the financial institutions providing these services and potential bank regulatory changes, which may increase the cost of providing such guarantees.[602]

Additionally, our floating NAV proposal has an explicit exemption for retail funds that will permit sponsors to offer retail funds that seek to maintain a stable price and invest in municipal securities. We expect that the net investment in municipal money market funds will not change in response to the floating NAV proposal because we understand that few institutional investors invest in retail funds today and believe that most retail investors would not object to the daily $1,000,000 redemption limit. Investment in retail money market funds may in fact increase, if investors see stable price retail funds as an attractive cash management tool compared to other alternatives.

Both the floating NAV proposal and the requirement of increased disclosure under each alternative regarding the fund's market-based value and liquidity as well as any sponsor support or defaults in portfolio securities, among other matters, should improve informational efficiency. The floating NAV alterative as well as the proposed shadow NAV disclosure requirement under the liquidity fees and gates alternative provide greater transparency to shareholders regarding the daily market-based value of the fund. This should improve investors' ability to allocate capital efficiently across the economy. Under the liquidity fees and gates proposal, if a fund imposes a liquidity fee or redemption gate, this may hamper allocative efficiency and hence capital formation to the extent that investors are unable to reallocate their assets to their preferred use while the fee or gate is in place.

Our proposals may or may not affect competition within the short-term financing markets. On the one hand, the competitive effects are likely to be small or negligible if shareholders either remain in money market funds or move to alternatives that, in turn, invest in similar underlying assets. On the other hand, the effects may be large if investors reallocate (whether directly or through intermediaries) their investments into substantively different assets. In that case, issuers are likely to offer higher yields to attract capital, whether from the smaller money market fund industry or from other investors. Either way, issuers that are unable to offer the required higher yield may have difficulties raising their required capital, at least in the short-term financing markets.

We request comment on what effects our proposals would have on issuers and the short-term financing markets for issuers. In particular, we request that commenters discuss whether the effects would be different between the floating NAV alterative and the liquidity fees and gates alternative and to provide analysis of the magnitude of the difference.

- How would either reform proposal affect issuers in the short-term financing markets, whether through a smaller money market fund industry or through fewer highly risk-averse investors holding money market funds shares?
- Would either reform proposal result in increased stability in money market funds and hence enhance stability in the short-term financing markets and the willingness of issuers to rely on short-term financing because the issuers would be less exposed to volatility in the availability of short-term financing from money market funds?
- What effect would either proposal have on the issuers of commercial paper and short-term municipal debt? How would either proposal affect the market for short-term government securities?
- What would be the long-term effect from either alternative on the economy? Please include empirical data to support any conclusions.

We expect that yields in prime money market funds under the floating NAV alternative could be higher than yields under our fees and gates alternative. Under the fees and gates proposal, prime money market funds would have an incentive to closely manage their weekly liquid assets, which they could do by holding larger amounts of such assets, which tend to have comparatively low yields. If so, this would provide a competitive advantage for issuers that are able and willing to issue assets that qualify as weekly liquid assets, and it might result in the overall short-term financing markets being tilted toward shorter-term issuances. We believe that prime money market funds under this proposal would not meet the increased demand for weekly liquid assets solely by increasing their investments in Treasury securities because investors that want the risk-return profile that comes from Treasury securities would probably prefer to invest in Treasury funds, which would be exempt from key aspects of either of our provisions of the proposal. Under the floating NAV proposal, prime money market funds might not have an incentive to reduce portfolio risk if the relatively more risk-averse investors avoid prime money market funds and invest in government money market funds or retail funds, which would continue to maintain a stable price. If so, this would provide a competitive advantage for issuers of higher-yielding 2a–7-eligible assets. The potential differing portfolio composition of money market funds under our two reform proposals, therefore, could have an effect on issuers and the short-term financing markets through differing levels of money market fund demand for certain types of portfolio securities.

We request comment on this aspect of our proposal and how the effect on money market fund yields, short-term debt security issuers, and the short-term financing markets would differ depending on which alternative we adopted.

We request comment on our assumptions, expectations, and estimates described in this section.

- Are they correct?
- Do commenters agree with our analyses of certain effects on efficiency, competition, and capital formation that may arise from our floating NAV and liquidity fees and gates proposals? Do commenters agree with our analysis of potential additional implications of these proposals on current investments in money market funds and on the short-term financing markets?
- Are there alternative assumptions, expectations, or estimates that we have

[601] *See* Securities Industry and Financial Markets Association U.S. Municipal VRDO Update (Dec. 2012), *available at http://www.sifma.org/research/item.aspx?id=8589941389.* This data has some limitations as its estimate for outstanding VRDNs in December 2012 is lower than our estimate of money market fund holdings of VRDNs from Form N–MFP as of December 31, 2012.

[602] *See, e.g.,* Moody's Downgrades U.S. Muni Obligations Backed by Banks and Securities Firms with Global Capital Markets Operations (June 22, 2012), *available at http://www.moodys.com/research/Moodys-downgrades-US-muni-obligations-backed-by-banks-and-securities-PR_248937*; Chris Reese, *Money Market Funds' Investments Declining,* Reuters (Oct. 24, 2011) (stating that supplies of VRDNs have been constrained and that the ''decline in issuance can be attributed to low interest rates, challenges of budget shortfalls at state and local governments and knock-on effects from European banking concerns''); Dan Seymour, *Liquidity Fears May Be Overblown,* Bond Buyer (Jan. 31, 2011).

not discussed? If so, what are they and how would they affect our analyses?

• Are there any other economic effects associated with our proposed alternatives that we have not discussed? Please quantify and explain any assumptions used in response to these questions (and any others) to the extent possible.

• What would have been the effect on money market funds, investors, the short-term financing markets, and capital formation if our floating NAV proposal or our liquidity fees and gates proposal had been in place in 2007 and 2008?

*F. Amendments to Disclosure Requirements*

We are proposing amendments to rule 2a–7 and Form N–1A that would require money market funds to provide additional disclosure in certain areas to provide greater transparency regarding money market funds, so that investors have an opportunity to better evaluate the risks of investing in a particular fund and that the Commission and other financial regulators obtain important information needed to administer their regulatory programs. As discussed in more detail below, these amendments would require enhanced registration statement and Web site disclosure [603] about: (i) Any type of financial support provided to a money market fund by the fund's sponsor or an affiliated person of the fund; (ii) the fund's daily and weekly liquidity levels; and (iii) the fund's daily current NAV per share, rounded to the fourth decimal place in the case of funds with a $1.0000 share price or an equivalent level of accuracy for funds with a different share price (*e.g.,* $10.000 or $100.00 per share). In addition, we are considering whether to require more frequent disclosure of money market funds' portfolio holdings. We are also proposing amendments to rule 2a–7 that would require stable price money market funds to calculate their current NAV per share (rounded to the fourth decimal place in the case of funds with a $1.0000 share price or an equivalent level of accuracy for funds with a different share price) daily, as a corollary to the proposed requirement for money market funds to disclose their daily current NAV per share.

In addition, we are proposing a new rule [604] that would require money market funds to file new Form N–CR with the Commission when certain events (such as instances of portfolio security default, sponsor support of funds, and other similar significant events) occur. The proposed Form N–CR filing requirements are discussed below at section III.G.

1. Financial Support Provided to Money Market Funds

a. Proposed Disclosure Requirements

Throughout the history of money market funds, and in particular during the 2007–2008 financial crisis, money market fund sponsors and other fund affiliates have, on occasion, provided financial support to money market funds.[605] Indeed, one study estimates that during the period from 2007 to 2011, direct sponsor support to money market funds totaled at least $4.4 billion, for 78 of the 314 funds the study reviewed.[606] We continue to believe that sponsor support will provide fund sponsors with the flexibility to protect shareholder interests. Additionally, if we ultimately adopt the liquidity fees and gates alternative, sponsor support would allow sponsors the flexibility to prevent a money market fund from breaching the 15% weekly liquid asset threshold that would otherwise require the board to impose a liquidity fee (absent a board finding that doing so would not be in the fund's best interest) and permit the board to impose a gate. However, we believe that if money market fund investors do not understand the nature and extent that the fund's sponsor has discretionarily supported the fund, they may not fully appreciate the risks of investing in the fund.[607]

For these reasons, we propose requiring money market funds to disclose current and historical instances of sponsor support. We believe that these disclosure requirements would clarify, to current and prospective money market fund investors as well as to the Commission, the frequency, nature, and amount of financial support provided by money market fund sponsors. We believe that the disclosure of historical instances of sponsor support would allow investors, regulators, and the fund industry to understand better whether a fund has required financial support in the past. Currently, when sponsor support is provided during circumstances in which a money market fund experiences stress but does not ''break the buck,'' and sponsor support is not immediately disclosed, investors may be unaware that their money market fund has come under stress.[608] The proposed historical disclosure would permit investors to understand whether, for instance, a fund's sponsor or affiliate has provided financial support to help mitigate liquidity stress experienced by the fund, or has repurchased fund portfolio securities that have fallen in value. While we recognize that historical occurrences are not necessarily indicative of future events, the proposed disclosure also would permit investors to assess the sponsor's past ability and willingness to provide financial support to the fund, which could reflect the sponsor's financial position or management style.[609] Finally, the proposed disclosure would provide greater information to regulators and the fund industry regarding the extent of financial support that money market funds receive from their sponsors and other affiliates, which could assist regulators in overseeing money market funds and administering their regulatory programs.

Accordingly, we are proposing amendments to Form N–1A that would require money market funds to provide SAI disclosure [610] regarding historical instances in which the fund has received financial support from a sponsor or fund affiliate.[611] Specifically, the proposed amendments would require each money market fund to disclose any occasion during the last ten years on which an affiliated person, promoter, or principal underwriter of the fund, or an affiliated person of such

[603] *See supra* note 448.

[604] Proposed rule 30b1–8.

[605] *See, e.g., supra* section II.B.3; *see also* RSFI Study, *supra* note 21, at notes 20–21 and accompanying text.

[606] *See* Federal Reserve Bank of Boston Staff Risk and Policy Analysis Working Paper No. 12–3 (Aug. 13, 2012).

[607] *See* FSOC Proposed Recommendations, *supra* note 114 (noting, for example, that ''[w]hile MMF prospectuses must warn investors that their shares may lose value, the extensive record of sponsor intervention and its critical role historically in maintaining MMF price stability may have obscured some investors' appreciation of MMF risks and caused some investors to assume that MMF sponsors will absorb any losses, even though sponsors are under no obligation to do so'') (internal citations omitted). *But see* ICI Jan. 24 FSOC Comment Letter, *supra* note 25, and Federated Investors Feb. 15 FSOC Comment Letter, *supra* note 192.

[608] *See* RSFI Study, *supra* note 21, at text following note 25.

[609] *But see* Moody's Investors Service, ''Sponsor Support Key to Money Market Funds'' (Aug. 9, 2010), at 5–6 *available at http://www.alston.com/files/docs/Moody's_report.pdf* (suggesting that fund sponsors may be unwilling to provide sponsor support in future years).

[610] *See supra* note 440 (discussing guiding principles that are used to determine whether to include disclosure items in a fund's prospectus or SAI).

[611] *See* proposed (FNAV) Item 16(g) of Form N–1A; proposed (Fees & Gates) Item 16(g)(2) of Form N–1A. Requiring this disclosure to appear in the fund's SAI, rather than the prospectus, reflects the principle that funds should limit disclosure in prospectuses generally to information that is necessary for an average or typical investor to make an investment decision. *See* Registration Statement Adopting Release, *supra* note 310, at section I.

person,[612] provided any form of financial support to the fund.[613] With respect to each such occasion, the proposed amendments would require the fund to describe the nature of support, the amount of support, the date the support was provided, the security supported and its value on the date the support was initiated (if applicable), the reason for the support, the term of support (if applicable), and any contractual restrictions relating to the support.[614] We believe that the proposed 10-year look-back period would provide shareholders and the Commission with a historical perspective that would be long enough to provide a useful understanding of past events, and to analyze patterns with respect to financial support received by the fund, but not so long as to include circumstances that may no longer be a relevant reflection of the fund's management or operations. We believe that disclosing historical information about the financial support that a fund has received from a sponsor or fund affiliate in the fund's SAI is the clearest and least expensive means to disseminate this disclosure. We believe that other possible methods, such as requiring public disclosure of a sponsor's financial statements (such that non-shareholders could evaluate the sponsor's capacity to provide support) would provide less straightforward information to investors, and would be costlier for funds to implement than the proposed SAI disclosure requirement.

Because past analyses of financial support provided to money market funds have differed in their assessment of what actions constitute such support,[615] we are also proposing instructions to the proposed amendments that would clarify the meaning of the term ''financial support'' for purposes of the required disclosure.[616] These proposed instructions would specify that the term ''financial support'' would include, but not be limited to (i) any capital contribution, (ii) purchase of a security from the fund in reliance on rule 17a–9, (iii) purchase of any defaulted or devalued security at par, (iv) purchase of fund shares, (v) execution of a letter of credit or letter of indemnity, (vi) capital support agreement (whether or not the fund ultimately received support), (vii) performance guarantee, or (viii) any other similar action to increase the value of the fund's portfolio or otherwise support the fund during times of stress.[617] The Commission believes that all of these actions should be included in the term ''financial support'' because they each represent means by which a fund's sponsor or affiliate could provide financial or monetary assistance to a fund by directly increasing the value of a fund's portfolio, or (for funds that maintain a stable share price) by otherwise permitting a fund to maintain its current intended stable price per share. We are also proposing instructions to the proposed amendments to clarify that funds must disclose any financial support provided to a predecessor fund (in the case of a merger or other reorganization) within the proposed look-back period, in order to allow investors to understand the full extent of historical support, provided to a fund or its predecessor. Specifically, these proposed instructions would state that if the fund has participated in a merger with another investment company during the last ten years,[618] the fund must additionally provide the required disclosure with respect to the other investment company.[619]

We request comment on the proposed amendments to Form N–1A that would require money market funds to provide disclosure regarding historical instances in which the fund has received financial support from a sponsor or other fund affiliate.

- Would the proposed disclosure regarding historical instances of financial support provided to money market funds assist investors in appreciating the risks of investing in money market funds generally, and/or in particular money market funds? Do investors already appreciate the extent of financial support that money market funds sponsors and other affiliates have historically provided, and that such support has been provided on a discretionary basis?
- We request comment on the specific disclosure items contemplated by the proposed SAI disclosure requirement. Is there any additional information, with respect to the historical instances in which a money market fund has received financial support from a sponsor or other fund affiliate, that funds should be required to disclose? Would all of the items included in the proposed SAI disclosure assist shareholders' understanding of the historical financial support provided to a fund? If not, which items should we not include, and why?
- Instead of, or in addition to, requiring funds to disclose historical information about financial support received from a sponsor or fund affiliate on the fund's SAI, should we require fund sponsors to publicly disclose their financial statements, in order to permit non-shareholders to evaluate the sponsor's capacity to provide support? Why or why not?
- We request comment on the proposed instruction clarifying the meaning of the term ''financial support'' by providing a non-exclusive list of examples of actions that would be deemed to be ''financial support'' for purposes of the proposed disclosure requirement. Should the proposed instruction be expanded or limited, and if so, how and why?
- We request comment on the 10-year look-back period contemplated by the proposed SAI disclosure requirement. Should the proposed disclosure requirement include a longer or shorter look-back period, and if so, why?
- We request comment on the list of persons whose financial support of a fund would necessitate disclosure under the proposed SAI disclosure requirement. Should this list of persons be expanded or limited, and if so, why?
- We request comment on the proposed instruction requiring disclosure of any financial support provided to a predecessor fund. Are there other situations, besides those identified in this instruction, in which disclosure of financial support provided

[612] Rule 2a–7 currently requires a money market fund to report to the Commission the purchase of money market fund portfolio securities by an affiliated person, promoter, or principal underwriter of the fund, or an affiliated person of such person, pursuant to rule 17a–9. *See* rule 2a–7(c)(7)(iii)(B). Because the proposed definition of ''financial support'' includes the purchase of a security pursuant to rule 17a–9 (as well as similar actions), we believe that the scope of the persons covered by the proposed definition should reflect the scope of persons covered by rule 2a–7(c)(7)(iii)(B).

[613] *See* proposed (FNAV) Item 16(g) of Form N–1A; proposed (Fees & Gates) Item 16(g)(2) of Form N–1A.

[614] *See infra* notes 616 and 617 and accompanying text for a discussion of actions that would be deemed to constitute ''financial support.''

[615] *See, e.g.,* study accompanying Comment Letter of Linus Wilson (Jan. 1, 2013) (available in File No. FSOC–2012–0003) (discussing various definitions of ''support'' used in analyzing historical instances of support provided to money market funds by their sponsors or other affiliated persons).

[616] *See* Instruction 1 to proposed (FNAV) Item 16(g) of Form N–1A; Instruction 1 to proposed (Fees & Gates) Item 16(g)(2) of Form N–1A.

[617] *Id.*

[618] For purposes of this instruction, the term ''merger'' means a merger, consolidation, or purchase or sale of substantially all of the assets between the fund and another investment company. *See* Instruction 2 to proposed (FNAV) Item 16(g) of Form N–1A; Instruction 2 to proposed (Fees & Gates) Item 16(g)(2) of Form N–1A.

[619] *See* Instruction 2 to proposed (FNAV) Item 16(g) of Form N–1A; Instruction 2 to proposed (Fees & Gates) Item 16(g)(2) of Form N–1A. Additionally, if a fund's name has changed (but the corporate or trust entity remains the same), we would expect the fund to provide the required disclosure with respect to the entity or entities identified by the fund's former name.

to a fund or other entity besides the fund named on the registration statement would assist shareholders in understanding attendant investment risks? Are there any situations in which the merger-related disclosure that we propose to require would not assist shareholders in understanding the risks of investing in the fund named on the registration statement (for instance, if the fund's sponsor has changed as a result of the merger)? Would the proposed merger-related disclosure make it more difficult for a fund with a history of support to merge with another fund?

• Would it be useful for shareholders for the Commission to require prospective prospectus and/or SAI disclosure regarding the circumstances under which a money market fund's sponsor, or an affiliated person of the fund, may offer any form of financial support to the fund, as well as any limits to this support? If so, what kind of disclosure should be required?

We believe it is important for money market funds to inform existing and prospective shareholders of any present occasion on which the fund receives financial support from a sponsor or other fund affiliate. We believe that this disclosure could influence prospective shareholders' decision to purchase shares of the fund, and could inform shareholders' assessment of the ongoing risks associated with an investment in the fund. We believe that it is possible that shareholders would interpret prior support as a sign of fund strength, as it demonstrates the sponsor's willingness to backstop the fund. However, we also recognize that this disclosure could potentially make shareholders quicker to redeem shares if they believe the provision of financial support to be a sign of weakness, or an indication that the fund may not continue in business in the future (for instance, if providing financial support to a fund were to weaken the sponsor's own financial condition, possibly affecting its ability to manage the fund).

We are proposing an amendment to rule 2a–7 that would require a fund to post prominently on its Web site substantially the same information that the fund is required to report to the Commission on Form N–CR regarding the provision of financial support to the fund.[620] The fund would be required to include this Web site disclosure on the same business day as it files a report to the Commission in response to an event specified in Part C of Form N–CR, and the disclosure would be required to be posted for a period of not less than one year following the date on which the fund filed Form N–CR concerning the event.[621] We believe that requiring Web site disclosure, along with Form N–CR disclosure, is an important step towards increased transparency because we believe that significant information about a money market fund is already made available at that fund's Web site.[622] As discussed in more detail below, we believe that this time frame for reporting balances the exigency of the report with the time it will reasonably take a fund to compile the required information (which is the same information a fund would be required to file on Form N–CR).[623] We believe that the one-year minimum time frame for Web site disclosure is appropriate because this time frame would effectively oblige a fund to post the required information in the interim period until the fund files an annual post-effective amendment updating its registration statement, which update would incorporate the same information.[624]

We request comment on the proposed amendment to rule 2a–7 that would require money market funds to inform current and prospective shareholders, via Web site, of any present occasion on which the fund receives financial support from a sponsor or other fund affiliate.

• Should any more, any less, or any other information be required to be posted on the fund's Web site than that disclosed on Form N–CR? Is the fund's Web site the best place for us to require such disclosure?

• As proposed, should we require this information to be posted ''prominently'' on the fund's Web site? Should we provide any other instruction as to the presentation of this information, in order to highlight the information and/or lead investors efficiently to the information, for example, should we require that the information be posted on the fund's home page or be accessible in no more than two clicks from the fund's home page?

• Should this information be posted on the fund's Web site for a longer or shorter period than one year following the occurrence of any event specified in Part C of Form N–CR?

• How would the requirement for money market funds to disclose current instances of financial support affect the behavior of fund shareholders and/or the market as a whole? For instance, could this disclosure make shareholders quicker to redeem shares if they believe the provision of financial support to be a sign of portfolio weakness?[625] Alternatively, would shareholders prefer funds with histories of support because of the sponsors' demonstrated willingness to backstop the funds?

b. Economic Analysis

The qualitative benefits and costs of the proposed requirements regarding the disclosure of financial support received by a fund from its sponsor or a fund affiliate are discussed above. The Commission staff has not measured the quantitative benefits of these proposed requirements at this time because of uncertainty regarding how the proposed disclosure may affect different investors' behavior.[626] Because the required registration statement and Web site disclosure overlap with the information that a fund must disclose on Form N–CR when the fund receives financial support from a sponsor or fund affiliate, we anticipate that the costs a fund will incur to draft and finalize the disclosure that will appear in its registration statement and on its Web site will largely be incurred when the fund files Form N–CR, as discussed below in section III.G.3.[627] In addition, we

[620] *See* proposed (FNAV) rule 2a–7(h)(10)(v); proposed (Fees & Gates) rule 2a–7(h)(10)(v); proposed (FNAV) Form N–CR Part C; proposed (Fees & Gates) Form N–CR Part C; *see also infra* section III.G (discussing the proposed Form N–CR requirements).

[621] *See* proposed (FNAV) rule 2a–7(h)(10)(v); proposed (Fees & Gates) rule 2a–7(h)(10)(v). A fund would also be required to file Form N–CR no later than the first business day following the occurrence of any event specified in Part C of Form N–CR.

[622] *See supra* note 448.

[623] *See infra* text following note 710.

[624] *See supra* notes 611—619 and accompanying text. Of course, in the likely event that the fund files a post-effective amendment within one year following the provision of financial support to the fund, information about the financial support would appear both in the fund's registration statement and on the fund's Web site for the remainder of the year following the provision of support.

[625] *See* Federated Investors Feb. 15 FSOC Comment Letter, *supra* note 192 (noting that enhanced disclosure requirements may have unintended consequences).

[626] Likewise, the SEC staff has not presently quantified the benefits of the proposed requirements on account of uncertainty regarding the effects that the requirements may have on, for example, investors' understanding of the risks associated with money market funds, investors' ability to compare the relative risks of investing in different funds, the potential imposition of market discipline on portfolio managers, or the Commission's ability to execute its oversight role.

[627] Although the proposed registration statement disclosure would include historical information about the financial support that a fund has received from its sponsor or other fund affiliate(s), and the proposed Form N–CR and Web site disclosure would include information about current instances of financial support, the required disclosure elements for the proposed Form N–CR disclosure, Web site disclosure, and registration statement disclosure are identical. Therefore, we anticipate that a fund would largely be able to use the disclosure it drafted for purposes of the Form N–CR and Web site disclosure requirements for

estimate that a fund would incur costs of $148[628] to review and update the historical disclosure in its registration statement (plus printing costs), and costs of $207[629] each time that it updates its Web site to include the required disclosure.

We believe that the proposed requirements could increase informational efficiency by providing additional information to investors and the Commission about the frequency, nature, and amount of financial support provided by money market fund sponsors. This in turn could assist investors in analyzing the risks associated with particular funds, which could increase allocative efficiency[630] and could positively affect competition by permitting investors to choose whether to invest in certain funds based on this information. However, the proposed requirements could advantage larger funds and fund groups, if a fund sponsor's ability to provide financial support to a fund is perceived to be a competitive benefit. Also, if investors move their assets among money market funds or decide to invest in investment products other than money market funds as a result of the proposed disclosure requirements, this could adversely affect the competitive stance of certain money market funds, or the money market fund industry generally.

The proposed disclosure requirements also could have additional effects on capital formation, depending on if investors interpret financial support as a sign of money market fund strength or weakness. If sponsor support (or the lack of need for sponsor support) were understood to be a sign of fund strength, the proposed requirements could enhance capital formation by promoting stability within the money market fund industry. On the other hand, the proposed disclosure requirements could detract from capital formation if sponsor support were understood to indicate fund weakness and made money market funds more susceptible to heavy redemptions during times of stress, or if money market fund investors decide to move their money out of money market funds entirely as a result of the proposed disclosure. Accordingly, because we do not have the information necessary to provide a reasonable estimate, we are unable to determine the effects of this proposal on capital formation. Finally, the required disclosure could assist the Commission in overseeing money market funds and developing regulatory policy affecting the money market fund industry, which might affect capital formation positively if the resulting more efficient or more effective regulatory framework encouraged investors to invest in money market funds.

We request comment on this economic analysis:

- Are any of the proposed disclosure requirements unduly burdensome, or would they impose any unnecessary costs?
- We request comment on the staff's estimates of the operational costs associated with the proposed disclosure requirements.
- We request comment on our analysis of potential effects of these proposed disclosure requirements on efficiency, competition, and capital formation. In particular, would the proposed disclosure increase informational efficiency by increasing awareness of sponsor support? If so, would the disclosure requirements for sponsor support make money market funds more or less susceptible to heavy redemptions in times of fund and market stress?

2. Daily Disclosure of Daily Liquid Assets and Weekly Liquid Assets

a. Proposed Disclosure Requirements

We are proposing amendments to rule 2a–7 that would require money market funds to disclose prominently on their Web sites the percentage of the fund's total assets that are invested in daily and weekly liquid assets, as well as the fund's net inflows or outflows, as of the end of the previous business day.[631] The proposed amendments would require a fund to maintain a schedule, chart, graph, or other depiction on its Web site showing historical information about its investments in daily liquid assets and weekly liquid assets, as well as the fund's net inflows or outflows, for the previous 6 months, and would require the fund to update this historical information each business day, as of the end of the preceding business day.[632] These amendments would complement the proposed requirement, as discussed elsewhere in this Release, for money market funds to provide on their monthly reports on Form N–MFP the percentage of total assets invested in daily liquid assets and weekly liquid assets broken out on a weekly basis.[633]

We believe that daily disclosure of money market funds' daily liquid assets and weekly liquid assets would promote transparency regarding how money market funds are managed, and thus may permit investors to make more efficient and informed investment decisions. Additionally, we believe that this enhanced disclosure may impose external market discipline on portfolio managers, in that it may encourage fund managers to carefully manage their daily and weekly liquid assets, which may decrease portfolio risk and promote stability in the short-term financing markets.[634] We also believe that it could encourage funds to ensure that the fund's liquidity level is at least as large as its shareholders' demand for liquidity. The proposed daily disclosure requirement would provide an additional level of detail to the proposed requirement for money market funds to break out their daily liquid assets and weekly liquid assets on a weekly basis on their monthly reports on Form N–MFP, which in turn would further enhance investors' and the Commission's ability to monitor fund risks. For example, daily Web site disclosure of liquid asset levels would help investors estimate, in near-real time, the likelihood that a fund may be able to satisfy redemptions by using internal cash sources (rather than by selling portfolio securities) in times of market turbulence, or, if our liquidity fees and gates proposal is adopted, whether a fund may approach or exceed a trigger for the potential imposition of a liquidity fee or gate. Requiring daily Web site disclosure of liquid assets across the money market fund industry also would permit investors more readily to determine whether liquidity-related stresses are idiosyncratic to particular funds, thus minimizing the prospect of redemption pressures on funds that are not similarly affected.[635] This disclosure also could make information about fund liquidity more accessible to a broad range of investors. This daily Web site disclosure should also assist the Commission in its

purposes of the registration statement disclosure requirement.

[628] The costs associated with updating the fund's registration statement are paperwork-related costs and are discussed in more detail in *infra* section IV.A.7 and IV.B.7.

[629] The costs associated with updating the fund's Web site are paperwork-related costs and are discussed in more detail in *infra* section IV.A.1.f and IV.B.1.f.

[630] *See supra* note 562 and accompanying text.

[631] *See* proposed (FNAV) rule 2a–7(h)(10)(ii); proposed (Fees & Gates) rule 2a–7(h)(10)(ii). A ''business day,'' defined in rule 2a–7 as ''any day, other than Saturday, Sunday, or any customary business holiday,'' would end after 11:59 p.m. on that day.

[632] *Id.*

[633] *See infra* note 769 and accompanying text.

[634] *See* ICI Jan. 24 FSOC Comment Letter, *supra* note 25 (stating that prime money market funds should be required to make frequent public disclosure (via their Web sites) of their weekly liquid asset levels to ''enhance transparency and encourage a highly conservative approach to portfolio management'').

[635] *See* ICI Jan. 24 FSOC Comment Letter, *supra* note 25.

oversight role and promote certain efficiencies, in that it would permit the Commission to access detailed portfolio liquidity information as necessary to its oversight of money market funds, without the need to contact fund management or service providers to obtain it. However, the proposed disclosure could also change behavior, in that it could make shareholders quicker to redeem shares if they believe a decrease in portfolio liquidity could affect the fund's ability to satisfy redemptions.[636] The proposed disclosure also could increase the volatility of a fund's flows, even during times when the fund is not under stress, if shareholders are sensitive to changes in the fund's liquidity levels.[637]

While investors will be able to access historical information about money market funds' daily liquid assets and weekly liquid assets if the proposed amendments to Form N–MFP are adopted,[638] we believe that daily Web site disclosure of money market funds' daily liquid assets and weekly liquid assets, as well as the fund's net inflows or outflows, would permit shareholders to access more detailed information in a more convenient and detailed manner than comparing monthly Form N–MFP filings. We believe that investors would be able to compare current liquidity information with previous information from which they (or others) may discern trends. Public daily disclosure of money market funds' daily liquid assets and weekly liquid assets also could decrease funds' susceptibility to runs, as shareholders might be less likely to redeem fund shares during the occurrence of negative market events if they could ascertain, in near real time, that the fund had enough liquidity such that remaining shareholders would not bear the costs of liquidity incurred by redeeming shareholders. Because money market funds are currently required to maintain a six-month record of portfolio holdings on the fund Web site,[639] requiring a fund to post its daily liquid assets and weekly liquid assets for the same period would permit investors to analyze the relationship between the fund's portfolio holdings and its liquidity levels over time. Additionally, we believe that disclosure of information about net shareholder flow would provide helpful contextual information regarding the significance of the reported liquidity information, as a fund would require greater liquidity to respond to greater shareholder flow volatility, and vice versa.

We request comment on the proposed amendments to rule 2a–7 that would require money market funds to disclose daily the percentages of fund assets invested in daily and weekly liquid assets, as well as the fund's net inflows or outflows.

- Would the proposed amendments be useful in assisting shareholders in better understanding how money market funds are managed and in assessing a fund's risk? Would the proposed amendments promote the goals of enhancing transparency and encouraging market discipline on money market funds in a way that increases stability in the short-term financing markets? How, if at all, would the proposed amendments affect the amount of liquid assets that a money market fund's investment adviser purchases on behalf of the fund? Would disclosing information about net shareholder flows assist investors in understanding the significance of the reported liquidity information?
- Should we require that any more, any less, or any other information regarding portfolio liquidity be posted on money market funds' Web sites?
- As proposed, should we require this information to be posted ''prominently'' on the fund's Web site? Should we provide any other instruction as to the presentation of this information, in order to highlight the information and/or lead investors efficiently to the information? For example, should we require that the information be posted on the fund's home page or be accessible in no more than two clicks from the fund's home page?
- Should we require information regarding the percentage of money market fund assets invested in daily liquid assets and weekly liquid assets to be posted less frequently than daily? Should we require funds to maintain this information on their Web sites for a period of more or less than 6 months?
- Would the proposed amendments incentivize a money market fund, in certain circumstances, to sell assets that are not weekly liquid assets rather than weekly liquid assets? Will this harm non-redeeming shareholders?
- How would the requirement for money market funds to disclose the percentages of fund assets invested in daily liquid assets and weekly liquid assets affect the behavior of fund shareholders and/or the market as a whole? For instance, could this disclosure make shareholders quicker to redeem shares upon a decrease in portfolio liquidity, or generally increase the volatility of a fund's flows? Would this disclosure result in reducing the chances that better-informed shareholders may redeem ahead of retail or less informed shareholders? If the liquidity fees and gates proposal is adopted, would transparency of fund liquidity be important to permit investors in funds other than the one imposing a fee to assess the liquidity position of their fund before determining whether to redeem? Would such transparency affect investors' redemptions in normal market conditions or just in periods when liquidity is costly? Would such transparency affect investors' willingness to buy shares? How are these factors related to what motivates money market fund investors to redeem?
- Would disclosure of money market funds' liquidity levels, coupled with portfolio holdings reported on Form N–MFP (and more frequent portfolio holdings disclosure on funds' Web sites, to the extent the Commission determines to require this[640]), enable other market participants to infer a fund's potential liquidity demand and likely trading needs by the fund? Would this disadvantage a money market fund in any way?

b. Economic Analysis

The qualitative benefits and costs of the proposed requirements regarding disclosure of the percentage of a money market fund's assets that are invested in daily liquid assets and weekly liquid assets, as well as the fund's net inflows or outflows, are discussed above.[641] We believe that the proposed requirements could increase informational efficiency by providing additional information about money market funds' liquidity to investors and the Commission. This in turn could assist investors in analyzing the risks associated with particular funds, which could increase allocative efficiency and could positively affect competition by permitting investors to choose whether to invest in certain funds based on this information. However, if investors were to move their assets among money market funds or decide to invest in investment products other than money market funds as a

[636] *See* FSOC Proposed Recommendations, *supra* note 114 (''There is a risk that more frequent reporting of portfolio information may make investors quicker to redeem when these indicators show signs of deterioration. In addition, more frequent reporting of portfolio information such as daily mark-to-market per share values or liquidity levels could increase the volatility of MMFs' flows, even when the funds are not under stress, if investors are highly sensitive to changes in those levels.'').

[637] *See id.*

[638] *See infra* note 769 and accompanying text.

[639] *See* rule 2a–7(c)(12).

[640] *See infra* section III.F.4.

[641] *See supra* note 626 and accompanying text for a discussion of the reasons that the Commission staff has not measured the quantitative benefits of these proposed requirements at this time.

result of the proposed disclosure requirements, this could adversely affect the competitive stance of certain money market funds, or the money market fund industry generally.

The proposed requirements could also have effects on capital formation. The required disclosure could assist the Commission in overseeing money market funds and developing regulatory policy affecting the money market fund industry, which might affect capital formation positively if the resulting regulatory framework more efficiently or more effectively encouraged investors to invest in money market funds. The proposed requirements also may impose external market discipline on portfolio managers, which in turn could create market stability and enhance capital formation, if the resulting market stability encouraged more investors to invest in money market funds. However, the proposed requirements could detract from capital formation by decreasing market stability if investors became quicker to redeem during times of stress as a result of the proposed disclosure requirements. Accordingly, we do not have the information necessary to provide a reasonable estimate the effects of these proposed requirements on capital formation.

Costs associated with these disclosure requirements include initial, one-time costs, as well as ongoing costs. Initial costs include the costs to design the schedule, chart, graph, or other depiction showing historical liquidity information in a manner that clearly communicates the required information and to make the necessary software programming changes to the fund's Web site to present the depiction in a manner that can be updated each business day. We estimate that the average one-time costs for each money market fund to design and present the historical depiction of daily liquid assets and weekly liquid assets would be $20,150.[642] Funds also would incur ongoing costs to update the depiction of daily liquid assets and weekly liquid assets each business day. We estimate that the average ongoing annual costs that each fund would incur to update the required disclosure would be $9,184.[643] Because money market funds currently must calculate the percentage of their assets that are invested in daily liquid assets and weekly liquid assets each day for purposes of compliance with the portfolio liquidity provisions of rule 2a–7, funds should incur no additional costs in obtaining this data for purposes of the proposed disclosure requirements.

We request comment on this economic analysis:

- Are any of the proposed disclosure requirements unduly burdensome, or would they impose any unnecessary costs?
- We request comment on the staff's estimates of the operational costs associated with the proposed disclosure requirements.
- We request comment on our analysis of potential effects of these proposed disclosure requirements on efficiency, competition, and capital formation.

3. Daily Web site Disclosure of Current NAV per Share

a. Proposed Disclosure Requirements

We are proposing amendments to rule 2a–7 that would require each money market fund to disclose daily, prominently on its Web site, the fund's current NAV per share, rounded to the fourth decimal place in the case of a fund with a $1.0000 share price of an equivalent level of accuracy for funds with a different share price[644] (the fund's ''current NAV'') as of the end of the previous business day.[645] The proposed amendments would require a fund to maintain a schedule, chart, graph, or other depiction on its Web site showing historical information about its daily current NAV per share for the previous 6 months, and would require the fund to update this historical information each business day as of the end of the preceding business day.[646]

If we were to adopt the floating NAV alternative, the proposed amendments would effectively require a money market fund to publish historical information about the sale and redemption price of its shares each business day as of the end of each preceding business day.[647] The proposed amendments would require a government money market fund or retail money market fund (which generally would be permitted to transact at stable price per share), on the other hand, to publish historical information about its market-based current NAV per share, rounded to the fourth decimal place in the case of funds with a $1.0000 share price or an equivalent level of accuracy for funds with a different share price, each business day as of the end of each preceding business day. Likewise, if we were to adopt the liquidity fees and gates alternative, the proposed amendments would require all money market funds to publish historical information about the fund's market-based current NAV per share each business day as of the end of each preceding business day.[648] The proposed amendments would complement the current requirement for a money market fund to disclose its shadow price monthly on Form N–MFP.[649]

Whether we adopt either of the proposed reform alternatives, we believe that daily disclosure of money market funds' current NAV per share would increase money market funds' transparency and permit investors to better understand money market funds' risks.[650] While Form N–MFP information about money market funds' month-end shadow prices is currently publicly available with a 60-day lag,[651] the proposed amendments would permit shareholders to reference funds' current NAV per share in near real time to assess the effect of market events on their portfolios.[652] Public disclosure of money market funds' daily current NAV per share also could decrease funds' susceptibility to runs, as shareholders might be less likely to sell fund shares during the occurrence of negative market events if they could ascertain that their investment was not affected by such events on a near real-time basis.[653] Requiring daily disclosure of

[642] Staff estimates that these costs would be attributable to project assessment (associated with designing and presenting the historical depiction of daily liquid assets and weekly liquid assets), as well as project development, implementation, and testing. *See supra* note 245 (discussing the bases of our staff's estimates of operational and related costs). The costs associated with these activities are all paperwork-related costs and are discussed in more detail in *infra* section IV. *See infra* section IV.A.1.f.

[643] *See id.*

[644] *E.g.,* $10.000 or $100.00 per share.

[645] *See* proposed (FNAV) rule 2a–7(h)(10)(iii); proposed (Fees & Gates) rule 2a–7(h)(10)(iii).

[646] *Id.*

[647] *See* proposed (FNAV) rule 2a–7(h)(10)(iii); 17 CFR 270.22c–1.

[648] *See* proposed (Fees & Gates) rule 2a–7(h)(10)(iii). The proposed amendments under the liquidity fees and gates alternative also would require money market funds to calculate their market-based NAV at least once each business day. *See infra* section III.F.5.

[649] *See* Form N–MFP, Item 18. *But see* proposed Form N–MFP Item A.20 and B.5 (requiring money market funds to provide net asset value per share data as of the close of business on each Friday during the month reported).

[650] *See supra* note 167 and accompanying text (discussing the extent to which investors treat money market funds as essentially risk-free).

[651] We are proposing to eliminate the 60-day delay in making Form N–MFP information publicly available. *See infra* section III.H.4.

[652] *See* Comment Letter of Capital Advisors Group, Inc. (Feb. 1, 2013) (available in File No. FSOC–2012–0003) (''Capital Advisors Group FSOC Comment Letter'').

[653] *See id. But see* Federated Investors Feb. 15 FSOC Comment Letter, *supra* note 192 (noting that enhanced disclosure requirements ''may have unintended consequences that should also be weighed.''); Larry G. Locke, Ethan Mitra, and

Continued

money market funds' current NAV per share also could prevent month-end ''window dressing.'' [654] This enhanced disclosure also could impose external market discipline on portfolio managers consistent with their investment objective, as well as the stability of short-term financing markets generally.[655] However, the proposed disclosure could also change behavior, in that it could make shareholders quicker to redeem shares if they believe a decrease in the fund's current NAV signals portfolio deterioration or foreshadows other problems.[656] The proposed disclosure also could increase the volatility of a fund's flows, even during times when the fund is not under stress, if shareholders are sensitive to changes in the fund's current NAV.[657]

Although current and prospective shareholders may presently obtain historical information about money market funds' month-end shadow prices on Form N–MFP, we believe that requiring a six-month record of the fund's daily current NAV on the fund's Web site would permit shareholders to access more detailed information in a more convenient manner than comparing monthly Form N–MFP filings. We believe that investors should be able to compare recent NAV information with previous information from which they (or others analyzing the data) may discern trends. Because money market funds are presently required to maintain a six-month record of portfolio holdings on the fund Web site,[658] requiring a fund to post its daily current NAV for the same period would permit investors to analyze any relationship between the fund's portfolio holdings and its daily current NAV over time.

There has been a significant amount of industry support for the more frequent disclosure of money market funds' current NAV per share. In January and February of 2013, a number of money market fund sponsors of large funds began voluntarily disclosing their funds' daily current NAV per share, calculated using available market quotations.[659] Additionally, industry groups have advocated for more frequent public disclosure of money market funds' current NAV per share.[660] We request comment on the proposed amendments to rule 2a–7 that would require money market funds to disclose the fund's daily market-based NAV per share on the fund Web site:

- Would daily disclosure of money market funds' current NAV per share be useful to assist shareholders in increasing money market funds' transparency and better understanding money market funds' risks? Would the proposed amendments promote the goals of enhancing transparency and encouraging fund managers to manage portfolios in a manner that increases stability in the short-term financing markets? Would the daily disclosure of market prices encourage funds to invest in easier-to-price securities or less volatile securities? How, if at all, would the effects of the proposed disclosure requirement differ for stable price funds (which would be required to disclose their market-based current NAV per share) and floating NAV funds (which would be required to disclose the sale and redemption price of their shares)?
- How, if at all, have shareholders responded to the monthly disclosure of funds' current NAV per share, as required by the 2010 amendments? Would shareholders respond differently to the proposed daily disclosure than they have to historical monthly disclosure?
- Should information regarding money market funds' current NAV per share be required to be posted to a fund's Web site less frequently than the proposed amendments would require? Should funds be required to maintain this information on their Web sites for a period of more or less than 6 months?
- As proposed, should we require this information to be posted ''prominently'' on the fund's Web site? Should we provide any other instruction as to the presentation of this information, in order to highlight the information and/or lead investors efficiently to the information, for example, should we require that the information be posted on the fund's home page or be accessible in no more than two clicks from the fund's home page?
- How would the requirement for money market funds to disclose their current NAV per share daily affect the behavior of fund shareholders and/or the market as a whole? For instance, could this disclosure make shareholders quicker to redeem shares upon a decrease in current NAV, or generally increase the volatility of a fund's flows?

b. Economic Analysis

The qualitative benefits and costs of the proposed requirements regarding daily disclosure of a money market fund's current NAV per share are discussed above.[661] We believe that the proposed requirements' effects on efficiency, competition, and capital formation would likely be similar to the effects of the proposed daily disclosure requirements regarding funds' daily liquid assets and weekly liquid assets, discussed above.[662] We believe that the proposed requirements could increase informational efficiency by providing greater information about money market funds' daily current per-share NAV to investors and the Commission. This in turn could assist investors in analyzing the risks associated with particular funds, which could increase allocative efficiency and could positively affect competition by permitting investors to choose whether to invest in certain funds based on this information. However, if investors move their assets among money market funds or decide to invest in investment products other than money market funds as a result of the proposed disclosure requirements, this could adversely affect the competitive stance of certain money market funds, or the money market fund industry generally.

The proposed requirements could also have effects on capital formation. On one hand, the proposed requirements may impose external market discipline on portfolio managers, which in turn could create market stability and enhance capital formation, if the resulting market stability encouraged more investors to invest in money market funds. On the other hand, the proposed requirements could detract from capital formation by decreasing market stability if investors became quicker to redeem during times of stress as a result of the proposed disclosure

Virginia Locke, *Harnessing Whales: The Role of Shadow Price Disclosure in Money Market Mutual Fund Report,* 11 J. Bus. & Econ. Res. 4 (2013) (asserting that, under the current Form N–MFP shadow price disclosure regime, there is no statistical correlation between the shadow price of money market funds and their investment activity, but that the effects on shareholder behavior of increased transparency and frequency of fund information reporting are hard to predict).

[654] *See* Capital Advisors Group FSOC Comment Letter, *supra* note 652.

[655] *See* ICI Jan. 24 FSOC Comment Letter, *supra* note 25 (maintaining that prime money market funds should be required to make frequent public disclosure (via their Web sites) of their market-based share price to ''enhance transparency and encourage a highly conservative approach to portfolio management'').

[656] *See* FSOC Proposed Recommendations, *supra* note 114 at 60.

[657] *See id.*

[658] *See* rule 2a–7(c)(12).

[659] A number of large fund complexes have begun (or plan) to disclose daily money market fund market valuations (*i.e.,* shadow prices), including BlackRock, Charles Schwab, Federated Investors, Fidelity Investments, Goldman Sachs, J.P. Morgan, Reich & Tang, and State Street Global Advisors. *See, e.g., Money Funds' New Openness Unlikely to Stop Regulation,* Wall St. J. (Jan. 30, 2013).

[660] *See e.g.,* ICI Jan. 24 FSOC Comment Letter, *supra* note 25; SIFMA FSOC Comment Letter, *supra* note 358, at 11.

[661] *See supra* note 626 and accompanying text for a discussion of the reasons that the Commission staff has not measured the quantitative benefits of these proposed requirements at this time.

[662] *See supra* section III.F.2.

requirements. Accordingly, we do not have the information necessary to provide a reasonable estimate of the effects of these proposed requirements on capital formation.

Costs associated with these disclosure requirements include initial, one-time costs, as well as ongoing costs.[663] Initial costs include the costs to design the schedule, chart, graph, or other depiction showing historical NAV information in a manner that clearly communicates the required information and to make the necessary software programming changes to the fund's Web site to present the depiction in a manner that will be able to be updated each business day. We estimate that the average one-time costs for each money market fund to design and present the fund's daily current NAV would be $20,150.[664] Funds also would incur ongoing costs to update the depiction of the fund's current NAV each business day. We estimate that the average ongoing annual costs that each fund would incur to update the required disclosure would be $9,184.[665] Because floating NAV money market funds would be required to calculate their sale and redemption price each day, these funds should incur no additional costs in obtaining this data for purposes of the proposed disclosure requirements. Stable price money market funds (including government money market funds and retail funds if we adopt the floating NAV proposal, and all funds if we adopt the liquidity fees and gates proposal), which would be required to calculate their current NAV per share daily pursuant to proposed amendments to rule 2a–7, likewise should incur no additional costs in obtaining this data for purposes of the proposed disclosure requirements.[666]

We request comment on this economic analysis:

- Are any of the proposed disclosure requirements unduly burdensome, or would they impose any unnecessary costs?
- We request comment on the staff's estimates of the operational costs associated with the proposed disclosure requirements.
- We request comment on our analysis of potential effects of these proposed disclosure requirements on efficiency, competition, and capital formation.

4. Disclosure of Portfolio Holdings

a. Harmonization of Rule 2a–7 and Form N–MFP Portfolio Holdings Disclosure Requirements

Money market funds are currently required to file information about the fund's portfolio holdings on Form N–MFP within five business days after the end of each month, and to disclose much of the portfolio holdings information that Form N–MFP requires on the fund's Web site each month with 60-day delay.[667] We are proposing amendments to rule 2a–7 in order to harmonize the specific portfolio holdings information that rule 2a–7 currently requires funds to disclose on the fund's Web site with the corresponding portfolio holdings information proposed to be reported on Form N–MFP pursuant to proposed amendments to Form N–MFP. We believe that these proposed amendments would benefit money market fund investors by providing additional, and more precise, information about portfolio holdings information, which could allow investors better to evaluate the current risks of the fund's portfolio investments. Specifically, we are proposing amendments to the categories of portfolio investments reported on Form N–MFP, and are therefore also proposing amendments to the categories of portfolio investments currently required to be reported on a money market fund's Web site.[668] We are also proposing an amendment to Form N–MFP that would require funds to report the maturity date for each portfolio security using the maturity date used to calculate the dollar-weighted average life maturity, and therefore we are also proposing amendments to the current Web site disclosure requirements regarding portfolio securities' maturity dates.[669] In addition, we are proposing amendments to the current requirement for funds to disclose the ''amortized cost value'' of each portfolio security to reflect the fact that funds under each proposal would no longer be permitted to use the amortized cost method to value portfolio securities.[670] Currently, we do not require funds to disclose the market-based value of portfolio securities on the fund's Web site, because doing so would disclose this information prior to the time the information becomes public on Form N–MFP (on account of the current 60-day delay before Form N–MFP information becomes publicly available). Because we propose to remove this 60-day delay, we are also proposing that funds make the market-based value of their portfolio securities available on the fund Web site at the same time that this information becomes public on Form N–MFP.[671]

Because the new information that a fund would be required to present on its Web site overlaps with the information that a fund would be required to disclose on Form N–MFP, we anticipate that the costs a fund will incur to draft and finalize the disclosure that will appear in its Web site will largely be incurred when the fund files Form N–MFP, as discussed below in section III.H.6. In addition, we estimate that a fund would incur annual costs of $2,484 associated with updating its Web site to include the required monthly disclosure.[672]

- We request comment on the Web site disclosure that we propose to harmonize with the disclosure proposed to be reported on Form N–MFP. Should any of the information that is proposed to be reported on Form N–MFP, and that we propose to require funds to disclose on the fund's Web site, not be required to appear on the fund's Web site?
- We request comment on the staff's estimates of the operational costs associated with the proposed disclosure requirements.

b. Request for Comment About Additional Web Site Disclosure on Portfolio Holdings

Because certain money market funds have high portfolio turnover rates, the monthly disclosure requirement described above may not permit fund investors to fully understand a fund's portfolio composition and its attendant

[663] As discussed above, some money market funds presently publicize their current NAV per share daily on the fund's Web site. The staff expects these funds to incur few, if any, additional costs to comply with these proposed disclose requirements.

[664] Staff estimates that these costs would be attributable to project assessment (associated with designing and presenting the historical depiction of the fund's daily current NAV per share), as well as project development, implementation, and testing. *See supra* note 245 (discussing the bases of our staff's estimates of operational and related costs). The costs associated with these activities are all paperwork-related costs and are discussed in more detail in *infra* sections IV.A.1.f and IV.B.1.f.

[665] *Id.*

[666] *See infra* section III.F.5 (discussing the proposed requirement for stable price money market funds to calculate their current NAV per share daily, as well as the operational costs associated with this proposed daily calculation requirement).

[667] *See* rule 2a–7(c)(12)(ii); rule 30b1–7; Form N–MFP, General Instruction A.

[668] *See* proposed (FNAV and Fees & Gates) rule 2a–7(h)(10)(i)(B); proposed Form N–MFP, Item C.6.

[669] *See* proposed (FNAV and Fees & Gates) rule 2a–7(h)(10)(i)(B); proposed Form N–MFP, Item C.12.

[670] *See* proposed (FNAV and Fees & Gates) rule 2a–7(h)(10)(i)(B).

[671] *See* proposed (Fees & Gates) rule 2a 7(h)(10)(i)(B).

[672] The costs associated with updating the fund's Web site are paperwork-related costs and are discussed in *infra* section IV.A.1.f.i.

risks.[673] For this reason, during times of stress, uncertainty regarding portfolio composition could increase investors' incentives to redeem in between reporting periods, as they would not be able to determine if their fund is exposed to certain stressed assets.[674]

We are considering whether to require more frequent disclosure of money market funds' portfolio holdings on a fund's Web site, including the market value of individual portfolio securities.[675] Increasing the frequency of such disclosure might provide greater transparency to investors and the Commission regarding the risks of the investments held by money market funds. More frequent portfolio holdings disclosure also could assist investors, particularly during times of stress, in differentiating between money market funds based on the quality and stability of their investments, potentially limiting the incentive to run.[676] In addition, requiring money market funds to disclose their portfolio holdings more frequently may impose external market discipline on portfolio managers consistent with their investment objective.[677]

On the other hand, more frequent disclosure of portfolio holdings could make investors quicker to redeem when these holdings show signs of deterioration, and also could encourage money market funds to use less differentiated investment strategies.[678] More frequent disclosure of portfolio holdings also might lead to ''front running'' of the portfolio, where other investors could trade ahead of money market fund purchasers, or ''free riding,'' where other investors mirror the investment strategies of the money market fund. In past years, some fund complexes have begun disclosing money market fund portfolio holdings weekly and daily on their Web sites, citing shareholder demand as the impetus for this disclosure.[679]

We request comment on whether we should require money market funds to disclose portfolio holdings via their Web site more frequently than monthly.

- Would more frequent disclosure of money market funds' portfolio holdings be useful to assist shareholders in assessing a fund's risk? Would more frequent disclosure promote the goals of enhancing transparency, permitting shareholders to differentiate between money market funds, and encouraging fund managers to manage portfolios in a manner that increases stability in the short-term financing markets? How, if at all, would more frequent disclosure of portfolio holdings affect the portfolio assets that a money market fund's investment adviser purchases on behalf of the fund?
- What type of investors would be most likely to benefit from more frequent disclosure of money market funds' portfolio holdings? Would this disclosure allow more attentive investors to disadvantage less attentive investors?
- If more frequent disclosure of money market funds' portfolio holdings would be useful, how frequently should such disclosure be required? Daily? Weekly?
- During the 2007–2008 financial crisis, some funds voluntarily chose to disclose portfolio information more frequently than usual, while other funds did not change their disclosure practices. How and why did funds make these decisions, and how did investors respond? How would the benefits and costs of disclosure be affected by moving from a voluntary system to a mandated system? What would be the benefits of retaining a voluntary system? Would investors view voluntary disclosure as a signal regarding the level of transparency of a fund?
- Should any requirement for more frequent disclosure of portfolio holdings be limited to a certain type or types of money market fund (*e.g.,* prime money market funds, which have historically been more prone to heavy redemptions during times of market stress than other kinds of money market funds)?[680]
- How would more frequent disclosure of money market funds' portfolio holdings affect the behavior of fund shareholders and/or the market as a whole? For instance, would this disclosure increase or decrease funds' susceptibility to runs, affect money market funds' ability to use differentiated investment strategies, or lead to ''front running'' or ''free riding''?
- If we were to require more frequent Web site disclosure of money market funds' portfolio holdings, should we also require more frequent filing of Form N–MFP (which includes certain portfolio information that we do not currently require, and do not currently propose to require, funds to disclose on their Web sites) with the Commission? If so, should we require Form N–MFP to be filed as frequently as we require Web site disclosure of portfolio holdings? What impact would this have, if any, on analysts who use Form N–MFP data?

5. Daily Calculation of Current NAV per Share Under the Liquidity Fees and Gates Proposal

a. Proposed Daily NAV Calculation Requirement for Stable Price Funds

We are proposing amendments to rule 2a–7 that would require stable price funds (including government and retail funds under the floating NAV proposal, and all funds under the fees and gates proposal) to calculate the fund's current NAV per share based on current market factors at least once each business day.[681] Rule 2a–7 currently requires money market funds to calculate the fund's NAV per share, using available market quotations (or an appropriate substitute that reflects current market conditions), at such intervals as the board of directors determines appropriate and reasonable in light of current market conditions.[682] We believe that daily disclosure of money market funds' current NAV per share

[673] *See* Federal Reserve Bank Presidents FSOC Comment Letter, *supra* note 38 (noting that as of month end November 2012, prime funds turned over on average 44% of portfolio assets every week).

[674] *See id.*

[675] We also request comment on whether we should require more frequent filing of Form N–MFP, which would result in more frequent disclosure of portfolio holdings on Form N–MFP, in *infra* section III.H.5.

[676] *See* FSOC Proposed Recommendations, *supra* note 114, at 60.

[677] *See supra* notes 654 and 655 and accompanying text. *See also* RSFI Study, *supra* note 21, at 38 (noting that increased transparency of portfolio holdings ''might dampen a fund manager's willingness to hold securities whose ratings are at odds with the underlying risk, especially at times when credit conditions are deteriorating'').

[678] *See* FSOC Proposed Recommendations, *supra* note 114, at 61.

[679] *See, e.g.,* Dreyfus FSOC Comment Letter, *supra* note 174 (''We decided to disclose portfolio holdings daily for client-servicing purposes to facilitate due diligence inquiries from fund shareholders on portfolio composition issues on a real-time basis in a manner consistent with applicable law. Institutional investors in particular are keenly aware of risk of loss in their money market fund investments. As part of their due diligence, they regularly analyze Dreyfus fund portfolio holdings for credit, issuer, liquidity, and counterparty concerns, among others.''); Colleen Sullivan & Mike Schnitzel, Money Funds Move to Update Holdings Faster, FUND ACTION, Sept. 29, 2008, *available at http://www.fundaction.com/pdf/FA092908.pdf* (noting that American Beacon Funds, Fidelity Investments, Evergreen Investments, Oppenheimer Funds, and Sentinel Investments provide money market fund portfolio holdings information more frequently than monthly, for reasons related to investor demand).

In addition, such Web site disclosures would also address issues related to selective disclosure of portfolio holdings. *See Disclosure Regarding Market Timing and Selective Disclosure of Portfolio Holdings,* Securities Act Release No. 33–8408 (Apr. 19, 2004) [69 FR 22300 (Apr. 23, 2004)] at section II.C.

[680] *See supra* notes 79–89 and accompanying text.

[681] *See* proposed (FNAV and Fees & Gates) rule 2a–7(h)(10)(iii); *see also* text accompanying *supra* notes 644 and 645 for definition of ''current NAV.''

[682] Rule 2a–7(c)(8)(ii). Item 18 of Form N–MFP currently requires a fund to disclose its market-based NAV monthly.

would increase money market funds' transparency and permit investors to better understand money market funds' risks, and thus we propose amendments to rule 2a–7 that would require this proposed disclosure.[683] Because we are proposing to require money market funds to disclose their current NAV daily on the fund Web site, we correspondingly are proposing to amend rule 2a–7 to require funds to make this calculation on a daily basis, rather than at the board's discretion.[684] Many money market funds already calculate and disclose their current NAV on a daily basis, and thus we do not expect that requiring all money market funds to perform a daily calculation should entail significant additional costs.[685]

We request comments on the proposed amendments to rule 2a–7 that would require money market funds to calculate their current NAV daily if the we were to adopt the liquidity fees and gates alternative.

• Would the proposed daily calculation requirement affect what assets a money market fund purchases? For example, would the requirement make funds less willing to invest in assets that are more difficult to value, or in more volatile assets?

• Rule 2a–7 currently requires a money market fund's board of directors to review the amount of deviation between the fund's market-based NAV per share and the fund's amortized cost per share ''periodically.'' [686] If we require a money market fund to calculate its current NAV daily, should we also require the fund's board to review the deviation between the current NAV per share and the fund's intended stable price per share at a specified interval? If so, what would be an appropriate interval? Weekly? Monthly? Quarterly?

b. Economic Analysis

The qualitative benefits and costs of the proposed requirement for money market funds to calculate the fund's current NAV per share daily are discussed above.[687] We believe that this proposed requirement may positively affect competition, in that it would require all money market funds to calculate their daily current per-share NAV. Presently, some funds but not others calculate their current NAV per share daily, and therefore the proposed requirement would help level the associated costs incurred by all money market funds and neutralize any competitive advantage associated with determining not to calculate daily current per-share NAV. We believe that the effects on efficiency and capital formation of calculating the fund's current NAV daily cannot be separated from the effects of disclosing money market funds' current NAV per share daily, which are discussed above.

The costs associated with this proposed requirement include the costs for funds to determine the current values of their portfolio securities each day. We estimate that 25% of active money market funds, or 147 funds, will incur new costs to comply with this requirement.[688] However, the proposed requirement will result in no additional costs for those money market funds that presently determine their current NAV per share daily on a voluntary basis.[689]

All money market funds are presently required to disclose their market-based NAV per share monthly on Form N–MFP, and if the proposed amendments to Form N–MFP are adopted, the frequency of this disclosure would increase to weekly.[690] As discussed below, some money market funds license a software solution from a third party that is used to assist the funds to prepare and file the information that Form N–MFP requires, and some funds retain the services of a third party to provide data aggregation and validation services as part of preparing and filing of reports on Form N–MFP on behalf of the fund.[691] We expect, based on conversations with industry representatives, that money market funds that do not presently calculate the current values of their portfolio securities each day would generally use the same software or service providers to calculate the fund's current NAV per share daily that they presently use to prepare and file Form N–MFP, and for these funds, the associated base costs of using this software or these service providers should not be considered new costs. However, the third-party software suppliers or service providers may charge more to funds to calculate a fund's current NAV per share daily, which costs would be passed on to the fund. While we do not have the information necessary to provide a point estimate (as they depend on a variety of factors, including discounts relating to volume and economies of scale, which pricing services may provide to certain funds), we estimate that the average additional annual costs that a fund would incur associated with calculating its current NAV daily would range from $6,111 to $24,444.[692] Assuming, as discussed above, that 147 money market funds do not presently determine and publish their current NAV per share daily, the average additional annual cost that these 147 funds will collectively incur would range from $898,317 to $3,593,268.[693] These costs could be less than our estimates if funds were to receive significant discounts based on economies of scale or the volume of securities being priced.

We request comment on this economic analysis:

• Are any of the proposed requirements unduly burdensome, or would they impose any unnecessary costs?

• We request comment on the staff's estimates of the operational costs

[683] *See supra* section III.F.3.

[684] If we were to adopt the floating NAV alternative, money market funds would be required to calculate a potentially fluctuating sale and redemption price daily, and therefore, under the floating NAV alternative, we do not propose to amend rule 2a–7 in order to require daily market-based NAV calculations.

[685] The costs for those funds that do not already calculate and disclose their market-based NAV on a daily basis are discussed in detail below. *See infra* notes 689–693 and accompanying text.

[686] Rule 2a–7(c)(8)(ii)(A)(2). The proposed amendments to rule 2a–7 do not include this requirement, as money market funds under each proposal generally would no longer be able to use amortized cost valuation for their portfolio holdings. *See supra* notes 140, 177, 182, and 328 and accompanying text.

[687] *See supra* note 626 and accompanying text for a discussion of the reasons that the Commission staff has not measured the quantitative benefits of these proposed requirements at this time.

[688] Commission staff estimates that there are currently 586 active money market funds. This estimate is based on a staff review of reports on Form N–MFP filed with the Commission for the month ended February 28, 2013. 586 money market funds × 25% = 147 money market funds.

[689] Based on our understanding of money market fund valuation practices, we estimate that 75% of active money market funds presently determine their current NAV daily.

[690] *See* proposed Form N–MFP Item A.21 and B.5 (requiring money market funds to provide net asset value per share data as of the close of business on each Friday during the month reported).

[691] *See infra* sections III.H.6, IV.A.3 and IV.B.3.

[692] We estimate, based on discussions with industry representatives, that obtaining the price of a portfolio security would range from $0.25–$1.00 per CUSIP number per quote. We estimate that each money market fund's portfolio consists of, on average, securities representing 97 CUSIP numbers. Therefore, the additional daily costs to calculate a fund's market-based NAV per share would range from $24.25 ($0.25 × 97]) to $97.00 ($1.00 × 97). The additional annual costs would therefore range from $6,111 (252 business days in a year × $24.25) to $24,444 (252 business days in a year × $97.00).

[693] This estimate is based on the following calculations: low range of $6,111 × 147 funds = $898,317; high range of $24,444 × 147 funds = $3,593,268. *See supra* note 692. This figure likely overestimates the costs that stable price funds would incur if the floating NAV proposal were adopted. This is because fewer than 586 active money market funds would be stable price funds required to calculate their current NAV per share daily, and thus the estimate of 147 funds (25% × 586 active funds) that would be required to comply with this requirement is likely overinclusive. Under the floating NAV proposal, floating NAV funds would calculate their shares' purchase and sale price daily, but the costs associated with this calculation are included in the costs discussed above at section III.A.7.

associated with the proposed disclosure requirements. In particular, we request comment on our assumption that money market funds would generally use the same software or service providers to calculate the fund's current NAV per share daily that they presently use to prepare and file Form N–MFP.

• We request comment on our analysis of potential effects of these proposed requirements on efficiency, competition, and capital formation.

6. Money Market Fund Confirmation Statements

Rule 10b–10 under the Securities Exchange Act of 1934 (the ''Confirmation Rule'') addresses broker-dealers' obligations to confirm their customers' securities transactions. The rule provides an exception for transactions in money market funds that attempt to maintain a stable net asset value and where no sales load or redemption fee is charged.[694] The rule permits a broker-dealer to provide transaction information to fund shareholders on a monthly basis in lieu of individual, immediate confirmations for all purchases and redemptions of shares of these money market funds.

The floating NAV proposal, if adopted, would negate applicable exemptions that have historically permitted money market funds to maintain a stable net asset value. Instead, money market funds, like other mutual funds, would sell and redeem shares at prices that reflect the current market values of their portfolio securities. Given the likelihood that share prices of money market funds that are not exempt from the floating NAV proposal will fluctuate, broker-dealers may not be permitted under the Confirmation Rule to provide money market fund shareholders transaction information on a monthly basis.[695]

The Confirmation Rule was designed to provide customers with the relevant information relating to their investment decisions at or before the completion of a transaction. The Confirmation Rule exception was adopted because the Commission believed that in cases where funds maintain a constant net asset value per share and no load is charged, monthly statements were adequate to ensure investor protection due to the stable pricing of the fund shares.[696] However, for transactions in a floating NAV fund, investors would not know relevant information about the costs of transacting in fund shares before, or at the time of, the transaction. Because of the floating NAV, investors may desire to obtain more immediate confirmations for all purchases and redemptions to obtain better price transparency at or before the completion of a transaction. We request comment on whether, if we adopt the floating NAV requirement, we should leave the Confirmation Rule unchanged, which would have the effect of requiring broker-dealers to provide fund investors immediate confirmations of their transactions.

• Should broker-dealers be required to provide immediate confirmations to shareholders of funds with a floating NAV, or should broker-dealers be permitted to continue to provide confirmations for these transactions on a monthly basis? What are the advantages and disadvantages of requiring broker-dealers to provide fund shareholders with immediate confirmations of transactions in floating NAV money market funds rather than monthly confirmations?

• If a floating NAV were implemented, what are the reasons why shareholders might prefer to receive this information immediately? Are there any additional costs to broker-dealers associated with providing immediate confirmations? If so, what are the nature and magnitude of such costs? Should the Commission consider alternative exceptions to the Confirmation Rule in the context of a floating NAV, such as permitting confirmations to be provided to shareholders for some different time period (*e.g.,* weekly statements)? What benefits and costs would be associated with any alternative approach?

• How, if at all, do the proposed amendments that require money market funds to disclose daily market-based NAV per share affect the need for immediate confirmations?

*G. New Form N–CR*

We are proposing a new rule that would require money market funds to file new Form N–CR with the Commission when certain events occur.[697] The information reported on Form N–CR would include instances of portfolio security default, sponsor support of funds, and other similar significant events. We believe that this information would enable the Commission to enhance its oversight of money market funds and its ability to respond to market events. It would also provide investors with better and more timely disclosure of potentially important events. The Commission would be able to use the information provided on Form N–CR in its regulatory, disclosure review, inspection, and policymaking roles. Like Form 8–K under the Exchange Act,[698] Form N–CR would require disclosure, by means of a current report filed with the Commission, related to specific reportable events. A report on Form N–CR would be made public on the Commission's Electronic Data Gathering, Analysis, and Retrieval system (''EDGAR'') immediately upon filing. We would require reporting on Form N–CR under both of the reform alternatives we are proposing today, but the Form would differ in certain respects depending on the alternative that we adopt.

1. Proposed Disclosure Requirements Under Both Reform Alternatives

Under both the floating NAV alternative and the liquidity fees and gates alternative, we are proposing to require that money market funds file a current report on new Form N–CR within a specified period of time after the occurrence of certain events.[699] Under each proposed alternative, we would require a money market fund to file a report on Form N–CR if the issuer of one or more of the fund's portfolio securities, or the issuer of a demand feature or guarantee, experiences a default or event of insolvency[700] (other

[694] *See* Exchange Act rule 10b–10(b).

[695] Our proposal includes exemptions from the floating NAV requirement for government and retail money market funds, which would permit these funds to continue to maintain a stable price per share. *See supra* sections III.A.3 and III.A.4. Accordingly, for investor transactions in such exempt funds, broker-dealers would still be able to take advantage of the exception in the Confirmation Rule and send monthly transaction reports.

[696] The Commission's adopting release extending the confirmation delivery requirement exception noted that ''where shares are priced at a constant net asset value per share and no load is charged, the need for investors to receive immediate confirmations does not appear to outweigh the cost to broker-dealers of providing the confirmation.'' *See* Exchange Act Release 34–19887 (Apr. 18, 1983); [48 FR 17585 (Apr. 25, 1983)], at section II.1.

[697] Proposed rule 30b1–8.

[698] 17 CFR 249.308.

[699] Proposed (FNAV) Form N–CR General Instructions; proposed (Fees & Gates) Form N–CR General Instructions. Proposed Form N–CR would also require a fund to report the following general information: (i) the date of the report; (ii) the registrant's central index key (''CIK'') number; (iii) the EDGAR series identifier; (iv) the Securities Act file number; and (v) the name, email address, and telephone number of the person authorized to receive information and respond to questions about the filing. *See* proposed (FNAV) Form N–CR Part A; proposed (Fees & Gates) Form N–CR Part A. The name, email address, and telephone number of the person authorized to receive information and respond to questions about the filing would not be disclosed publicly on EDGAR.

[700] *See* 17 CFR 270.5b–3(c)(2) (defining ''event of insolvency'' as (i) an admission of insolvency, the application by the person for the appointment of a trustee, receiver, rehabilitator, or similar officer for all or substantially all of its assets, a general assignment for the benefit of creditors, the filing by the person of a voluntary petition in bankruptcy or application for reorganization or an arrangement with creditors; (ii) the institution of similar proceedings by another person which proceedings

than an immaterial default unrelated to the financial condition of the issuer), and immediately before the default or event of insolvency the portfolio security or securities (or the securities subject to the demand feature or guarantee) accounted for at least ½ of 1% of the fund's total assets.[701] Although rule 2a–7 currently requires money market funds to report defaults or events of insolvency to the Commission by email,[702] we believe that requiring funds to report these events on Form N–CR would provide important transparency to fund shareholders, and also would provide information more uniformly and efficiently to the Commission. Form N–CR would require funds to disclose certain information about these reportable events, including the nature and financial effect of the default or event of insolvency, as well as the security or securities affected.[703] The Commission believes that the factors specified in the required disclosure are all necessary to understand the nature and extent of the default, as well as the potential effect of the default on the fund's operations and its portfolio as a whole.

We would require funds to file a report on Form N–CR within one business day after the default or event of insolvency occurs, which time frame balances, we believe, the exigency of the report with the time it will reasonably take a fund to compile the required information.[704] The Commission and shareholders have a significant interest in receiving the information filed in response to Form N–CR Part B as soon as possible, as the default or event of insolvency required to be reported could signal circumstances that may require Commission action or analysis, and that may affect an investor's decision to purchase shares of the fund or remain invested in the fund.

Additionally, we believe that current reports of occasions on which a money market fund receives financial support from a sponsor or other fund affiliate would provide important transparency to shareholders and the Commission, and also could help shareholders better understand the ongoing risks associated with an investment in the fund.[705] Therefore, under each proposed reform alternative, we would require all money market funds to report all instances of sponsor support on proposed Form N–CR. Specifically, we propose to require money market funds to file Form N–CR if the fund's sponsor, or another affiliated person of the fund, provides any form of financial support to the fund.[706] The term ''financial support'' includes, but is not limited to, (i) any capital contribution, (ii) purchase of a security from the fund in reliance on rule 17a–9, (iii) purchase of any defaulted or devalued security at par, (iv) purchase of fund shares, (v) execution of letter of credit or letter of indemnity, (vi) capital support agreement (whether or not the fund ultimately received support), (vii) performance guarantee, or (viii) any other similar action to increase the value of the fund's portfolio or otherwise support the fund during times of stress.[707] Form N–CR would require funds receiving such financial support to disclose certain information about the support, including the nature, amount, and terms of the support, as well as the relationship between the person providing the support and the fund.[708] The Commission believes that factors specified in the required disclosure are necessary for investors to understand the nature and extent of the sponsor's discretionary support of the fund.[709] The Commission also believes that these factors are necessary for Commission staff to analyze the economic effects of financial support that money market funds receive from sponsors or other affiliated persons.

We would require funds to file a report on Form N–CR within one business day after a fund receives such financial support,[710] which time frame we believe balances the exigency of the report with the time it will reasonably take a fund to compile the required information. The Commission and shareholders have a significant interest in receiving the information filed in response to Form N–CR Part C as soon as possible, as the financial support required to be reported could signal circumstances that may require Commission action or analysis, and that may affect an investor's decision to purchase shares of the fund or remain invested in the fund.

Today, when a sponsor supports a fund by purchasing a security pursuant to rule 17a–9, we require prompt disclosure of the purchase by email to the Director of the Commission's Division of Investment Management, but we do not otherwise receive notice of such support unless the fund needs and requests no-action or other relief.[711] The proposed Form N–CR reporting requirement would permit the

are not contested by the person; or (iii) the institution of similar proceedings by a government agency responsible for regulating the activities of the person, whether or not contested by the person).

[701] *See* proposed (FNAV) Form N–CR Part B; proposed (Fees & Gates) Form N–CR Part B; *see also* rule 2a–7(c)(7)(iii)(A).

[702] *See* rule 2a–7(c)(7)(iii)(A). We propose to eliminate this requirement should proposed Form N–CR be adopted, as it would duplicate with the proposed Form N–CR reporting requirements discussed in this section.

[703] *See* proposed (FNAV) Form N–CR Part B; proposed (Fees & Gates) Form N–CR Part B. Proposed Form N–CR would require a fund to disclose the following information: (i) the security or securities affected; (ii) the date or dates on which the defaults or events of insolvency occurred; (iii) the value of the affected securities on the dates on which the defaults or events of insolvency occurred; (iv) the percentage of the fund's total assets represented by the affected security or securities; and (v) a brief description of the actions the fund plans to take in response to such event. *See id.*

An instrument subject to a demand feature or guarantee would not be deemed to be in default, and an event of insolvency with respect to the security would not be deemed to have occurred, if: (i) in the case of an instrument subject to a demand feature, the demand feature has been exercised and the fund has recovered either the principal amount or the amortized cost of the instrument, plus accrued interest; (ii) the provider of the guarantee is continuing, without protest, to make payments as due on the instrument; or (iii) the provider of a guarantee with respect to an unrated, first-tier asset-backed security, as defined by rule 2a–7, is continuing, without protest, to provide credit, liquidity, or other support as necessary to permit the asset-backed security to make payments as due. *See* Instruction to proposed (FNAV) Form N–CR Part B; Instruction to proposed (Fees & Gates) Form N–CR Part B. This instruction is based on the current definition of the term ''default'' in the provisions of rule 2a–7 that require funds to report defaults or events of insolvency to the Commission. *See* rule 2a–7(c)(7)(iv).

[704] *See* General Instruction A to proposed (FNAV) Form N–CR; general Instruction A to proposed (Fees & Gates) Form N–CR.

[705] *See supra* section III.F.1.b (discussing the potential benefits and costs of the proposed requirement for a money market fund to disclose on its Web site any present occasion on which the fund receives financial support from a sponsor or other fund affiliate).

[706] *See* proposed (FNAV) Form N–CR Part C; proposed (Fees & Gates) Form N–CR Part C.

[707] *See id.*

[708] *See id.* Proposed Form N–CR would require a fund to disclose the following information: (i) a description of the nature of the support; (ii) the person providing support; (iii) a brief description of the relationship between the person providing the support and the fund; (iv) a brief description of the reason for the support; (v) the date the support was provided; (vi) the amount of support; (vii) the security supported, if applicable; (viii) the market-based value of the security supported on the date support was initiated, if applicable; (ix) the term of support; and (x) a brief description of any contractual restrictions relating to support.

In addition, if an affiliated person, promoter, or principal underwriter of the fund, or an affiliated person of such a person, purchases a security from the fund in reliance on rule 17a–9, the money market fund would be required to provide the purchase price of the security, as well as certain other information. Instruction to proposed (FNAV) Form N–CR Part C; Instruction to proposed (Fees & Gates) Form N–CR Part C.

[709] *See supra* note 607.

[710] *See* General Instruction A to proposed (FNAV) Form N–CR; general Instruction A to proposed (Fees & Gates) Form N–CR.

[711] *See* rule 2a–7(c)(7)(iii)(B). We propose to eliminate this requirement should proposed Form N–CR be adopted, as it would duplicate with the proposed Form N–CR reporting requirements discussed in this section.

Commission additionally to receive notification of other kinds of financial support (which could affect a fund as significantly as a security purchase pursuant to rule 17a–9) and a description of the reason for the support, and it would also assist investors in understanding the extent to which money market funds receive financial support from their sponsors or other affiliates.[712]

Under either alternative proposal, we also would require funds that are permitted to transact at a stable price to file a report on proposed Form N–CR on the first business day after any day on which the fund's current NAV per share [713] (rounded to the fourth decimal place in the case of a fund with a $1.0000 share price, or an equivalent level of accuracy for funds with a different share price) deviates downward significantly from its intended stable price (generally, $1.00). We believe that this requirement to file a report for each day the fund's current NAV is low would not only permit the Commission and others to better monitor indicators of stress in specific funds or fund groups and in the industry, but also help increase money market funds' transparency and permit investors to better understand money market funds' risks.[714] We believe that a deviation of ¼ of 1 percent is sufficiently significant that it could signal future, further deviations in the fund's NAV that could require a stable price fund's board to consider re-pricing the fund's shares (among other actions).[715] To this end, if we adopt the floating NAV alternative, we would require only government or retail money market funds to file a report on Form N–CR if the fund's current NAV per share deviates downward from its intended stable price by more than ¼ of 1 percent.[716] If we adopt the liquidity fees and gates alternative, we would require all money market funds to file a report on Form N–CR if the fund's current NAV per share deviates downward from its intended stable price by more than ¼; of 1 percent.[717] The Commission believes that the factors specified in the required disclosure are all necessary to understanding the nature and extent of the deviation, as well as the potential effect of the deviation on the fund's operations.

We would require funds to file a report on Form N–CR within one business day following the reportable movement of the fund's current NAV, which time frame we believe balances the exigency of the report with the time it will reasonably take a fund to compile the required information.[718] The Commission and shareholders have a significant interest in receiving the information filed in response to Form N–CR Part D as soon as possible, as the NAV deviation required to be reported could signal circumstances that may require Commission action or analysis, and that may affect an investor's decision to purchase shares of the fund or remain invested in the fund.

We request comments on the proposed general disclosure requirements of new Form N–CR:

- Are there any other events that warrant a current report filing obligation for money market funds under either or both of the proposed reform alternatives? If so, what are they? Should we add any additional disclosure requirements to proposed Form N–CR? Should any proposed requirements not be included in Form N–CR?
- With respect to the proposed requirement for stable price money market funds to report certain deviations between the fund's current NAV and its intended stable price per share, is our proposed threshold of reporting (¼ of 1 percent deviation) appropriate? How frequently should we expect to receive reports based on this threshold? Which threshold would help the public differentiate funds that are having difficulties maintaining their stable price from those that are not? Should we adopt a lower threshold (such as 10 or 20 basis points) or a higher threshold (such as 30 or 40 basis points)? Why or why not? How would investors interpret and respond to this reporting threshold? Would it affect their purchase and redemption activity in the reporting fund or in other funds, and if so, how and why?
- Do the proposed reporting deadlines for each part appropriately balance the Commission's and the public's need for information on current events affecting money market funds with the costs of preparing and submitting a report on Form N–CR? Should we require a longer or shorter time frame in which to file a report on any of the parts of Form N–CR?
- Would the particular information that we propose requiring funds to report in response to Parts B, C, and D of Form N–CR be useful to shareholders in understanding the events triggering the filing of Form N–CR, as well as certain of the risks associated with an investment in the fund? Should we require any more, any less, or any other information to be reported?
- How frequently do commenters anticipate that funds would file Form N–CR to report a default or event of insolvency with respect to portfolio securities, the provision of financial support to the fund, or a significant deviation between the fund's current per-share NAV and its intended stable price? For how many consecutive days do commenters anticipate that funds would likely report low current NAVs? Under what conditions would these reports trigger investor redemptions? Under what conditions would these reports affect investor purchases?
- Which types of investors (or other parties) would be most likely to monitor Form N–CR filings in real time?
- Would the proposed requirement to file a report in response to Part C of Form N–CR make funds less likely to request sponsor support? Why or why not? How would this affect the sponsor's willingness to provide support?
- Would the requirement to file a report in response to Part D of Form N–CR make funds more likely to request sponsor support? Why or why not? How would this affect the sponsor's willingness to provide support?
- How would the requirement to file Form N–CR affect the fund's investment decisions? Would the reporting requirement make the fund more

[712] As discussed above, money market funds' receipt of financial support from sponsors and other affiliates has not historically been disclosed to investors, which has resulted in a lack of clarity among investors about which money market funds have received such financial support. *See supra* text following note 49.

[713] *See* text accompanying *supra* notes 644 and 645 for definition of ''current NAV.''

[714] *See generally supra* section III.F.3.b (discussing the potential benefits and costs of the proposed requirement for a money market fund to disclose its current NAV on its Web site).

[715] *See* rule 2a–7(c)(8)(ii)(B) and (C); *see also* rule 30b1–6T (interim final temporary rule (no longer in effect) requiring money market funds to provide the Commission certain weekly portfolio and valuation information if their market-based net asset value per share declines below 99.75% of its stable NAV).

[716] Proposed (FNAV) Form N–CR Part D. Proposed Form N–CR would require a fund to disclose the following information: (i) the date or dates on which such deviation exceeded ¼ of 1 percent; (ii) the extent of deviation between the fund's current NAV per share and its intended stable price; and (iii) the principal reason for the deviation, including the name of any security whose market-based value or sale price, or whose issuer's downgrade, default, or event of insolvency (or similar event) has contributed to the deviation.

[717] Proposed (Fees & Gates) Form N–CR Part D. Proposed Form N–CR would require a fund to disclose the following information: (i) the date or dates on which such deviation exceeded ¼ of 1 percent; (ii) the extent of the deviation between the fund's current net asset value per share and its intended stable price; and (iii) the principal reason for the deviation, including the name of any security whose market-based value or sale price, or whose issuer's downgrade, default, or event of insolvency (or similar event) has contributed to the deviation.

[718] *See* General Instruction A to proposed (FNAV) Form N–CR; general Instruction A to proposed (Fees & Gates) Form N–CR.

conservative, investing in safer securities to reduce the chance of being required to file Form N–CR? Would this affect fund yield to the point that it would affect how investors choose to invest in the fund?

2. Additional Proposed Disclosure Requirements Under Liquidity Fees and Gates Alternative

We propose to require that money market funds file a report on Form N–CR if a fund reaches the threshold triggering board consideration of a liquidity fee or redemption gate, if we adopt the proposed liquidity fees and gates alternative. This report would include a description of the fund's response (such as whether and why a fee was not imposed, as rule 2a–7 requires by default, or whether any why a gate was imposed).[719] The Commission believes that the factors specified in the required disclosure are necessary for investors and the Commission to understand the circumstances surrounding the fund's weekly liquid assets falling below 15% of total fund assets, or the imposition or removal of a liquidity fee or gate. This in turn could affect the Commission's oversight of the fund and regulation of money market funds generally, and could influence investors' decisions to purchase shares of the fund or remain invested in the fund. Disclosure of the board's analysis regarding whether to impose a liquidity fee or gate could provide investors and the Commission with a greater understanding of the events affecting and potentially causing stress to the fund, and could provide insight into the manner in which the board handles periods of fund stress.

We would also require money market funds to file a report on Form N–CR when the board lifts the fee or resumes redemptions of fund shares.[720] We would require funds to file an initial report on Form N–CR on the first business day following any occasion on which the fund's weekly liquid assets fall below 15% of its total assets, the fund's board imposes (or removes) a liquidity fee, or the fund's board temporarily suspends (or resumes) the fund's redemptions, which report would provide the date of the triggering event(s).[721] Funds would need to file an amendment to the initial report on Form N–CR by the fourth business day following any of these triggering events, which amendment would provide additional detailed information about the event(s) (namely, a description of the facts and circumstances leading to the triggering event, as well as a discussion of the fund board's analysis supporting the decision with respect to the imposition of fees or gates).[722] We believe that these reporting requirements would permit the Commission to better monitor and respond to indicators of stress, and also would help alert shareholders to events that could influence their decision to purchase shares of the fund, as well as their decision or ability to sell fund shares. We believe that the deadlines of one business day for filing an initial report and four business days for amending the initial report balance the exigency of the reports with the time it will reasonably take a fund to compile the required information. The Commission and shareholders have a significant interest in knowing that a fund's weekly liquid assets have fallen below 15% of total fund assets, and that the fund has imposed or removed a liquidity fee or gate, as soon as possible. This information directly affects investors' ability to redeem shares of a fund, and it could be a material factor in determining whether to purchase or redeem fund shares. The Commission requires this information to effectively oversee money market funds that have come under stress, and to ensure the protection of investors in these funds. The Part E and Part F initial reports, as well as Part G, do not require funds to submit substantial analysis of the underlying factors; thus, we propose to require funds to submit Part E and Part F initial reports, as well as Part G, within one business day of the event triggering the filing.

The Commission and shareholders also have a substantial interest in receiving the information that a fund would submit in amending an initial report filed in response to events specified in Part E or Part F. However, we believe that receiving an analysis of the factors leading to the imposition of fees and/or gates, as well as the board's determination whether to impose a fee and/or gates, would be of less immediate concern to the Commission and shareholders. Also, the disclosure in the amendment would require more time to compose and compile than the information required to be submitted in the initial report. Because funds would be required to submit a moderate amount of explanatory information in amending initial Part E or Part F reports, and because the personnel of a fund required to file a Part E or Part F report will likely simultaneously be occupied resolving fund liquidity pressures, we propose to permit funds to submit amendments to initial Part E or Part F reports within four business days.

We request comments on the proposed additional requirements in new Form N–CR specific to the proposed liquidity fees and gates alternative:

- Should we add any additional disclosure requirements to proposed Form N–CR specific to the proposed liquidity fees and gates alternative? Should any of the proposed requirements not be included in Form N–CR?
- Should we require reporting not just when a fund reaches the thresholds that trigger consideration of board action, but also before those triggers are reached? If so, when should we require reporting? When weekly liquid assets reach 25% of portfolio assets? Some other number? What additional

[719] Proposed (Fees & Gates) Form N–CR Parts E and F. Specifically, we propose requiring a report to be filed on Form N–CR if a fund's weekly liquid assets fall below 15% of total fund assets as set forth in proposed (Fees & Gates) rule 2a–7(c)(2). We would require the fund to disclose the following information: (i) the date on which the fund's weekly liquid assets fell below 15% of total fund assets; (ii) if the fund imposes a liquidity fee pursuant to proposed (Fees & Gates) rule 2a–7(c)(2)(i), the date on which the fund instituted the liquidity fee; (iii) a brief description of the facts and circumstances leading to the fund's weekly liquid assets falling below 15% of total fund assets; and (iv) a short discussion of the board of directors' analysis supporting its decision that imposing a liquidity fee pursuant to proposed (Fees & Gates) rule 2a–7(c)(2)(i) (or not imposing such a liquidity fee) would be in the best interest of the fund. Proposed (Fees & Gates) Form N–CR Part E.

Similarly, if a money market fund whose weekly liquid assets fall below 15% of total fund assets suspends the fund's redemptions pursuant to [rule 2a–7(c)(2)(ii)], we would require the fund to disclose the following information: (i) the date on which the fund's weekly liquid assets fell below 15% of total fund assets; (ii) the date on which the fund initially suspended redemptions; (iii) a brief description of the facts and circumstances leading to the fund's weekly liquid assets falling below 15% of total fund assets; and (iv) a short discussion of the board of directors' analysis supporting its decision to suspend the fund's redemptions. Proposed (Fees & Gates) Form N–CR Part F.

[720] Proposed (Fees & Gates) Form N–CR Part G. Specifically, we would require the fund to disclose the date on which the fund removed the liquidity fee and/or resumed fund redemptions.

[721] *See* General Instruction A to (Fees & Gates) Form N–CR; Instructions to proposed (Fees & Gates) Form N–CR Parts E and F.

[722] *Id.* The instructions to proposed (Fees & Gates) Form N–CR Part E and Part F specify which information a fund must file in the initial report, and which information a fund must file in the amendment to the initial report. Specifically, funds would need to include the date of the triggering event(s) on the initial report. The amendment to the initial report would include a brief description of the facts and circumstances leading to the fund's weekly liquid assets falling below 15% of total fund assets, and a short discussion of the board's rationale in determining whether to impose a liquidity fee (if the fund is filing Part E) or gate (if the fund is filing Part F).

Proposed (Fees & Gates) Form N–CR Part G would not require an amendment after its initial filing, because Part G simply requires a fund to disclose the date on which the fund lifted liquidity fees and/or resumed fund redemptions.

information should we ask? Would a higher reporting requirement result in too-frequent reporting?

• Should we require reporting not just when a fund reaches the thresholds that trigger consideration of board action, but also at some threshold after those triggers are reached? If yes, when should we require the additional reporting? When weekly liquid assets reach 10% of portfolio assets? Some other number? Should we require similar reporting when daily liquid assets drop below a certain threshold? If so, what threshold should we require? When daily liquid assets reach 0%, or should we set a higher threshold such as 5%?

• Would the particular information that we propose requiring funds to report in response to Parts E, F, and G of Form N–CR be useful to shareholders in understanding the events triggering the filing of Form N–CR? Should we require any more, any less, or any other information to be reported?

• How frequently do commenters anticipate that funds would file reports on proposed Form N–CR in response to the proposed requirements specific to the proposed liquidity fees and gates alternative? What average length of time do commenters anticipate transpiring between a fund's initial report in response to Part E or Part F of Form N–CR, and a fund's report in response to Part G of Form N–CR?

• Do the proposed reporting deadlines appropriately balance the Commission's and the public's need for information on current events affecting money market funds with the costs of preparing and submitting a report on Form N–CR? Does the proposed requirement to file an initial report on Form N–CR for Parts E and F within one business day following a triggering event, and then to file an amended report within four business days following the event, appropriately balance the exigency of the reports with the time that it will reasonably take a fund to compile the required information for each part? Should we require a longer or shorter time frame in which to file a report on Form N–CR for any of the parts?

• Are there any other events that warrant a current report filing obligation under the proposed liquidity fees and gates alternative?

• How, if at all, would the requirement to file Form N–CR affect the fund's investment decisions, including the fund's decision to invest in weekly liquid assets?

• How, if at all, would the requirement to file Form N–CR affect the fund's decisions with respect to accepting investments from certain groups of shareholders? For example, would funds be less likely to accept investments from large shareholders or short-term shareholders?

• How, if at all, would the requirement to file Form N–CR affect the board's decisions surrounding the imposition of liquidity fees and gates? Would the Form N–CR filing requirement affect the board's willingness to deviate from the default liquidity fee requirements? Why or why not?

3. Economic Analysis

As discussed above, we believe that the Form N–CR reporting requirements would provide important transparency to investors and the Commission, and also could help investors better understand the risks associated with a particular money market fund, or the money market fund industry generally. The Form N–CR reporting requirements would permit investors and the Commission to receive information about certain money market fund material events consistently and relatively quickly. As discussed above, we believe that investors and the Commission have a significant interest in receiving this information because it would permit investors and the Commission to monitor indicators of stress in specific funds or fund groups, as well as the money market fund industry, and also to analyze the economic effects of certain material events. The Form N–CR reporting requirements could give investors and the Commission a greater understanding of the circumstances leading to events of stress, and also how a fund's board handles events of stress. We believe that investors could find all of this information to be material and helpful in determining whether to purchase fund shares, or remain invested in a fund. However, we recognize that the Form N–CR reporting requirements have operational costs (discussed below), and also may result in opportunity costs, in that personnel of a fund that has experienced an event that requires Form N–CR reporting may lose a certain amount of time that could be used to respond to that event because of the need to comply with the reporting requirement. However, as discussed above, we believe that the proposed time frames for filing reports on Form N–CR balance the exigency of the report with the time it will reasonably take a fund to compile the required information.

We believe that the proposed Form N–CR reporting requirements may complement the benefits of increased transparency of publicly available money market fund information that have resulted from the requirement that money market funds report their portfolio holdings and other key information on Form N–MFP each month. The RSFI Study found that the additional disclosures that money market funds are required to make on Form N–MFP improve fund transparency (although funds file the form on a monthly basis with no interim updates, and the Commission currently makes the information public with a 60-day lag).[723] The RSFI Study also noted that this ''increased transparency, even if reported on a delayed basis, might dampen a fund manager's willingness to hold securities whose ratings are at odds with the underlying risk, especially at times when credit conditions are deteriorating.'' [724] Additionally, the availability of public, standardized, money market fund-related data that has resulted from the Form N–MFP filing requirement has assisted both the Commission and the money market fund industry in various studies and analyses of money market fund operations and risks.[725] The proposed Form N–CR reporting requirement could extend these benefits of Form N–MFP by providing additional transparency about money market funds' risks on a near real-time basis, which may, like Form N–MFP disclosure, impose market discipline on portfolio managers and provide additional data that would allow investors to make investment decisions, and the Commission and the money market fund industry to conduct risk- and operations-related analyses.

We believe that the proposed reporting requirements may positively affect regulatory efficiency because all money market funds would be required to file information about certain material events on a standardized form, thus improving the consistency of information disclosure and reporting, and assisting the Commission in overseeing individual funds, and the money market fund industry generally, more effectively. The proposed requirements also could positively affect informational efficiency. This could assist investors in understanding various risks associated with certain

[723] *See* RSFI Study, *supra* note 21, at 31; *see also infra* note 793 and accompanying text (discussing the Commission's proposal to eliminate the 60-day delay in making Form N–MFP information publicly available).

[724] *See* RSFI Study, *supra* note 21, at 38.

[725] *See, e.g., Money Market Mutual Funds, Risk, and Financial Stability in the Wake of the 2010 Reforms,* 19 ICI Research Perspective No. 1 (Jan. 2013), at n.29 (noting that certain portfolio-related data points are often only available from the SEC's Form N–MFP report).

funds, and risks associated with the money market fund industry generally, which in turn could assist investors in choosing whether to purchase or redeem shares of certain funds. The proposed requirements could positively affect competition because funds could compete with each other based on certain information required to be disclosed on Form N–CR, as well as based on more traditional competitive factors such as price and yield. For instance, investors might see a fund that invests in securities whose issuers have never experienced a default as a more attractive investment than a similar fund that frequently files reports in response to Form N–CR Part B (''Default or Event of Insolvency of portfolio security issuer''). However, if investors move their assets among money market funds or decide to invest in investment products other than money market funds as a result of the Form N–CR reporting requirements, this could negatively affect the competitive stance of certain money market funds, or the money market fund industry generally. If money market fund investors decide to move all or a substantial portion of their money out of the market, this could negatively affect capital formation.[726] On the other hand, capital formation could be positively affected if the Form N–CR reporting requirements were to assist the Commission in overseeing and regulating the money market fund industry, and the resulting regulatory framework more efficiently or more effectively encouraged investors to invest in money market funds. Additional effects of these proposed filing requirements on efficiency, competition, and capital formation would vary according to the event precipitating the Form N–CR filing, and they are substantially similar to the effects of other proposed disclosure requirements, as discussed in more detail above.[727]

The operational costs of filing Form N–CR in response to the events specified in Parts B–G of Form N–CR are discussed below.[728] The Commission staff has not measured the quantitative benefits of these proposed requirements at this time because of uncertainty about how increased transparency may affect different investors' understanding of the risks associated with money market funds and their imposition of market discipline.[729]

We have estimated that the costs of filing a report in response to an event specified on Part B of Form N–CR would be higher than the costs that money market funds currently incur in complying with rule 2a–7(c)(7)(iii)(A), which requires money market funds to report defaults or events of insolvency to the Commission by email.[730] We estimate the costs of filing a report in response to an event specified on Part B of Form N–CR to be $1,708 per filing,[731] and we expect, based on our estimate of the average number of notifications of events of default or insolvency that money market funds currently file each year, that the Commission would receive approximately 20 such filings per year.[732] Therefore, we expect that the annual costs relating to filing a report on Form N–CR in response to an event specified on Part B would be $34,160.[733]

Likewise, we have estimated that the costs of filing a report in response to an event specified on Part C of Form N–CR in part by reference to the costs that money market funds currently incur in complying with rule 2a–7(c)(7)(iii)(B), which requires disclosure to the Commission by email when a sponsor supports a money market fund by purchasing a security in reliance on rule 17a–9. However, because Part C of Form N–CR defines ''financial support'' more broadly than the purchase of a security from a fund in reliance on rule 17a–9, and because the requirements of Part C of Form N–CR are more extensive than the requirements of rule 2a–7(c)(7)(iii)(B), we expect that the costs associated with filing a report in response to a Part C event would be higher than the current costs of compliance with rule 2a–7(c)(7)(iii)(B). We estimate the costs of filing a report in response to an event specified on Part C of Form N–CR to be $1,708 per filing,[734] and we expect, based in part by reference to our estimate of the average number of notifications of security purchases in reliance on rule 17a–9 that money market funds currently file each year, that the Commission would receive approximately 40 such filings per year.[735] Therefore, we expect that the annual costs relating to filing a report on Form N–CR in response to an event specified on Part C would be $68,320.[736]

As discussed in more detail in section IV below, we have estimated the costs associated with filing a report on Form N–CR in response to an event specified on Part D, E, F, or G on a broad average basis. In particular, in an event of filing, the staff believes a fund's particular circumstances that gave rise to a reportable event would be the predominant factor in determining the time and costs associated with filing a report on Form N–CR. Accordingly, on average, we estimate the costs of filing a report in response to an event specified on Part D of Form N–CR to be $1,708 per report.[737] On average, we estimate the costs of filing a report in response to an event specified on Part E or Part F of Form N–CR to be $1,708 per filing.[738] On average, we estimate

[726] For an analysis of the potential macroeconomic effects of our proposals, *see supra* section III.E.1.

[727] We believe that the effects on efficiency, competition, and capital formation of filing Form N–CR in response to Part B or C would overlap significantly with the effects of the proposed disclosure requirements regarding the financial support provided to money market funds. *See* discussion in *supra* section III.F.1.b. We believe that the effects of filing Form N–CR in response to Part D would overlap significantly with the effects of the proposed disclosure requirements regarding a money market fund's daily market-based NAV per share. *See* discussion in *supra* section III.F.3.b. We believe that the effects of filing Form N–CR in response to Parts E, F, and G would overlap significantly with the effects of the proposed disclosure requirements regarding current and historical instances of the imposition of liquidity fees and/or gates. *See supra* section III.B.8.f.

[728] These costs incorporate the costs of responding to Part A (''General information'') of Form N–CR. We anticipate that the costs associated with responding to Part A will be minimal, because Part A requires a fund to submit only basic identifying information.

[729] Likewise, uncertainty regarding the proposed disclosure's effect on different investors' behavior makes it difficult for the SEC staff to measure the quantitative benefits of the proposed requirements at this time.

[730] The requirements of rule 2a–7(c)(7)(iii)(A) and the requirement of Part B of Form N–CR are substantially similar, although Part B on its face specifies more information to be reported than rule 2a–7(c)(7)(iii)(A). However, Commission staff understands that funds disclosing events of default or insolvency pursuant to rule 2a–7(c)(7)(iii)(A) already have historically reported substantially the same information proposed to be required by Part B.

[731] The costs associated with filing Form N–CR in response to an event specified on Part B of Form N–CR are paperwork-related costs and are discussed in more detail in *infra* section IV.A.4 and IV.B.4.

[732] *See Submission for OMB Review, Comment Request, Extension: Rule 2a–7, OMB Control No. 3235–0268,* Securities and Exchange Commission [77 FR 236 (Dec. 7, 2012)].

[733] These estimates are based on the following calculations: $1,708 (cost per report) × 20 filings per year = $34,160 per year. *See supra* notes 731–732 and accompanying text.

[734] The costs associated with filing Form N–CR in response to an event specified on Part C of Form N–CR are paperwork-related costs and are discussed in more detail in *infra* section IV.A.4 and IV.B.4.

[735] *See Submission for OMB Review, Comment Request, Extension: Rule 2a–7, OMB Control No. 3235–0268,* Securities and Exchange Commission [77 FR 236 (Dec. 7, 2012)].

[736] These estimates are based on the following calculations: $1,708 (cost per report) × 40 filings per year = $68,320 per year. *See supra* notes 734–735 and accompanying text.

[737] *See infra* section IV.A.4 and IV.B.4.

[738] *Id.* This estimate includes the costs of filing an initial report, as well as amending the initial report. *See* instructions to proposed (Fees & Gates) Form N–CR Parts E, F.

the costs of filing a report in response to an event specified on Part G of Form N–CR to be $1,708 per filing.[739]

We request comment on this economic analysis:

- Would any of the proposed disclosure requirements impose unnecessary costs? Why or why not?
- How many filings would be made each year in response to the events specified on each of Part B, Part C, Part D, Part E, Part F, and Part G of Form N–CR?
- Please comment on our analysis of the potential effects of these proposed disclosure requirements on efficiency, competition, and capital formation.

*H. Amendments to Form N–MFP Reporting Requirements*

The Commission is proposing to amend Form N–MFP, the form that money market funds use to report to us their portfolio holdings and other key information each month. We use the information to monitor money market funds and support our examination and regulatory programs. Each fund must file information on Form N–MFP electronically within five business days after the end of each month. We make the information public 60 days after the end of the month.[740] Money market funds began reporting this information to us in November 2010.[741]

We are proposing to amend Form N–MFP to reflect amendments to rule 2a–7 discussed above, as well as request certain additional information that would be useful for our oversight of money market funds, and make other improvements to the form based on our experience with filings submitted during the past two and a half years. As discussed below in section III.H.1, our proposed amendments related to rule 2a–7 changes proposed elsewhere in this Release would be adopted under either regulatory alternative. Regardless of the regulatory alternative adopted, or if neither alternative is adopted, we anticipate that we would adopt the other amendments that we propose to make to the Form described in this section relating to new reporting requirements, clarifying amendments, and public availability of information (sections III.H.2–III.H.4 below) because they would be relevant to the Commission's efforts to oversee the stability of money market funds and compliance with rule 2a–7.[742] In connection with these amendments, we propose to renumber the items of Form N–MFP to separate the items into four separate sections.[743]

1. Amendments Related to Rule 2a–7 Reforms

Under our floating NAV proposal or our liquidity fees and gates proposal, we would revise Form N–MFP to reflect certain proposed amendments to rule 2a–7. Because both alternative proposals would require that all money market funds (including government and retail money market funds otherwise exempt) value portfolio securities using market-based factors and/or fair value pricing (not amortized cost[744]), we propose to amend the items in Form N–MFP that reference ''amortized cost.'' Those items instead would require that funds disclose the ''value'' of portfolio securities.[745]

Accordingly, without amortized cost, funds would not have a ''shadow price'' to disclose. Therefore, we also propose to eliminate the items in Form N–MFP that require disclosure of ''shadow prices.''[746] A fund would still be required to disclose the net asset value per share at the series level and class level, but we propose to require that each monthly report include the net asset value per share as of the close of business on each Friday during the month reported. Thus, while funds would continue to file reports on Form N–MFP once each month (as they do today), certain limited information (such as the NAV per share) would be reported on a weekly basis. In addition, we propose to require, both for each series and each class, reporting of the net asset value per share, rounded to the fourth decimal place for a fund with a $1.00 share price (or an equivalent level of accuracy for funds with a different share price).[747] If we adopted our floating NAV proposal, this would conform net asset value per share reporting to the rounding convention in our rule proposal.[748] If we adopted our liquidity fees and gates proposal, these items would in effect require reporting of the fund's price per share without penny rounding. This information would be used by the Commission and others to identify money market funds that continue to seek to maintain a stable price per share[749] and better evaluate any potential deviations in their unrounded share price. Finally, we propose to amend the category options at the series level that money market funds use to identify themselves and include government funds that would

[739] *Id.*

[740] *See* rule 30b1–7(b).

[741] On average, 616 money market funds filed Form N–MFP with us each month during 2012. Funds reported information on nearly 68,000 securities on average each month.

[742] References to Form N–MFP will be ''Proposed Form N–MFP Item.'' We are not proposing to amend items in Form N–MFP that reference credit ratings. References to credit ratings will be addressed in a separate rulemaking. *See supra* note 130 and accompanying text.

[743] *See* proposed Form N–MFP: (i) General information (Items 1–8); (ii) information about each *series* of the fund (Items A.1–A.21; (iii) information about each *class* of the fund (Items B.1–B.8); and (iv) information about portfolio securities (Items C.1–C.25). Our proposed renumbering of the items will enable us to add or delete items in the future without having to re-number all subsequent items in the form.

[744] As discussed above, money market funds, like other mutual funds, would be able to use amortized cost to value securities with maturities of 60 days or less provided the fund's board determines that the security's fair value is its amortized cost and the circumstances do not suggest otherwise. *See supra* note 136 and accompanying discussion. Because the board in these circumstances must conclude that the amortized value of the securities is the fair value of the securities, there would be no need for separate disclosure of both values. In addition, government and retail money market funds, which would be exempt from our floating NAV proposal, would be required to value portfolio securities using market-based factors (not amortized cost), but continue to be allowed to use penny rounding to maintain a stable price per share. *See supra* sections III.A.3 and III.A.4.

[745] Form N–MFP requires that each series of a fund disclose the total amortized cost of its portfolio securities (Item 13) and the amortized cost for each portfolio security (Item 41). We propose to amend Items 13 and 41 by replacing amortized cost with ''value'' as defined in section 2(a)(41) of the Act. *See* proposed Form N–MFP Items A.14.b, C.18, and proposed Form N–MFP General Instructions, E. Definitions. As a result, we propose to remove current Form N–MFP Items 45 and 46, which require that a fund disclose the value of each security using available market quotations, both with and without the value of any capital support agreement. Proposed Form N–MFP Item C.18 would require that MMFs report portfolio security market values both including and excluding the value of any sponsor support. To improve transparency of MMF's risks, we propose to clarify that MMFs must disclose the value of ''any sponsor support'' applicable to a particular portfolio security, rather than ''capital support agreements'' as stated in current Form N–MFP Items 45 and 46.

[746] Form N–MFP currently requires a fund to disclose the shadow price of the fund series (Item 18) and each fund class (Item 25), both of which we propose to eliminate.

We also propose to amend the definition of ''money market fund'' to conform to our proposed amendment. As proposed, a money market fund means a fund that holds itself out as a money market fund and meets all of the requirements of rule 2a–7 (eliminating the specific reference to rule 2a–7's maturity, quality, and diversification requirements). *See* proposed Form N–MFP General Instructions, E. Definitions (defining ''Money Market Fund'').

[747] *See* proposed Form N–MFP Items A.21 and B.5 (noting that if the reporting date falls on a holiday or other day on which the fund does not calculate the net asset value per share, provide the value as of the close of business on the date in that week last calculated). This reporting instruction also applies to our proposed weekly reporting of daily and weekly liquid assets. *See* proposed Form N–MFP Item A.13.

[748] *See* proposed (FNAV) rule 2a–7(c)(1).

[749] We propose to require that a fund that seeks to maintain a stable price per share state the price that the fund seeks to maintain. *See* proposed Form N–MFP Item A.18.

be exempt under either alternative proposal.[750]

Our proposed amendment to require that each monthly report include the net asset value per share as of the close of business on each Friday during the month reported would be consistent with other actions taken by the Commission and fund industry participants to increase the frequency of disclosure of funds' NAV per share (on funds' Web sites).[751] Despite the increased frequency of disclosure within the monthly report, funds would continue to file reports on Form N–MFP once each month. By including this information in Form N–MFP, in addition to a fund's Web site, Commission staff and others may better monitor the risks that may be present in declining prices, for example. This information, if available on Form N–MFP, could then be aggregated and analyzed across the fund industry. If we adopt our floating NAV proposal, funds required to price their shares at the market-based NAV per share would already have this information readily available. Also, as noted above, many money market funds have begun disclosing shadow prices daily on fund Web sites and therefore we believe this information is readily available to funds. Any effect resulting from our proposed amendment to require that each monthly report include NAV per share data on a weekly basis is included in our economic analysis of our proposed amendment to require that money market funds disclose NAV per share daily on fund Web sites.[752] Finally, we note that the remaining proposed changes would omit or amend disclosure requirements that would no longer be relevant if we adopt the changes we are proposing to rule 2a–7. Accordingly, we do not believe that the proposed amendments would impose costs on money market funds other than those required to modify systems used to aggregate data and file reports on Form N–MFP. These costs are discussed in section III.H.6 below.

We believe that the proposed revised form will be easier for investors to understand because the simplifications allow investors to focus on a single market-based valuation for individual portfolio securities and the fund's overall NAV per share. This approach is also consistent with today's standard practice for mutual funds that are not money market funds. We expect that the overall effects will be to increase efficiency for not only investors but also the funds themselves. As discussed above, the floating NAV proposal and the liquidity fees and gates proposal will affect both competition and capital formation. Because we believe that investors are likely to make at least incremental changes to their trading patterns in money market funds due to the proposed changes to Form N–MFP, it is likely that the changes will affect competition and capital formation. Although it is difficult to quantify the size of these effects without better knowledge about how investors will respond, we believe that the effects from the proposed changes to Form N–MFP will be small relative to the effects of the underlying alternative proposals. We seek comment on this aspect of our proposal.

- Should money market funds be required to include in each monthly Form N–MFP filing the NAV per share as of the close of business on each Friday during the month reported? Or should we require that money market funds report market-based NAV per share data daily on Form N–MFP? Would the costs be significantly different from reporting monthly data, as is currently required? Would the costs to funds be significantly different from reporting weekly data, as we propose above? Please describe the associated costs.
- Do commenters agree with our analysis of potential effects on efficiency, competition, and capital formation?

2. New Reporting Requirements

We are also proposing (regardless of the alternative proposal adopted, if any) several new items to Form N–MFP that we believe will improve our (and investors') ability to monitor money market funds.[753] These proposed amendments would address gaps in information that have become apparent during the time we have received Form N–MFP filings and our staff has analyzed the data. As discussed further below, each proposed amendment requires reporting of additional information that should be readily available to the fund and, in many cases, should infrequently change from report to report.

Several proposed amendments are designed to help us and investors better identify fund portfolio securities.[754] To facilitate monitoring and analysis of the risks posed by funds, it is important for Commission staff to be able to identify individual portfolio securities. Fund shareholders and potential investors that are evaluating the risks of a fund's portfolio would similarly benefit from the clear identification of a fund's portfolio securities. Currently, the form requests information about the CUSIP number of a security, which the staff uses as a search reference. The staff has found that some securities reported by money market funds lack a CUSIP number, and this absence has reduced the usefulness of other information reported.[755] To address this issue going forward, we propose to require that funds report, in addition to the CUSIP, the Legal Entity Identifier (''LEI'') that corresponds to the security.[756] The proposed amendments would also

[750] *See* proposed Form N–MFP Item A.10 (adding ''Exempt Government'' category). If we adopt the floating NAV alternative, we would also add a new category for ''Exempt Retail'' funds.

[751] *See supra* section III.F.3 (proposing to require that money market funds disclose on fund Web sites the fund's current market-based NAV per share); *see also infra* note 793 and accompanying text (noting the current industry trend to disclose shadow prices daily on fund Web sites).

[752] *See supra* section III.F.3.

[753] The proposed new reporting requirements, clarifying amendments, amendments related to public availability of information, and potential amendment to Form N–MFP's filing date, discussed in *infra* sections III.H.2–5 are separate from the proposed amendments to Form N–MFP related to the rule 2a–7 reforms discussed above (*see supra* section III.H.1). Thus, even if we do not adopt amendments to rule 2a–7, we may adopt the other proposed amendments to Form N–MFP.

[754] We also propose to require that a fund provide the name, email address, and telephone number of the person authorized to receive information and respond to questions about Form N–MFP. We plan to exclude this information from Form N–MFP information that is made publicly available through EDGAR. Proposed Form N–MFP Item 8.

[755] Our inability to identify specific securities, for example, limits our ability to compare ownership of the security across multiple funds and monitor issuer exposure. During the month of February 2013, funds reported 6,821 securities without CUSIPs (approximately 10% of all securities reported on the form).

[756] *See* proposed Form N–MFP Item C.4; Proposed Form N–MFP General Instructions, E. Definitions (defining ''LEI''). To ensure accurate identification of Form N–MFP filers and update the Form for pending industry-wide changes, we are also proposing that each registrant provide its LEI, if available. *See* proposed Form N–MFP Item 3. The Legal Entity Identifier is a unique identifier associated with a single corporate entity and is intended to provide a uniform international standard for identifying counterparties to a transaction. The Commission has begun to require disclosure of the LEI, once available. *See, e.g.,* Form PF, Reporting Form for Investment Advisers to Private Funds and Certain Commodity Pool Operators and Commodity Trading Advisors, *available at http://www.sec.gov/rules/final/2011/ia-3308-formpf.pdf.* A global LEI standard is currently in the implementation stage. *See Frequently Asked Questions: Global Legal Entity Identifier (LEI)* (Feb. 2013), U.S. Treasury Dept., *available at http://www.treasury.gov/initiatives/ofr/data/Documents/LEI_FAQs_February2013_FINAL.pdf.* Consistent with staff guidance provided in a Form PF Frequently Asked Questions (*http://www.sec.gov/divisions/investment/pfrd/pfrdfaq.shtml*), funds that have been issued a CFTC Interim Compliant Identifier (''CICI'') by the Commodity Futures Trading Commission may provide this identifier in lieu of the LEI until a global LEI standard is established.

require that funds report at least one other security identifier.[757]

We also propose amendments that are designed to help the staff (and investors) better identify certain risk characteristics that the form currently does not capture. Responses to these new items, together with other information reported, would improve the staff's (and investors') understanding of a fund and its potential risks. First, we propose to require funds to report whether a security is categorized as a level 1, level 2, or level 3 measurement in the fair value hierarchy under U.S. Generally Accepted Accounting Principles.[758] Level 1 measurements include quoted prices for identical securities in an active market (*e.g.,* active exchange-traded equity securities; U.S. government and agency securities). Level 2 measurements include: (i) Quoted prices for similar securities in active markets; (ii) quoted prices for identical or similar securities in non-active markets; and (iii) pricing models whose inputs are observable or derived principally from or corroborated by observable market data through correlation or other means for substantially the full term of the security. Securities categorized as level 3 are those whose value cannot be determined by using observable measures (such as market quotes and prices of comparable instruments) and often involve estimates based on certain assumptions.[759]

We understand that most money market fund portfolio securities are categorized as level 2. Although we understand that very few of a money market fund's portfolio securities are currently valued using unobservable inputs, information about any such securities would enable our staff to identify individual securities that may be more susceptible to wide variations in pricing.[760] Commission staff could also use this information to monitor for increased valuation risk in these securities, and to the extent there is a concentration in the security across the industry, identify potential outliers that warrant additional monitoring or investigation. Our proposed amendment would permit the Commission and others to analyze movements in the assets in each level, for example, movements in level 2 securities as a percentage of net assets. In addition, Commission staff would be better able to identify anomalies in reported data by aggregating all money market fund holdings industry-wide into the various level categories. We believe that most funds directly evaluate the fair value level measurements when they acquire the security and re-assess the measurements when they perform portfolio valuations.[761] Accordingly, we believe that funds should have ready access to the nature of the portfolio security valuation inputs used.

- Would our new proposed requirements help us better identify certain risk characteristics that the form currently does not capture?
- Would information about each security's categorization as a level 1, level 2, or level 3 measurement better enable our staff to identify individual securities that may be more susceptible to wide variations in pricing?
- Is our understanding about how fund sponsors value most money market fund portfolio securities (*i.e.,* using Level 2 measurements) correct?
- Do our assumptions about fund valuation procedures and access to the nature of portfolio security valuation inputs correspond to fund practices? Is this information readily available to a fund?
- Are there other ways in which a fund could identify and disclose securities that do not have readily available market quotations or observable inputs?
- Do commenters agree that this information will help the Commission and investors better identify risk characteristics?

Second, we would require that funds disclose additional information about each portfolio security, including, in addition to the total principal amount,[762] the purchase date, the yield at purchase, the yield as of the Form N–MFP reporting date (for floating and variable rate securities, if applicable),[763] and the purchase price.[764] We would require that funds report this information separately for each lot purchased.[765] In addition, we propose to require that money market funds disclose the same information for any security sold during the reporting period.[766] Because money market funds often hold multiple maturities of a single issuer, each time a security is purchased or sold, price discovery occurs and an issuer yield curve could be updated and used for revaluing all holdings of that particular credit. Therefore, our proposed amendments would have the incidental benefit of facilitating price discovery and would enable the Commission and others to evaluate pricing consistency across funds (and identify potential outliers).[767] We request comment on this aspect of our proposal.

- Do commenters agree that our proposed additional requirements would facilitate price discovery? Would any of our proposed additional requirements not facilitate price discovery? Are there other requirements than those proposed that would be helpful?
- Should we require a different convention for pricing fixed income securities? If so, what?

In addition, we would require funds to report the amount of cash they

[757] *See* proposed Form N–MFP Item C.5 (requiring that, in addition to the CUSIP and LEI, a fund provide at least one additional security identifier (*e.g.,* ISIN, CIK or other unique identifier)). Security identifiers should be readily available to funds. *See, e.g., http://www.sec.gov/edgar/searchedgar/cik.htm* (providing a CIK lookup that is searchable by company name). We are also proposing to require that a fund provide the CUSIP number and LEI (if available) for a security subject to a repurchase agreement. *See* proposed Form N–MFP Items C.8.c. and C.8.d.

[758] *See* Accounting Standards Codification 820, ''Fair Value Measurement''; Proposed Form N–MFP Item C.20.

[759] *See* Accounting Standards Codification 820, ''Fair Value Measurement''.

[760] For a discussion of some of the challenges regulators may face with respect to Level 3 accounting, *see, e.g.,* Konstantin Milbradt, *Level 3 Assets: Booking Profits and Concealing Losses,* in 25 Rev. Fin. Stud. 55–95 (2011).

[761] Funds should regularly evaluate the pricing methodologies used and test the accuracy of fair value prices (if used). *See* Accounting Series Release No. 118, Financial Reporting Codification (CCH) section 404.03 (Dec. 23, 1970).

[762] Current Form N–MFP Item 40.

[763] We understand that the yields on variable rate demand notes, for example, may vary daily, weekly, or monthly. Our proposed amendment would provide Commission staff and others with a way to monitor the market's response to changes in credit quality, as well as identify potential outliers. We believe that money market funds have this information readily available because funds require this information to calculate daily distributions of income, and thus, should not impose costs on funds (other than those discussed in *infra* section III.H.6).

[764] *See* proposed N–MFP Item C.17. Because yield at purchase would be disclosed in a separate item, we propose to delete the reference to ''(including coupon or yield)'' from current Form N–MFP Item 27 (Proposed Form N–MFP Item C.2). The purchase price must be reported as a percentage of par, rounded to the nearest one thousandth of one percent. *See* proposed Form N–MFP Item C.17.e. We believe this represents the standard convention for pricing fixed-income securities. For example, a security issued at a 1% premium to par would report the purchase price as $101.000.

[765] *See* proposed Form N–MFP Item C.17.

[766] See proposed Form N–MFP Item C.25 (requiring that a fund disclose, for each security sold by the series during the reporting period, (i) the total principal amount; (ii) the purchase price; (iii) the sale date; (iv) the yield at sale; and (v) the sale price. Information about any securities sold by the fund during the reporting period would also provide the Commission and others with important information about how the fund may be handling heavy redemptions (*e.g.,* selling securities at a haircut).

[767] *See* Federal Reserve Bank Presidents FSOC Comment Letter, *supra* note 38 (suggesting that more frequent reporting on Form N–MFP might increase price discovery (for market-based NAV calculations)).

hold,[768] the fund's Daily Liquid Assets and Weekly Liquid Assets,[769] and whether each security is considered a Daily Liquid Asset or Weekly Liquid Asset.[770] Unlike the other items of disclosure on Form N–MFP which must be disclosed on a monthly basis, we propose to require that funds report the Daily Liquid Assets and Weekly Liquid Assets on a weekly basis. Similarly, we propose to require that money market funds disclose the weekly gross subscriptions (including dividend reinvestments) and weekly gross redemptions for each share class, once each week during the month reported.[771] As discussed earlier, money market funds would continue to file reports on Form N–MFP once each month, but certain information (including disclosure of Daily and Weekly Liquid Assets and shareholder flow) would be reported weekly within the Form.

Our proposed amendments would provide Commission staff and others with more relevant data to efficiently monitor fund risk, such as the likelihood that a fund might trip a liquidity-based trigger (*e.g.,* a liquidity fee or gate, if that regulatory alternative is adopted) and correlated risk shifts in liquidity across the industry.[772] Increased periodic disclosure of the daily and weekly liquid assets on Form N–MFP would provide increased transparency into how funds manage their liquidity, and it may also impose market discipline on portfolio managers. In addition, increased disclosure of weekly gross subscriptions and gross redemptions (reported weekly, in addition to monthly) would improve the ability of the Commission and others to better understand the significance of other liquidity disclosures required by our proposals (*e.g.,* daily and weekly liquid assets). As a result, investors may make more informed investment decisions and fund managers may manage fund portfolios in a way that enhances stability in the short-term financing markets. We also propose to require that funds disclose whether, during the reporting period, any person paid for or waived all or part of the fund's operating expenses or management fees.[773] Information about expense waivers will help us understand potential strains on a fund's investment adviser during periods of low interest rates. We request comment on these aspects of our proposed reforms.

- Would reporting the daily and weekly liquid asset levels and gross subscriptions and redemptions as of the close of business each Friday during the reporting period conflict with the fund's other disclosure requirements, which are required only as of the last business day or any later calendar day in the month? Should we require that this information be provided to the Commission more or less frequently, or at a different time or day each week?
- Would reporting on expense waivers help us and investors better understand potential financial strains on a fund's investment adviser?
- Do commenters agree that increased transparency will lead to greater market discipline on portfolio managers and lead investors to make more informed decisions?

We also propose to require that funds disclose the total percentage of shares outstanding, to the nearest tenth of one percent, held by the twenty largest shareholders of record.[774] This information would help us (and investors) identify funds with significant potential redemption risk stemming from shareholder concentration, and evaluate the likelihood that a significant market or credit event might result in a run on the fund or the imposition of a liquidity fee or gate, if we were to adopt that aspect of our proposal.[775] Investors may avoid overly concentrated funds and this preference may incentivize some funds to avoid becoming too concentrated. This may, in turn, increase investment costs for large shareholders that are compelled to spread their investments across multiple funds, especially if they choose funds from multiple fund groups. We request comment on this proposed reporting.

- Would the total percentage of shares outstanding held by the fund's twenty largest shareholders help us and investors identify funds with significant potential redemption risk stemming from shareholder concentration?
- Would the use of omnibus accounts reduce the value of information about shareholder concentration? If so, is there other data we could require that would yield more useful information?
- Could funds or shareholders ''game'' this reporting requirement by splitting a large investment into smaller pieces? Are there reasonable rules the Commission could adopt to address this potential ''gaming?''
- Should we require that funds report the total holdings of a different number of top shareholders (*e.g.,* five, ten, or thirty shareholders)?
- Should we require the reporting of this information only if the top shareholders of record own in the aggregate at least a certain total percentage of the fund's outstanding shares? If so, how many shareholders should we consider, and what should that threshold be (*e.g.,* 1%, 2%, or 5%)?
- Is there a better way to assess the risks associated with shareholder concentration? Should we require aggregation of holdings by affiliates?

In addition, we propose that funds report the maturity date for each portfolio security using the maturity date used to calculate the dollar-weighted average life maturity (''WAL'') (*i.e.,* without reference to the exceptions in rule 2a–7(i) regarding interest rate readjustments).[776] In 2010, we adopted a requirement that limits the WAL of a fund's portfolio to 120 calendar days because we were concerned about the extent to which a manager could expose a fund to credit spread risk associated with longer-term, adjustable-rate securities.[777] This information will assist the Commission in monitoring and evaluating this risk, at the security level, as well as help evaluate

[768] *See* proposed Form N–MFP Item A.14.a; Proposed Form N–MFP General Instructions, E. Definitions (requiring disclosure of the amount of cash held and defining ''cash'' to mean demand deposits in insured depository institutions and cash holdings in custodial accounts). We propose to amend Item 14 of Current Form N–MFP (total value of other assets) to clarify that ''other assets'' excludes the value of assets disclosed separately (*e.g.,* cash and the value of portfolio securities). *See* proposed Form N–MFP Item A.14.c. Our proposed amendment would ensure that reported amounts are not double counted.

[769] *See* proposed Form N–MFP Item A.13.

[770] Proposed Form N–MFP Items C.21–C.22.

[771] *See* proposed Form N–MFP Item B.6. We propose to continue to require that money market funds also disclose the monthly gross subscriptions and monthly gross redemptions for the month reported. *See* current Form N–MFP Item 23 (proposed Form N–MFP Item B.6.f).

[772] As discussed in section III.F.2, under either alternative proposal, money market funds would also be required to disclose each day on its Web site the fund's Daily Liquid Assets and Weekly Liquid Assets.

[773] Proposed Form N–MFP Item B.8 (requiring that funds provide the name of the person and describe the nature and amount the expense payment or fee waiver, or both (reported in dollars).

[774] *See, e.g.,* Fidelity Investments, An Analysis of the SEC Study on Money Market Mutual Funds: Considering the Scope and Impact of Possible Further Regulation (Jan. 2013) at 5, *available at https://www.sec.gov/comments/mms-response/mmsresponse-16.pdf* (suggesting one key factor that could be used to distinguish between retail and institutional money market funds be whether the top 20 shareholders accounts for greater than or less than 15% of the fund's assets).

[775] Proposed Form N–MFP Item A.19. We are also proposing to require that a fund disclose the number of shares outstanding, to the nearest hundredth, at both the series level and class level. Proposed Form N–MFP Items A.17 and B.4. This information would permit us to verify or detect errors in information provided on Form N–MFP, such as net asset value per share.

[776] Proposed Form N–MFP Item C.12.

[777] *See* 2010 Adopting Release, *supra* note 92, at section II.B.2.

compliance with rule 2a–7's maturity provisions. In addition, our proposed amendments would make clear that funds disclose for each security all three maturity calculations as required under rule 2a–7: dollar-weighted average portfolio maturity (''WAM''), WAL, and the final legal maturity date.[778] Finally, the proposed amendments would require that a fund disclose additional information about certain types of securities held by the fund.[779] We request comment on our proposed amendments.

- Do commenters agree that disclosure of each security's WAL will assist the Commission and investors in evaluating credit spread risk? We note that Form N–MFP currently requires that funds disclose each security's WAM and final legal maturity date.[780]
- Would our proposed amendments to the category of investment increase the accuracy of how securities are categorized currently? Should we include other investment categories?

As detailed above, our proposed new reporting requirements are intended to address gaps in the reporting regime that Commission staff has identified through two and a half years of experience with Form N–MFP and to enhance the ability of the Commission and investors to monitor funds. Although the potential benefits are difficult to quantify, they would improve the ability of the Commission and investors to identify (and analyze) a fund's portfolio securities (*e.g.,* by requiring disclosure of LEIs and an additional security identifier beyond CUSIPs already required). In addition, many of our proposed new reporting requirements would enhance the ability of the Commission and investors to evaluate a fund's risk characteristics (by requiring that fund's disclose, for example, the following data: security categorizations as level 1, level 2, or level 3 measurements; more detailed information about securities at the time of purchase; liquidity metrics; and information about shareholder concentration). We believe that the additional information required should be readily available to funds as a matter of general business practice and therefore would not impose costs on money market funds other than those required to modify systems used to aggregate data and file reports on Form N–MFP. These costs are discussed in section III.H.6 below.

Our proposed new reporting requirements may improve informational efficiency by improving the transparency of potential risks in money market funds and promoting better-informed investment decisions, which, in turn, will lead to a better allocation of capital. Similarly, the increased transparency may promote competition as fund managers are exposed to external market discipline and better-informed investors who may be more likely to select an alternative investment if they are not comfortable with the risk-return profile of their fund. The newly disclosed information may cause some money market fund investors to exchange their assets between different money market funds, but because we do not have the information necessary to provide a reasonable estimate, we are unable to estimate this with specificity. In addition, some investors may exchange assets between money market funds and alternative investments or other segments of the short-term financing markets, but we are unable to estimate how frequently this will happen with specificity and we do not know how the other underlying assets compare with those of money market funds. Therefore, we are unable to estimate the overall net effect on capital formation. Nevertheless, we believe that the net effect will be small, especially during normal market conditions.

We request general comment on our proposed new reporting requirements.

- Do commenters agree that the information we would require is readily available to funds as a matter of general business practice? If not, are there other types of readily available data that would provide us with similar information?
- Are there costs associated with our proposed new reporting requirements (other than to make systems modifications discussed below) that we have not considered? If so, please describe the nature and amounts of those costs.
- Is there additional information that we have not identified that could be useful to us or investors in monitoring money market funds? How should such information be reported?

3. Clarifying Amendments

We are proposing (regardless of the alternative proposal adopted, if any) several amendments to clarify current instructions and items of Form N–MFP. Revising the form to include these clarifications should improve the ability of fund managers to complete the form and improve the quality of the data they submit to us.[781] We believe that many of our proposed clarifying amendments are consistent with current filing practices.[782]

We understand that some fund managers compile the fund's portfolio holdings information as of the last calendar day of the month, even if that day falls on a weekend or holiday. To provide flexibility, we propose to amend the instructions to Form N–MFP to clarify that, unless otherwise specified, a fund may report information on Form N–MFP as of the last business day *or* any later calendar day of the month.[783] We also propose to revise the

[778] We also propose to clarify that the maturity date required to be reported in current Form—N–MFP Item 35 is the maturity date used to calculate WAM under proposed (FNAV and Fees & Gates) rule 2a–7(d)(1)(ii) (*see* proposed Form N–MFP Item C.11) and the maturity date required to be reported in current Form—N–MFP Item 36 is the final legal maturity date, *i.e.,* the date on which, in accordance with the terms of the security without regard to any interest rate readjustment or demand feature, the principal amount must unconditionally be paid (*see* proposed Form N–MFP Item C.13). The final legal maturity date, as clarified, will help us distinguish between debt securities that are issued by the same issuer.

[779] We propose to amend the investment categories in proposed Form N–MFP Item C.6 to include new categories: ''Non U.S. Sovereign Debt,'' ''Non-U.S. Sub-Sovereign Debt,'' ''Other Asset-Backed Security,'' ''Non-Financial Company Commercial Paper'' (instead of ''Other Commercial Paper''), and ''Collateralized Commercial Paper,'' and amend ''*U.S.* Government Agency Debt'' and ''Certificate of Deposit (including Time Deposits *and Euro Time Deposits*).'' The new investment categories would help Commission staff identify particular exposures that otherwise are often reported in other less descriptive categories (*e.g.,* reporting sovereign debt as ''treasury debt'' or reporting asset-backed securities (that are not commercial paper) as ''other note'' or ''other instrument''). We note that a fund should only designate a security as ''U.S. Treasury Repurchase Agreement'' or ''Government Agency Repurchase Agreement'' when the underlying collateral is 100% Treasuries or Government Agency, respectively; otherwise, a fund should use the ''Other Repurchase Agreement'' category. We are also proposing to include a requirement that a fund disclose, where applicable, the period remaining until the principal amount of a security may be recovered through a demand feature and whether a security demand feature is conditional. Proposed Form N–MFP Items C.14.e. and C.14.f. These proposed amendments would improve the Commission's and investors' ability to evaluate and monitor a security's credit and default risk.

[780] Current Form N–MFP Item 35 (the maturity date taking into account the maturity shortening provisions of rule 2a–7(d), *i.e.,* ''WAM'') and Item 36 (the final legal maturity date taking into account any maturity date extensions that may be effected at the option of the issuer).

[781] We are proposing technical changes to the ''General Information'' section of the form that will clarify the circumstances under which a money market fund must complete certain question sub-parts. *See* proposed Form N–MFP Items 6 and 7.

[782] As discussed below, the proposed amendments are consistent with guidance our staff has provided to money market fund managers and service providers completing Form N–MFP.

[783] *See* proposed Form N–MFP General Instruction A (Rule as to Use of Form N–MFP); proposed rule 30b1–7. Our proposed approach is also consistent with a previous interpretation provided by our staff. *See* Staff Responses to Questions about Rule 30b1–7 and Form N–MFP, Question I.B.1 (revised July 29, 2011), *available at*

definition of ''Master-Feeder Fund'' to clarify that the definition of ''Feeder Fund'' includes unregistered funds (such as offshore funds).[784] Our proposed amendments also would clarify that funds should calculate the WAM and WAL reported on Form N–MFP using the same methods they use for purposes of compliance with rule 2a–7.[785] We also propose to require that funds disclose in Part B (Class-Level Information about the Fund) the required information for each class of the series, regardless of the number of shares outstanding in the class.[786]

We also are proposing to amend the reporting requirements for repurchase agreements by restating the item's requirements as two distinct questions.[787] The amendment would make clear that information about the securities subject to a repurchase agreement must be disclosed regardless of how the fund treats the acquisition of the repurchase agreement for purposes of rule 2a–7's diversification requirements.[788] Finally, we propose to amend the items in Form N–MFP that require information about demand features, guarantors, or enhancement providers to make clear that funds should disclose the identity of *each* demand feature issuer, guarantor, or enhancement provider and the amount (*i.e.,* percentage) of fractional support provided.[789] Our amendments also would clarify that a fund is not required to provide additional information about a security's demand feature(s) or guarantee(s) unless the fund is relying on the demand feature or guarantee to determine the quality, maturity, or liquidity of the security.[790]

As discussed above, our proposed clarifying amendments are intended to improve the quality of the data we receive on Form N–MFP by clarifying a number of reporting obligations so that all funds report information on Form N–MFP in a consistent manner. Accordingly, we do not believe that our proposed clarifying amendments would impose any new costs on funds other than those required to modify systems used to aggregate data and file reports on Form N–MFP. These costs are discussed in section III.H.6 below. Because our proposed clarifying amendments would not change funds' current reporting obligations, we believe there would be no effect on efficiency, competition, or capital formation.

We request comment on our proposed clarifying amendments.

- Is our understanding about current fund practices correct?
- Would our proposed amendments provide greater clarity and flexibility to funds? Are they consistent with current fund practices?
- Would our proposed amendments alter the manner in which data is currently reported to us on Form N–MFP, or alter the amount of data reported?
- Are there other clarifying amendments that we should consider that would improve the consistency and utility of the information reported on Form N–MFP to Commission staff and others?
- Should we adopt our proposed clarifying amendments even if we do not adopt either the floating NAV or liquidity fees and gates proposals?

4. Public Availability of Information

Currently, each money market fund must file information on Form N–MFP electronically within five business days after the end of each month and that information is made publicly available 60 days after the end of the month for which it is filed. We propose (regardless of the alternative proposal adopted, if any) to make Form N–MFP publicly available immediately upon filing.[791] The delay, which we instituted when we adopted the form in 2010, responded to commenters' concerns regarding potential reactions of investors to the disclosure of funds' portfolio information and shadow NAVs.[792] Although we did not believe that it was necessary to keep the portfolio information private for 60 days, we believed then that the shadow price data should not be made public immediately. However, we now believe that the immediate release of the shadow price

*http://www.sec.gov/divisions/investment/guidance/formn-mfpqa.htm.*

[784] *See* proposed Form N–MFP General Instruction E (defining ''Master-Feeder Fund,'' and defining ''Feeder Fund'' to include a registered or unregistered pooled investment vehicle). Form N–MFP requires that a master fund report the identity of any feeder fund. Our proposed amendment is designed to address inconsistencies in reporting of master-feeder fund data that we have observed in filings, and would help us determine the extent to which feeder funds, wherever located, hold a master fund's shares. The change would reflect how we understand data from master-feeder funds is collected by the Investment Company Institute for its statistical reports. We are also proposing to make grammatical and conforming amendments to proposed Form N–MFP Items A.7 and A.8.

[785] *See* proposed Form N–MFP Items A.11 and A.12 (defining ''WAM'' and ''WAL'' and cross-referencing the maturity terms to rule 2a–7). We also propose to amend the 7-day gross yield to require that the resulting yield figure be carried to (removing the words ''at least'') the nearest hundredth of one per cent and clarify that master and feeder funds should report the 7-day gross yield (current Form –N–MFP Item 17) at the master-fund level. Proposed Form N–MFP Item A.20. These proposed amendments are intended to achieve consistency in reporting and remove potential ambiguity for feeder funds when reporting the 7-day gross yield.

[786] *See* text before proposed Form N–MFP Item B.1. Our staff has found that funds inconsistently report fund class information, for example, when a fund does not report a fund class registered on Form N–1A because the fund class has no shares outstanding. Our proposed amendment is intended to clarify a fund's reporting obligations and provide Commission staff (and investors) with more complete information about each fund's capital structure.

[787] *See* proposed Form N–MFP Item C.7 (requiring that a fund disclose if it is treating the acquisition of a repurchase agreement as the acquisition of the underlying securities (*i.e.,* collateral) for purposes of portfolio diversification under rule 2a–7). *See* proposed Form N–MFP Item C.8 (requiring that a fund describe the securities subject to the repurchase agreement, including: (a) name of the *collateral* issuer; (b) CUSIP; (c) LEI (if available); (d) maturity date; (e) coupon or yield; (f) principal amount; (g) value of the collateral; and (h) the category of investments. We also propose to require that a fund specify whether the repurchase agreement is ''open'' (*i.e.,* by its terms, will be extended or ''rolled'' each business day unless the investor chooses to terminate it). This information should be readily available to funds and would enhance the ability of Commission staff and others to evaluate the risks (*e.g.,* rollover risk or the duration of the lending) presented by investments in repurchase agreements. *See* proposed Form N–MFP Item C.8.a. Our proposal would also provide a specific list of investment categories from which funds may choose, including new categories (Equity; Corporate Bond; Exchange Traded Fund; Trust Receipt (other than for U.S. Treasuries); and Derivative). Finally, our proposal would also clarify that a fund is required to disclose the name of the *collateral* issuer (and not the name of the issuer of the repurchase agreement). In addition, when disclosing a security's coupon or yield (as required in proposed Form N–MFP Item C.8.f), a fund would be required to report (i) the stated coupon rate, where the security is issued with a stated coupon; (ii) the interest rate at purchase, for instance, if the security is issued at a discount (without a stated coupon); and (iii) the coupon rate as of the Form N–MFP reporting date, if the security is floating or variable rate.

[788] We propose several other clarifications to other items. *See* proposed Form N–MFP Item 1 (amending the format of reporting date provided by funds); and proposed Form N–MFP Item A.10 (modifying, for consistency, the names of money market fund categories).

[789] *See* proposed Form N–MFP Items C.14–C.16.

[790] Form N–MFP already requires that a fund disclose only security enhancements on which the fund is relying to determine the quality, maturity, or liquidity of the security. *See* current Form N–MFP Item 39. Similarly, we propose to amend current Form N–MFP Items 37 (demand features) and 38 (guarantees) to make clear that funds are required to disclose information relating to demand features and guarantees only when the fund is relying on these features to determine the quality, maturity, or liquidity of the security. *See* proposed Form N–MFP Items C.14 and C.15.

[791] *See* proposed rule 30b1–7 (eliminating subsection (b), public availability).

[792] *See* 2010 Adopting Release, *supra* note 92, at section II.E.2 (noting that there may be less need in the future to require a 60-day delay). Commenters also objected to the disclosure of information filed on Form N–MFP because of the competitive effects on funds or fund managers. In the adopting release, we stated our belief that the competitive risks were overstated by commenters. We noted that the risks of trading ahead of funds (''front running'') or ''free riding'' on a fund's investment strategies were minimal because of the short-term nature of money market fund investments and the restricted universe of eligible portfolio securities.

data would not be harmful. This is based, in part, on our understanding that many money market funds now disclose their shadow prices every business day on their Web sites. Therefore we propose (under both alternatives we are proposing today) to eliminate the 60-day delay in making the information on the form publicly available.[793]

Eliminating the 60-day delay would provide more timely information to the public and greater transparency of money market fund information, which could promote efficiency. This disclosure could also make the monthly disclosure on Form N–MFP more relevant to investors, financial analysts, and others by improving their ability to more timely assess potential risks and make informed investment decisions. In other words, investors may be more likely to use the reported information because it is more timely and informative. In response to this potential heightened sensitivity of investors to the reported information, some funds might move toward more conservative investment strategies to reduce the chance of having to report bad outcomes. Because, as discussed above, shadow prices (which were a primary reason why we adopted the 60-day delay in making filings public) have been disclosed by a number of money market funds since February 2013 without incident, we do not believe that eliminating the 60-day delay would affect capital formation. We request comment on this aspect of our proposal.

- Do commenters believe that our five-day filing deadline continues to be appropriate? Should the filing delay be shorter or longer? Please provide support for any suggested change to the filing deadline.
- Do commenters agree that there have not been adverse impacts from recent publication of daily shadow NAVs by a number of large money market funds?
- Is a 60-day delay in making the information public still necessary to protect against possible ''front running'' or ''free riding?'' Have any developments occurred that should cause us to reconsider our 2010 decision that the information required to be disclosed would not be competitively sensitive?
- Would a shorter delay (45, 30, or 15 days) be more appropriate? If so, why?
- Do commenters agree with our estimated impact on efficiency, competition, and capital formation?
- Should we adopt our proposed amendment to eliminate the 60-day delay even if we do not adopt either the floating NAV or liquidity fees and gates proposals?

5. Request for Comment on Frequency of Filing

To increase further the transparency of money market funds and the utility of information disclosed, the Commission requests comment (regardless of the alternative proposal adopted, if any) on increasing the frequency of filing Form N–MFP from monthly to weekly. Given the rapidly changing composition of money market fund portfolios and increased emphasis on portfolio liquidity (*i.e.,* shortened maturities),[794] the information provided on Form N–MFP may become stale and less relevant. We believe that increasing the frequency of disclosure, as well as eliminating the 60-day delay in making information on Form N–MFP publicly available (discussed above), would further increase transparency into money market funds and make the information more relevant to investors, academic researchers, financial analysts, and economic research firms. We note that, under our floating NAV proposal, more frequent disclosure on Form N–MFP could also facilitate more accurate market-based valuations.[795] While we do not have the information necessary to provide a point estimate of the additional costs that may be imposed on funds because of more frequent filings of reports on Form N–MFP, we believe that the increased costs per fund would be negligible because most funds use a licensed software solution (either directly or through a third-party service provider) and would experience significant economies of scale.[796] Despite the incremental increase in costs to file the report more frequently, more timely and relevant data may increase competition and efficiency for the same reasons discussed above with respect to our proposed amendment to eliminate the 60-day delay.

We request comment on increasing the frequency of the filing of Form N–MFP.

- Do commenters agree with our analysis of the benefits and costs associated with increasing the frequency of disclosure of reports on Form N–MFP? Why or why not?
- Would increasing the frequency of reporting affect the investment strategies employed by fund managers, for example, causing managers to increase risk taking?
- Would fund managers be more likely to ''front-run'' or reverse engineer another fund's portfolio strategy?
- Would increasing the frequency of disclosure affect the costs or benefits associated with our proposed amendment to eliminate the 60-day delay in public availability? If so, how?
- What types of costs would funds incur to change from monthly to weekly filing of reports on Form N–MFP? Would funds have sufficient time to evaluate and validate data received from outside vendors?
- Should we increase the filing frequency even if we do not adopt either the floating NAV or liquidity fees and gates proposals?

6. Operational Implications

We anticipate that fund managers would incur costs to gather the new items of information we propose to require on Form N–MFP. To reduce costs, we have decided to propose needed improvements to the form at the same time we are proposing amendments necessitated by the amendments to rule 2a–7 we are proposing. We note that our proposed clarifying amendments should not affect, or should only minimally affect, current filing obligations or the information content of the filings.

We expect that the operational costs to money market funds to report the information required in proposed Form N–MFP would be the same costs we discuss in the Paperwork Reduction Act analysis in section IV of the Release, below. As discussed in more detail in that section, our staff estimates that our proposed amendments to Form N–MFP would result in, at the outside range, a first-year aggregate additional 49,810 burden hours at a total cost of $12.9 million plus $373,680 in total external costs (which represent fees to license a software solution and fees to retain a

[793] A number of large fund complexes have begun (or plan) to disclose daily money market fund market valuations (*i.e.,* shadow prices), including BlackRock, Charles Schwab, Federated Investors, Fidelity Investments, Goldman Sachs, J.P. Morgan, Reich & Tang, and State Street Global Advisors. *See, e.g., Money Funds' New Openness Unlikely to Stop Regulation,* Wall St. J. (Jan. 30, 2013).

[794] The RSFI Study notes that as of November 30, 2012, the typical prime fund held over 25% of its portfolio in daily liquid assets (''DLA'') (with 10% DLA required under rule 2a–7) and nearly 50% of its portfolio in weekly liquid assets (''WLA'') (with 30% WLA required under rule 2a–7). *See* RSFI Study, *supra* note 21, at 20.

[795] *See supra* note 767 and accompanying text.

[796] Staff estimates that our proposed amendments to Form N–MFP (12 filings per year) would result in, at the outside range, a first-year aggregate additional 49,810 total burden hours at a total cost of $12.9 million, and external costs of $373,680. *See infra* section IV.A.3. We expect that funds would incur substantially lower costs that those described above if we were to require that reports on Form N–MFP be filed weekly, rather than monthly as currently required.

third-party service provider).[797] Our operational cost estimates are based on our floating NAV proposal, but would not change if we instead adopted our liquidity fees and gates alternative proposal.

We request comment on our analysis of operational implications summarized above and described in detail in sections IV.A.3 and IV.B.3 below. We also request comment on the costs and benefits described above, including whether any proposed disclosure requirements are unduly burdensome or would impose unnecessary costs.

*I. Amendments to Form PF Reporting Requirements*

The Commission is proposing to amend Form PF, the form that certain investment advisers registered with the Commission use to report information regarding the private funds they manage, including ''liquidity funds,'' which are private funds that seek to maintain a stable NAV (or minimize fluctuations in their NAVs) and thus can resemble money market funds.[798] We adopted Form PF, as required by the Dodd-Frank Act,[799] to assist FSOC in its monitoring and assessment of systemic risk; to provide information for FSOC's use in determining whether and how to deploy its regulatory tools; and to collect data for use in our own regulatory program.[800] As discussed in more detail below, FSOC and the Commission have recognized the risks that may be posed by cash management products other than money market funds, including liquidity funds, and the potentially increased significance of such products in the event we adopt further money market fund reforms such as those we propose today.[801] Therefore, to enhance FSOC's ability to monitor and assess systemic risks in the short-term financing markets and to facilitate our oversight of those markets and their participants, we propose today to require large liquidity fund advisers—registered advisers with $1 billion or more in combined money market fund and liquidity fund assets—to file virtually the same information with respect to their liquidity funds' portfolio holdings on Form PF as money market funds are required to file on Form N–MFP.[802]

We share the concern expressed by some commenters that, if further money market fund reforms cause investors to seek alternatives to money market funds, including private funds that seek to maintain a stable NAV but that are not registered with the Commission, this shift could reduce transparency of the potential purchasers of short-term debt instruments, and potentially increase systemic risk.[803] We discuss in detail the potential for money market fund investors to reallocate their assets to alternative investments in section III.E above. The amendments that we propose to Form PF today are designed to achieve two primary goals. First, they are designed to ensure to the extent possible that any further money market fund reforms do not decrease transparency in the short-term financing markets, and to better enable FSOC to monitor and address any related systemic risks and to better enable us to develop effective regulatory policy responses to any shift in investor assets. Second, the proposed amendments to Form PF are designed to allow FSOC and us to more effectively administer our regulatory programs even if investors do not shift their assets as a result of any further money market fund reforms, as the increased transparency concerning liquidity funds, combined with information we already collect on Form N–MFP, will provide a more complete picture of the short-term financing markets in which liquidity funds and money market funds both invest.

1. Overview of Proposed Amendments to Form PF

Our proposal would apply to large liquidity fund advisers, which generally are SEC-registered investment advisers that advise at least one liquidity fund

[797] *See infra* section IV.A.3.

[798] For purposes of Form PF, a ''liquidity fund'' is any private fund that seeks to generate income by investing in a portfolio of short term obligations in order to maintain a stable net asset value per unit or minimize principal volatility for investors. *See* Glossary of Terms to Form PF.

[799] *See Reporting by Investment Advisers to Private Funds and Certain Commodity Pool Operators and Commodity Trading Advisors on Form PF,* Investment Advisers Act Release No. 3308 (Oct. 31, 2011) [76 FR 71128 (Nov. 16, 2011)] (''Form PF Adopting Release'') at section I. Form PF is a joint form between the Commission and the CFTC only with respect to sections 1 and 2 of the Form; section 3, which we propose to amend, and section 4, were adopted only by the Commission. *Id.*

[800] FSOC's regulatory tools include, for example, designating nonbank financial companies that may pose risks to U.S. financial stability for supervision by the Board of Governors of the Federal Reserve System, and issuing recommendations to primary financial regulators for more stringent regulation of financial activities that FSOC determines may create or increase systemic risk. Although Form PF is primarily intended to assist FSOC in its monitoring obligations under the Dodd-Frank Act, we also may use information collected on Form PF in our regulatory program, including examinations, investigations, and investor protection efforts relating to private fund advisers. *See* Form PF Adopting Release, *supra* note 799, at sections II and VI.A.

[801] *See infra* note 816 and accompanying text.

[802] We propose to incorporate in a new Question 63 in section 3 of Form PF the substance of virtually all of the questions on Part C of Form N–MFP as we propose to amend that form, except that we have modified the questions where appropriate to reflect that liquidity funds are not subject to rule 2a–7 (although some liquidity funds have a policy of complying with rule 2a–7's risk-limiting conditions) and have not added questions that would parallel Items C.7 and C.9 of Form N–MFP. We do not propose to include a question that would parallel Item C.7 because that item relates to whether a money market fund is treating the acquisition of a repurchase agreement as the acquisition of the collateral for purposes of rule 2a–7's diversification testing; liquidity funds, in contrast, are not subject to rule 2a–7's diversification limitations, and the information on repurchase agreement collateral we propose to collect through new Question 63(g) on Form PF would allow us to better understand liquidity funds' use of repurchase agreements and their collateral. Item C.9 asks whether a portfolio security is a rated first tier security, rated second tier security, or no longer an eligible security. We did not include a parallel question in Form PF because these concepts would not necessarily apply to liquidity funds, and we believe the additional questions on Form PF would provide sufficient information about a portfolio security's credit quality and the large liquidity fund adviser's use of credit ratings.

[803] *See, e.g.,* Dreyfus FSOC Comment Letter, *supra* note 174 (opposing a floating NAV and citing adverse redistribution of systemic risk); Dreyfus 2009 Comment Letter, *supra* note 350 (opposing a floating NAV and stating that, after surveying 37 of its largest institutional money market fund shareholders (representing over $60 billion in assets) regarding a floating NAV, 67% responded that their business could not continue to invest in a floating NAV product and that they would have to seek an alternative investment option); Nat. Assoc. of State Treasurers PWG Comment Letter, *supra* note 567 (opposing a floating NAV because, among other reasons, ''a floating NAV would push investors to less regulated or non-regulated markets''); AFP Jan. 2011 PWG Comment Letter, *supra* note 567 (reporting results of a survey of its members reflecting that four out of five organizations would likely move at least some of their assets out of money market funds if the funds were required to use floating NAVs, with 22% reporting that they would move their money market fund investments to ''fixed-value investment vehicles (*e.g.,* offshore money market funds, enhanced cash funds and stable value vehicles)''); ICI Apr 2012 PWG Comment Letter, *supra* note 62 (enclosing a survey commissioned by the Investment Company Institute and conducted by Treasury Strategies, Inc. finding, among other things, that if the Commission were to require money market funds to use floating NAVs, 79% of the 203 corporate, government, and institutional investors that responded to the survey would decrease their money market fund investments or stop using the funds); Federated Investors Alternative 1 FSOC Comment Letter, *supra* note 161 (stating that requiring money market funds to use floating NAVs, among other things, ''would cause investors to move liquidity balances elsewhere,'' including to ''to bank-sponsored short-term investment funds, hedge funds and offshore investment vehicles that are less transparent, less regulated, less efficient and result in the same 'roll-over risk' for issuers in the money markets that the Council apparently wants to ameliorate through its plan to change the structure of MMFs''); ICI Jan. 24 FSOC Comment Letter, *supra* note 25 (stating that if money market funds were required to use floating NAVs, ''[i]t is very likely that institutional investors would continue to seek out diversified investment pools that strive to maintain a stable value'' and that ''[m]ost of these pools are not regulated under the Investment Company Act—and some of them lie beyond the jurisdictional reach of U.S. regulators'').

and manage, collectively with their related persons, at least $1 billion in combined liquidity fund and money market fund assets.[804] Large liquidity fund advisers today are required to file information on Form PF quarterly, including certain information about each liquidity fund they manage.[805] Under our proposal, for each liquidity fund it manages, a large liquidity fund adviser would be required to provide, quarterly and with respect to each portfolio security, the following information for each month of the reporting period:[806]

- The name of the issuer;
- The title of the issue;
- The CUSIP number;
- The legal entity identifier or LEI, if available;
- At least one of the following other identifiers, in addition to the CUSIP and LEI, if Available: ISIN, CIK, or any other unique identifier;
- The category of investment (*e.g.,* Treasury debt, U.S. government agency debt, Asset-backed commercial paper, certificate of deposit, repurchase agreement[807]);
- If the rating assigned by a credit rating agency played a substantial role in the liquidity fund's (or its adviser's) evaluation of the quality, maturity or liquidity of the security, the name of each credit rating agency and the rating each credit rating agency assigned to the security;
- The maturity date used to calculate weighted average maturity;
- The maturity date used to calculate weighted average life;
- The final legal maturity date;
- Whether the instrument is subject to a demand feature, guarantee, or other enhancements, and information about any of these features and their providers;
- For each security, reported separately for each lot purchased, the total principal amount; the purchase date(s); the yield at purchase and as of the end of each month during the reporting period for floating or variable rate securities; and the purchase price as a percentage of par;
- The value of the fund's position in the security and, if the fund uses the amortized cost method of valuation, the amortized cost value, in both cases with and without any sponsor support;
- The percentage of the liquidity fund's assets invested in the security;
- Whether the security is categorized as a level 1, 2, or 3 asset or liability on Form PF;[808]
- Whether the security is an illiquid security, a daily liquid asset, and/or a weekly liquid asset, as defined in rule 2a–7; and
- Any explanatory notes.[809]

We also propose to remove current Questions 56 and 57 on Form PF. These questions generally require large liquidity fund advisers to provide information about their liquidity funds' portfolio holdings broken out by asset class (rather than security by security). We and FSOC would be able to derive the information currently reported in response to those questions from the new portfolio holdings information we propose to require advisers to provide. We also are proposing to require large liquidity fund advisers to provide information about any securities sold by their liquidity funds during the reporting period, including sale and purchase prices.[810] Finally, we propose to require large liquidity fund advisers to identify any money market fund advised by the adviser or its related persons that pursues substantially the same investment objective and strategy and invests side by side in substantially the same positions as a liquidity fund the adviser reports on Form PF.[811]

2. Utility of New Information, Including Benefits, Costs, and Economic Implications

The amendments that we propose today are designed to enhance FSOC's ability to fulfill its mission, and thereby to facilitate FSOC's ability to take measures to protect the U.S. economy from significant harm from future financial crises.[812] As we have explained, the information that advisers today must report on Form PF concerning their liquidity funds is designed to assist FSOC in assessing the risks undertaken by liquidity funds, their susceptibility to runs, and how their investments might pose systemic risks either among liquidity funds or through contagion to registered money market funds.[813] The information that advisers must report today also is intended to aid FSOC in its determination of whether and how to deploy its regulatory tools.[814] Finally, the information that advisers must report today is designed to assist FSOC in assessing the extent to which a liquidity fund is being managed consistent with restrictions imposed on registered money market funds that might mitigate their likelihood of posing systemic risk.[815]

We believe, based on our staff's consultations with staff representing the members of FSOC, that the additional information we propose to require advisers to report on Form PF will assist FSOC in carrying out these responsibilities. FSOC and the

[804] An adviser is a large liquidity fund adviser if it has at least $1 billion combined liquidity fund and money market fund assets under management as of the last day of any month in the fiscal quarter immediately preceding its most recently completed fiscal quarter. *See* Form PF: Instruction 3 and Section 3. This $1 billion threshold includes assets managed by the adviser's related persons, except that an adviser is not required to include the assets managed by a related person that is separately operated from the adviser. *Id.* An adviser's related persons include persons directly or indirectly controlling, controlled by, or under common control with the investment adviser. *See* Form PF: Glossary of Terms (defining the term ''related person'' by reference to Form ADV). Generally, a person is separately operated from an investment adviser if the adviser: (1) Has no business dealings with the related person in connection with advisory services the adviser provides to its clients; (2) does not conduct shared operations with the related person; (3) does not refer clients or business to the related person, and the related person does not refer prospective clients or business to the adviser; (4) does not share supervised persons or premises with the related person; and (5) has no reason to believe that its relationship with the related person otherwise creates a conflict of interest with the adviser's clients. *See* Form PF: Glossary of Terms (defining the term by reference to Form ADV).

[805] *See* Form PF: Instruction 3 and Section 3.

[806] *See* Question 63 of proposed Form PF. Advisers would be required to file this information with their quarterly liquidity fund filings with data for the quarter broken down by month. Advisers would not be required to file information on Form PF more frequently as a result of today's proposal because large liquidity fund advisers already are required to file information each quarter on Form PF. *See* Form PF: Instruction 9.

[807] For repurchase agreements we are also proposing to require large liquidity fund advisers to provide additional information regarding the underlying collateral and whether the repurchase agreement is ''open'' (*i.e.,* whether the repurchase agreement has no specified end date and, by its terms, will be extended or ''rolled'' each business day (or at another specified period) unless the investor chooses to terminate it).

[808] *See* Question 14 of Form PF. *See also infra* notes 758–761 and accompanying and following text.

[809] We also propose to define the following terms in Form PF: Conditional demand feature; credit rating agency; demand feature; guarantee; guarantor; and illiquid security. *See* proposed Form PF: Glossary of Terms.

[810] *See* Question 64 of proposed Form PF. *See also supra* notes 766–767 and accompanying text.

[811] *See* Question 65 of proposed Form PF. This question is based on the current definition of a ''parallel fund structure'' in Form PF. *See* Glossary of Terms to Form PF (defining a ''parallel fund structure'' as ''[a] structure in which one or more private funds (each, a 'parallel fund') pursues substantially the same investment objective and strategy and invests side by side in substantially the same positions as another private fund'').

[812] *See* Form PF Adopting Release, *supra* note 799, at nn.455–457 and accompanying and following text (explaining that ''Congress responded to the recent financial crisis, in part, by establishing FSOC as the center of a framework intended 'to prevent a recurrence or mitigate the impact of financial crises that could cripple financial markets and damage the economy' ''; the goal of this framework, we explained, ''is the avoidance of significant harm to the U.S. economy from future financial crises'') (internal citations omitted).

[813] *See* Form PF Adopting Release, *supra* note 799, at section II.C.3.

[814] *Id.*

[815] *Id.*

Commission have recognized the risks that may be posed by cash management products other than money market funds, including liquidity funds, and the potentially increased significance of such products in the event we adopt further money market fund reforms such as those we propose today.[816] FSOC also stated that it and its members ''intend to use their authorities, where appropriate and within their jurisdictions, to address any risks to financial stability that may arise from various products within the cash management industry in a consistent manner,'' as ''[s]uch consistency would be designed to reduce or eliminate any regulatory gaps that could result in risks to financial stability if cash management products with similar risks are subject to dissimilar standards.'' [817] We expect, therefore, that requiring advisers to provide additional information on Form PF as we propose today would enhance FSOC's ability to assess systemic risk across the short-term financing markets.

We propose to require only large liquidity fund advisers to report this additional information for the same reason that we previously determined to require these advisers to provide more comprehensive information on Form PF: So that the group of private fund advisers filing more comprehensive information on Form PF will be relatively small in number but represent a substantial portion of the assets of their respective industries.[818] Based on information filed on Form PF and Form ADV, as of February 28, 2013, we estimate that there were approximately 25 large liquidity fund advisers (out of 55 total advisers that advise at least one liquidity fund), with their aggregate liquidity fund assets under management representing approximately 98% of liquidity fund assets managed by advisers registered with the Commission.

This threshold also should minimize the costs of our proposed amendments because large liquidity fund advisers already are required to make quarterly reports on Form PF and, as of February 28, 2013, virtually all either advise a money market fund or have a related person that advises a money market fund. Requiring large liquidity fund advisers to provide substantially the same information required by Form N–MFP therefore may reduce the burdens associated with our proposal, which we discuss below, because large liquidity fund advisers generally already have (or may be able to obtain access to) the systems, service providers, and/or staff necessary to capture and report the same types of information for reporting on Form N–MFP. These same systems, service providers, and/or staff may allow large liquidity fund advisers to comply with our proposed changes to Form PF more efficiently and at a reduced cost than if we were to require advisers to report information that differed materially from that which the advisers must file on Form N–MFP.

In addition to our concerns about FSOC's ability to assess systemic risk, we also are concerned about losing transparency regarding money market fund investments that may shift into liquidity funds if we were to adopt the money market reforms we propose today and our ability effectively to formulate policy responses to such a shift in investor assets.[819] We note in particular that a run on liquidity funds could spread to money market funds because, for example, both types of funds often invest in the same securities as noted above.[820] Our ability to formulate a policy response to address this risk could be diminished if we had less transparency concerning the portfolio holdings of liquidity funds as compared to money market funds, and thus were not able as effectively to assess the degree of correlation between various funds or groups of funds that invest in the short-term financing markets, or if we were unable proactively to identify funds that own distressed securities. Indeed, Form PF, by defining large liquidity fund advisers subject to more comprehensive reporting requirements as advisers with $1 billion in *combined* money market fund and liquidity fund assets under management today reflects the similarities between money market funds and liquidity funds and the need for comprehensive information concerning advisers' management of large amounts of short-term assets through either type of fund. The need for this comprehensive data would be heightened if money market fund investors shift their assets to liquidity funds in response to any further money market fund reforms.

Finally, this increased information on liquidity funds managed by large liquidity fund advisers also would be useful to us and FSOC even absent a shift in money market fund investor assets. Collecting this information about these liquidity funds would, when combined with information collected on Form N–MFP, provide us and FSOC a more complete picture of the short-term financing markets, allowing each of us to more effectively fulfill our statutory

[816] *See* FSOC Proposed Recommendations, *supra* note 114, at 7 (''The Council recognizes that regulated and unregulated or less-regulated cash management products (such as unregistered private liquidity funds) other than MMFs may pose risks that are similar to those posed by MMFs, and that further MMF reforms could increase demand for non-MMF cash management products. The Council seeks comment on other possible reforms that would address risks that might arise from a migration to non-MMF cash management products.'') We, too, have recognized that ''[l]iquidity funds and registered money market funds often pursue similar strategies, invest in the same securities and present similar risks.'' *See* Form PF Adopting Release, *supra* note 799, at section II.A.4. *See also Reporting by Investment Advisers to Private Funds and Certain Commodity Pool Operators and Commodity Trading Advisors on Form PF,* Investment Advisers Act Release No. 3145 (Jan. 26, 2011) [76 FR 8068 (Feb. 11, 2011)] (''Form PF Proposing Release''), at n.68 and accompanying text (explaining that, ''[d]uring the financial crisis, several sponsors of 'enhanced cash funds,' a type of liquidity fund, committed capital to those funds to prevent investors from realizing losses in the funds,'' and noting that ''[t]he fact that sponsors of certain liquidity funds felt the need to support the stable value of those funds suggests that they may be susceptible to runs like registered money market funds''). *See generally supra* notes 113–118 and accompanying text.

[817] *See* FSOC Proposed Recommendations, *supra* note 114, at 7. The President's Working Group on Financial Markets reached a similar conclusion, noting that because vehicles such as liquidity funds ''can take on more risks than MMFs, but such risks are not necessarily transparent to investors . . . , unregistered funds may pose even greater systemic risks than MMFs, particularly if new restrictions on MMFs prompt substantial growth in unregistered funds.'' *See* PWG Report, *supra* note 111, at 21. The potentially increased risks posed by liquidity funds were of further concern because these risks ''are difficult to monitor, since [unregistered cash management products like liquidity funds] provide far less market transparency than MMFs.'' *Id.* at 35.

[818] *See* Form PF Adopting Release, *supra* note 799, at n.88 and accompanying text.

[819] *See, e.g.,* RSFI Study, *supra* note 21, at section 4.C (analysis of investment alternatives to money market funds, considering, among other issues, the potential for investors to shift their assets to money market fund alternatives, including liquidity funds, in response to further money market fund reforms and certain implications of a shift in investor assets).

[820] Liquidity funds may generally have a more institutional shareholder base because the funds rely on exclusions from the Investment Company Act's definition of ''investment company'' provided by section 3(c)(1) or 3(c)(7) of that Act. *See* section 202(a)(29) of the Advisers Act (defining the term ''private fund'' to mean ''an issuer that would be an investment company, as defined in section 3 of the Investment Company Act (15 U.S.C. 80a–3), but for section 3(c)(1) or 3(c)(7) of that Act''). Funds relying on those exclusions sell their shares in private offerings which in many cases are restricted to investors who are ''accredited investors'' as defined in rule 501(a) under the Securities Act. Investors in funds relying on section 3(c)(7), in addition, generally must be ''qualified purchasers'' as defined in section 2(a)(51) of the Investment Company Act. The funds' more institutional shareholder base may increase the potential for a run to develop at a liquidity fund. As discussed in greater detail in section II.C of this Release, redemption data from the 2007–2008 financial crisis show that some institutional money market fund investors are likely to redeem from distressed money market funds more quickly than other investors and to redeem a greater percentage of their holdings. This may be indicative of the way institutional investors in liquidity funds would behave, particularly liquidity funds that more closely resemble money market funds.

mandates. For example, the contagion risk we discuss above—of a run starting in a liquidity fund and spreading to money market funds—may warrant our or FSOC's attention even today. But it may be impossible effectively to assess this risk today without more detailed information about the portfolio holdings of the liquidity funds managed by advisers who manage substantial amounts of short-term investments and the ability to combine that data with the information we collect on Form N–MFP.

For example, if a particular security or issuer were to come under stress, our staff today would be unable to determine which liquidity funds, if any, held that security. This is because advisers currently are required only to provide information about the types of assets their liquidity funds hold, rather than the individual positions.[821] Our staff could see the aggregate value of all of a liquidity fund's positions in unsecured commercial paper issued by non-U.S. financial institutions, for example, but could not tell whether the fund owned commercial paper issued by any particular non-U.S. financial institution. If a particular institution were to come under stress, the aggregated information available today would not allow us or our staff to determine the extent to which liquidity funds were exposed to the financial institution; lacking this information, neither we nor our staff would be able as effectively to assess the risks across the liquidity fund industry and, by extension, the short-term financing markets.

Position level information for liquidity funds managed by large liquidity fund advisers also could allow our staff more efficiently and effectively to identify longer-term trends in the industry and at particular liquidity funds or advisers. The aggregated position information that advisers provide today may obscure the level of risk in the industry or at particular advisers or liquidity funds that, if more fully understood by our staff, could allow the staff to more efficiently and effectively target their examinations and enforcement efforts, and could better inform the staff's policy recommendations.

Indeed, our experience with the portfolio information money market funds report on Form N–MFP—which was limited at the time we adopted Form PF—has proved useful in our regulation of money market funds in these and other ways and has informed this proposal.[822] During the 2011 Eurozone debt crisis, for example, we and our staff benefitted from the ability to determine which money market funds were exposed to specific financial institutions (and other positions) and from the ability to see how funds changed their holdings as the crisis unfolded. This information was useful in assessing risk across the industry and at particular money market funds. Given the similarities between money market funds and liquidity funds and the possibility for risk to spread between the groups of funds, our experience with portfolio information filed on Form N–MFP suggests that virtually the same information for liquidity funds managed by large liquidity fund advisers would provide significant benefits for us and FSOC.

For all of these reasons and as discussed above, we expect that requiring large liquidity fund advisers to report their liquidity funds' portfolio information on Form PF as we propose would provide substantial benefits for us and FSOC, including positive effects on efficiency and capital formation. If this additional information allows FSOC more effectively to monitor systemic risk as intended, our proposed amendments to Form PF could benefit the broader U.S. economy, with positive effects on capital formation, to the extent FSOC is better able to protect the U.S. economy from significant harm from future financial crises.

In addition, as we explained in more detail when adopting Form PF, requiring advisers to report on Form PF is intended to positively affect efficiency and capital formation, in part by enhancing our ability to evaluate and develop regulatory policies and to more effectively and efficiently protect investors and maintain fair, orderly and efficient markets.[823] We explained, for example, that Form PF data was designed to allow us to more efficiently and effectively target our examination programs and, with the benefit of Form PF data, to better anticipate regulatory problems and the implications of our regulatory actions, and thereby to increase investor protection.[824] We also explained that Form PF data could have a positive effect on capital formation because, as a result of the increased transparency to regulators made possible by Form PF, private fund advisers might assess more carefully the risks associated with particular investments and, in the aggregate, allocate capital to investments with a higher value to the economy as a whole.[825]

The Form PF amendments that we propose today are designed to increase the same benefits we identified when we adopted Form PF, although we are unable to quantify them because their extent depends on future events that we cannot predict (*e.g.,* the nature and extent of any future financial crisis and the role that Form PF data could play in mitigating or averting it). The additional information on Form PF may better inform our understanding of the activities of liquidity funds and their advisers and the operation of the short-term financing markets, including risks that may arise in liquidity funds and harm other participants in those markets or those who rely on them—including money market funds and their shareholders and the companies and governments who seek financing in the short-term financing markets. The additional information we propose to require advisers to report on Form PF, particularly when combined with similar data reported on Form N–MFP, therefore may enhance our ability to evaluate and develop regulatory policies and enable us to more effectively and efficiently protect investors and maintain fair, orderly, and efficient markets. By further increasing transparency to regulators, the proposed amendments also could increase capital formation if private fund advisers, as a result, ultimately allocate capital to investments with a higher value to the economy as a whole, as discussed above. We note, however, that any effects on capital formation from increased transparency to regulators, positive and negative, likely would be less significant than those associated with our adoption of Form PF. This is because today's proposal would provide an incremental increase in transparency as opposed to the larger increase in transparency created by the adoption of Form PF in the first instance.

[821] *See* Question 56 of Form PF (requiring advisers to provide exposures and maturity information, by asset class, for liquidity fund assets under management); Question 57 of Form PF (requiring advisers to provide the asset class and percent of the fund's NAV for each open position that represents 5% or more of the fund's NAV).

[822] Money market funds were required to begin filing information on Form N–MFP by December 7, 2010. *See* 2010 Adopting Release, *supra* note 92, at n.340 and accompanying text. Form PF was proposed shortly thereafter on January 26, 2011, and adopted on October 31, 2011. *See* Form PF Proposing Release, *supra* note 816; Form PF Adopting Release, *supra* note 799.

[823] *See generally* Form PF Adopting Release, *supra* note 799, at section V.A (explaining that, in addition to assisting FSOC fulfill its mission, ''we expect this information to enhance [our] ability to evaluate and develop regulatory policies and improve the efficiency and effectiveness of our efforts to protect investors and maintain fair, orderly and efficient markets'').

[824] *See* Form PF Adopting Release, *supra* note 799, at section V.A.

[825] *See id.* at text accompanying and following n.494.

For these same reasons we believe that requiring large liquidity fund advisers to provide portfolio-level information is justified, and that it would be most beneficial and efficient to require large liquidity fund advisers to file virtually the same information for their liquidity funds as money market funds are required to file on Form N–MFP. We considered whether we and FSOC would be able as effectively to carry out our respective missions as discussed above using the information large liquidity fund advisers currently must file on Form PF. But as we discuss above, we expect that requiring large liquidity funds advisers to provide portfolio holdings information would provide a number of benefits and would allow us and FSOC to better understand the activities of large liquidity fund advisers and their liquidity funds than would be possible with the higher level, aggregate information that advisers file today on Form PF (*e.g.,* the ability to determine which liquidity funds own a distressed security).

For the reasons discussed above we also considered, but ultimately chose not to propose, requiring advisers to file portfolio information about their liquidity funds that differs from the information money market funds are required to file on Form N–MFP. Generally, different portfolio holdings information could be less useful than the types of information money market funds file on Form N–MFP, given our experience with Form N–MFP data, and could be more difficult to combine with Form N–MFP data. Requiring advisers to file on Form PF virtually the same information money market funds file on Form N–MFP also could be more efficient for advisers and reduce the costs of reporting.

Finally, we considered whether to propose to require large liquidity fund advisers to provide their liquidity funds' portfolio information more frequently than quarterly. Monthly filings, for example, would provide us and FSOC more current data and could facilitate our combining the new information with the information money market funds file on Form N–MFP (which money market funds file each month). We balanced the potential benefits of more frequent reporting against the costs it would impose and believe, at this time, that quarterly reporting may be more appropriate.[826]

We recognize, however, that our proposed amendments to Form PF, while limited to large liquidity fund advisers, would create costs for those advisers, and also could affect competition, efficiency, and capital formation. We expect that the operational costs to advisers to report the new information would be the same costs we discuss in the Paperwork Reduction Act analysis in section IV below. As discussed in more detail in that section, our staff estimates that our proposed amendments to Form PF would result in an annual aggregate additional 7,250 burden hours at a time cost of $1,836,500, plus $409,350 in total external costs (which represent fees to license a software solution and fees to retain a third-party service provider).[827] Allocating this burden across the estimated 25 large liquidity fund advisers that collectively advise 43 liquidity funds results in annual per large liquidity fund adviser costs, as discussed in more detail in section IV below, of 290 burden hours, at a time cost of $73,460, and $16,374 in external costs.[828]

These estimates are based on our staff's estimates of the paperwork burdens associated with our proposed amendments to Form N–MFP because advisers would be required to file on Form PF virtually the same information about their large liquidity funds as money market funds would be required to file on Form N–MFP as we propose to amend it. We therefore expect that the paperwork burdens associated with Form N–MFP (as we propose to amend it) are representative of the costs that large liquidity fund advisers could incur as a result of our proposed amendments to Form PF. We note, however, that this is a conservative approach for several reasons. Large liquidity fund advisers may experience economies of scale because, as discussed above, virtually all of them advise a money market fund or have a related person that advises a money market fund. Large liquidity fund advisers therefore likely would pay a combined licensing fee or fee to retain the services of a third party that covers filings on both Forms PF and Form N–MFP. We expect that this combined fee likely would be less than the combined estimated PRA costs associated with Forms PF and Form N–MFP. Finally, increased burdens associated with providing the proposed portfolio holdings information should be considered together with the cost savings that would result from our removing current Form PF questions 56 and 57.

We also recognize that large liquidity fund advisers may have concerns about reporting information about their liquidity funds' portfolio holdings and may regard this as commercially sensitive information. Indeed, previously we have noted in response to similar concerns that Form PF data—even if it were inadvertently or improperly disclosed—generally could not, on its own, be used to identify individual investment positions, and thus provides a limited ability for competitors to use Form PF data to replicate a trading strategy or trade against an adviser.[829] Today's proposal, of course, would require advisers to identify individual investment positions.

Without diminishing advisers' concerns about the sensitive nature of certain of the information reported on Form PF, we note that position-level information for liquidity funds generally may not be as sensitive as position-level data for other types of private funds. For example, although some commenters on proposed Form PF confirmed that the information on Form PF is competitively sensitive or proprietary, these commenters did not address liquidity funds in particular. Further, liquidity funds, by definition, invest in ''portfolio[s] of short term obligations.'' This increases the likelihood that any inadvertently or improperly disclosed Form PF data, notwithstanding the controls and systems for handling the data, would relate to securities that already had matured or that would mature shortly thereafter. And because we understand that liquidity funds, like money market funds, tend to hold many of their securities to maturity—rather than selling them in the market—any inadvertent or improper disclosure of a liquidity fund's portfolio holdings generally should not adversely affect the value of the fund's position.[830] The relatively limited universe of securities appropriate for purchase by a liquidity fund together with the similarity of investment strategies followed by

[826] Large liquidity fund advisers already are required to make quarterly filings on Form PF. *See* Form PF: Instruction 9. Requiring large liquidity fund advisers to provide the new portfolio holdings information on a quarterly basis should therefore be more cost effective for the advisers.

[827] *See infra* notes 1166–1168 and accompanying text.

[828] *See infra* note 1165 and accompanying text.

[829] *See* Form PF Adopting Release, *supra* note 799, at n.343 and accompanying text.

[830] In contrast, if the market learned that a private fund had a concentrated position in an equity security and determined that the fund likely would need to sell that security, market makers in the security and other market participants could lower their bid prices for the security in anticipation of the sale. Information about a liquidity fund's (relatively) concentrated position in a security likely to be held until maturity is unlikely to elicit the same reaction because market participants would not anticipate that the liquidity fund would sell the security, and there likely would not be broker-dealers making markets in the security in any event.

liquidity funds[831] also suggests that information about their portfolio holdings may be less sensitive than information about the holdings of hedge funds, for example, which may pursue a variety of investment strategies and whose holdings therefore may reveal more sensitive information.[832] Finally, because we expect that many large liquidity fund advisers also will advise money market funds, they already will be accustomed to managing their portfolios while also making continuous public disclosure of their portfolio holdings as proposed here (as compared to the non-public, quarterly reporting required on Form PF).

In addition to these considerations, and as we discussed in detail in the Form PF Adopting Release, we do not intend to make public Form PF information identifiable to any particular adviser or private fund, and indeed, the Dodd-Frank Act amended the Advisers Act to preclude us from being compelled to reveal this information except in very limited circumstances.[833] We therefore make Form PF data identifiable to any particular adviser or private fund available outside of the Commission only in very limited circumstances, primarily to FSOC as required by the Dodd-Frank Act, subject to the confidentiality provisions of the Dodd-Frank Act.[834] In recognition of the sensitivity of some of the data collected on Form PF, our staff is handling Form PF data in a manner that reflects the sensitivity of this data and is consistent with the confidentiality protections established in the Dodd-Frank Act.

In addition to any concerns advisers may have about the sensitivity of their portfolio holdings, we note that although the increased transparency to regulators provided by our proposal could positively affect capital formation as discussed above, increased transparency, as we observed when adopting Form PF, could also have a negative effect on capital formation if it increases advisers' aversion to risk and, as a result, reduces investment in enterprises that may be risky but beneficial to the economy as a whole.[835] To the extent that our proposal were to cause changes in investment allocations that lead to reduced economic outcomes in the aggregate, our proposal could result in a negative effect on capital available for investment. As we discuss above, however, any effects on capital formation from increased transparency to regulators—including these possible negative effects—likely would be less significant than those associated with our adoption of Form PF.

We also do not believe that our proposed amendments to Form PF would have a significant effect on competition because the information that advisers report on Form PF, including the new information we propose to require, generally will be non-public and similar types of advisers will have compatible burdens under the form as we propose to amend it.[836] We also do not believe that the proposed amendments would have a significant negative effect on capital formation, again because the information collected generally will be non-public and, therefore, should not affect large liquidity fund advisers' ability to raise capital.[837]

We request comment on all aspects of our proposed amendments to Form PF, including our discussion of the benefits, costs, and effects on competition, efficiency, and capital formation.

- Would the portfolio holdings information we propose to require large liquidity fund advisers to file on Form PF, together with the other information that advisers already must file on the form, appropriately identify the ways in which their liquidity funds might generate systemic risk? Are there ways these liquidity funds could create systemic risk, particularly if we were to adopt any of the money market fund reforms we are proposing today, that would not be reflected in the additional information?
- Should we require large liquidity fund advisers to file additional or different information about their liquidity funds? If so, which information and how would that information be useful to FSOC and the Commission? Do commenters expect they would derive efficiencies from our requiring large liquidity fund advisers to file the same types of information that must be reported on Form N–MFP?
- Is our proposal to require more comprehensive liquidity fund reporting by large liquidity fund advisers appropriate? Should we, instead, create a new subcategory of large liquidity fund advisers who would be subject to these additional reporting requirements? If so, how should we define that subcategory? Would requiring only those large liquidity fund advisers with a more substantial amount of combined liquidity fund and money market fund assets under management—for example, $10, $25 or $50 billion—allow us to more effectively achieve our goals?
- Rather than require all large liquidity fund advisers to file portfolio holdings information with respect to each of their liquidity funds, should we define ''qualifying'' liquidity funds and require any adviser to such a fund, potentially including advisers that are not large liquidity fund advisers, to file this more comprehensive information? If so, why, and how should we define such a qualifying liquidity fund? Should we define a ''qualifying liquidity fund'' as a liquidity fund that, together with funds managed in parallel with the liquidity fund, is at least a certain size? What size would be appropriate (*e.g.,* $100 million, $500 million, $1 billion)?
- Should we retain our proposed approach but provide an exemption for *de minimis* liquidity funds for which no additional reporting would be required? This would require a large liquidity fund adviser to provide portfolio holdings information about all of its liquidity funds except those that qualified for the *de minimis* exemption. Such an approach would prevent an adviser that is a large liquidity fund adviser primarily because of its money market funds assets under management from having to file portfolio holdings information for a relatively small liquidity fund (*e.g.,* an adviser with $10

[831] Liquidity funds, by definition, have similar investment objectives. *See* Glossary of Terms to Form PF (defining a ''liquidity fund'' as any private fund that ''seeks to generate income by investing in a portfolio of short term obligations in order to maintain a stable net asset value per unit or minimize principal volatility for investors'').

[832] We are not today proposing to require advisers to file position-level data about private funds other than liquidity funds managed by large liquidity fund advisers, in part, because of the more sensitive information that could be revealed by the position-level data of other types of private funds. In addition, the information we propose to require large liquidity fund advisers to file concerning their liquidity funds is designed primarily to enhance FSOC's ability to assess systemic risk, and thus is informed, in part, by FSOC's own particular concerns about systemic risk in the short-term financing markets. *See, e.g., supra* note 817 and accompanying text. FSOC has not expressed similar concerns about other types of private funds or other markets in which other types of private funds invest exclusively that would suggest FSOC would derive substantial benefits from position-level data about other types of private funds.

[833] *See* Form PF Adopting Release, *supra* note 799, at section II.D.

[834] We also may share Form PF data with other federal departments or agencies or with self-regulatory organizations, in addition to the CFTC and FSOC, for purposes within the scope of their jurisdiction, as contemplated by the Dodd-Frank Act. *Id.* In each case, any such department, agency or self-regulatory organization would be exempt from being compelled under FOIA to disclose to the public any information collected through Form PF and must maintain the confidentiality of that information. *Id.* Prior to sharing any Form PF data, we require that any such department, agency or self-regulatory organization represent to us that it has in place controls designed to ensure the use and handling of Form PF data in a manner consistent with the protections established in the Dodd-Frank Act. *Id.*

[835] *See* Form PF Adopting Release, *supra* note 799, at text accompanying and following n.537.

[836] *See id.* at text accompanying n.535.

[837] *See id.* at text following n.535.

billion in money market fund assets under management and a single liquidity fund with only $10 million in assets under management). Would this minimize reporting burdens on advisers to smaller or start up liquidity funds that are less likely to have a systemic impact while still providing us and FSOC information about the adviser's short-term investing activities, which in the aggregate may be relevant to an assessment of systemic risks? How would we structure such a *de minimis* exemption? Should it be based solely on the size of a liquidity fund and funds managed in parallel with the liquidity fund? Would a $1 billion threshold be appropriate because it would ensure that large liquidity fund advisers are only required to provide portfolio holdings information for relatively large liquidity funds?

• Do commenters agree that the new information we propose to require advisers to provide would be useful to FSOC and the Commission for the reasons we discuss above? Do commenters believe that the information would have the effects on capital formation, competition, and efficiency that we discuss above? Why or why not? Would there be additional effects that we have not discussed here?

• Do commenters agree with our assessment of the potential sensitivity of the information we propose to require advisers to provide? Why or why not? To the extent, advisers view the proposed information as sensitive and are concerned about the information's inadvertent or inappropriate disclosure, is there other information the advisers view as less sensitive that would achieve our goals?

• We propose to require large liquidity fund advisers to provide this new information quarterly with the information broken out monthly. Should we instead require these advisers to file the information more or less frequently? Would a monthly reporting requirement, consistent with Form N–MFP, be more appropriate?

• As discussed above, our proposed amendments to Form PF are designed to enhance FSOC's ability to monitor and assess systemic risks in the short-term financing markets and to facilitate our oversight of those markets and their participants, particularly in the event that further money market fund reforms cause investors to seek alternatives to money market funds, including private funds. Further money market reforms also could incentivize investors to seek out money market fund alternatives that are registered with the Commission, such as ultra-short bond mutual funds. Information about these and similar funds' portfolio holdings also could be useful to us and FSOC, particularly when combined with (or considered together with) information money market funds and advisers would file on amended Forms N–MFP and PF. Should we therefore require registered investment companies that invest in the short-term financing markets to file the same information money market funds must file on Form N–MFP and in the same format and with the same frequency to facilitate comparisons? If so, how should we designate which funds would be subject to this new requirement?

*J. Diversification*

Rule 2a–7 requires a money market fund's portfolio to be diversified, both as to the issuers of the securities it acquires and providers of guarantees and demand features related to those securities.[838] Generally, money market funds must limit their investments in the securities of any one issuer of a first tier security (other than government securities) to no more than 5% of fund assets.[839] They must also generally limit their investments in securities subject to a demand feature or a guarantee to no more than 10% of fund assets from any one provider, except that the rule provides a so-called ''twenty-five percent basket,'' under which as much as 25% of the value of securities held in a fund's portfolio may be subject to guarantees or demand features from a single institution.[840] We adopted these requirements in order to limit the exposure of a money market fund to any one issuer, guarantor, or demand feature provider.[841]

As further explained below, we are concerned that the diversification requirements in rule 2a–7 today may not appropriately limit money market fund risk exposures. We therefore propose, as discussed below, to: (1) require money market funds to treat certain entities that are affiliated with each other as single issuers when applying rule 2a–7's 5% issuer diversification requirement; (2) require funds to treat the sponsors of asset-backed securities as guarantors subject to rule 2a–7's diversification requirements unless the fund's board makes certain findings; and (3) remove the twenty-five percent basket.

1. Treatment of Certain Affiliates for Purposes of Rule 2a-7's Five Percent Issuer Diversification Requirement

The diversification requirements in rule 2a–7 apply to money market funds' exposures to issuers of securities (as well as providers of demand features and guarantees), as discussed above. Rule 2a–7, however, does not require a money market fund to aggregate its exposures to entities that are affiliated with each other when measuring its exposure for purposes of these requirements. As a result, a money market fund could be in compliance with rule 2a–7 while assuming a concentrated amount of risk to a single economic enterprise. For example, although a money market fund would not be permitted to invest more than 5% of its assets in the securities issued by a single bank holding company, the fund could invest well in excess of 5% of its assets in securities issued by the bank holding company together with its affiliates. Under current rule 2a–7, for example, a money market fund could invest 5% of its assets in Bank XYZ,

[838] Rule 2a–7(c)(4)(i) through (iv). The diversification requirements of rule 2a–7 differ in significant respects from the requirements for diversified management investment companies under section 5(b)(1) of the Act. A money market fund that satisfies the applicable diversification requirements of the paragraphs (c)(4) and (c)(6) of the rule is deemed to have satisfied the requirements of section 5(b)(1). Rule 2a–7(c)(4)(v). Subchapter M of the Internal Revenue Code contains other diversification requirements for a money market fund to be a ''regulated investment company'' for federal income tax purposes. 26 U.S.C. 851 *et seq. See also* 1990 Proposing Release, *supra* note 310, at n.25.

[839] Rule 2a–7(c)(4)(i)(A) and (B). A first tier security is any eligible security that has received a short-term credit rating in the highest short-term category for debt obligations or, if the security is an unrated security, that is of comparable quality, as determined by the money market fund's board of directors. Rule 2a–7(a)(14). Government securities and securities issued by money market funds also are first tier securities. *Id.* A fund also may invest no more than 0.5% of fund assets in any one issuer of a second tier security. Rule 2a–7(c)(4)(i)(C). A second tier security is an eligible security that is not a first tier security. Rule 2a–7(a)(24). The rule contains a safe harbor where a taxable and national tax-exempt fund may invest up to 25% of its assets in the first tier securities of a single issuer for a period of up to three business days after acquisition (but a fund may use this exception for only one issuer at a time). Rule 2a–7(c)(4)(i)(A).

[840] Rule 2a–7 currently applies a 10% diversification limit on guarantees and demand features only to 75% of a money market fund's total assets. *See* rule 2a–7(c)(4)(iii)(A). The money market fund, however, may only use the twenty-five percent basket to invest in demand features or guarantees that are first tier securities issued by non-controlled persons. *See* rule 2a–7(c)(4)(iii)(B) and (C). All of rule 2a–7's diversification limits are applied at the time of acquisition. For example, a fund may not invest in a particular issuer if, after acquisition, the fund's aggregate investments in the issuer would exceed 5% of fund assets. But if the fund's aggregate exposure after making the investment was less than 5%, the fund would not be required to later sell the securities if the fund's assets decreased and the fund's investment in the issuer came to represent more than 5% of the fund's assets.

[841] *See* 2009 Proposing Release, *supra* note 31, at n.220 and accompanying text; 1990 Proposing Release, *supra* note 310, at text accompanying n.23 (''Diversification limits investment risk to a fund by spreading the risk of loss among a number of securities.'').

NA, another 5% of its assets in Bank XYZ Corp., another 5% of its assets in Bank XYZ Securities, LLC, another 5% of its assets in Bank XYZ (Grand Cayman), another 5% of its assets in Bank XYZ (London), and so on.

Financial distress at an issuer can quickly spread to affiliates through a number of mechanisms. Firms within an affiliated group, for example, may issue financial guarantees, whether implicit or explicit, of each other's securities, effectively creating contingent liabilities whose values depend on the value of other firms in the group. These guarantees can be ''upstream,'' whereby a subsidiary guarantees its parent's debt; ''downstream,'' whereby a parent guarantees a subsidiary's debt; or ''cross stream,'' whereby one subsidiary guarantees another subsidiary's debt. Affiliates may be separate legal entities, but their valuations and the creditworthiness of their securities may depend on the financial well-being of other firms in the group. As an example, a firm may issue debt securities that would be considered to be in default if one of the firm's affiliates is unable to meet its financial obligations.

Alternatively, the value of a firm's securities may depend, implicitly or explicitly, on the strength of the affiliate group's consolidated financial statements. If an affiliate in the group experiences financial distress and the affiliate group's consolidated financials therefore suffer, then the value of the securities of the other firms in the group may decline. Indeed, bank holding companies are required to act as a source of financial strength to their bank subsidiaries, providing a means for financial distress at a bank subsidiary to affect the parent banking holding company.[842] The possibility for financial distress to transmit across affiliated entities was demonstrated during the 2007–2008 financial crisis when, for example, American International Group Inc. came under financial stress, which affected a number of its affiliates. In some cases, AIG's corporate group contagion required the sponsors of money market funds that owned AIG's affiliates' securities to seek no-action relief from our staff in order for the sponsors to support their funds.[843]

Rule 2a–7 today thus can allow a fund to take on highly concentrated risks, risks that appear inconsistent with the purposes of the diversification requirements and that may be inconsistent with investors' expectations of the level of risk posed by a money market fund. Indeed, we have explained that ''[d]iversification limits investment risk to a fund by spreading the risk of loss among a number of securities.'' [844] But exposure to entities that are affiliated with each other may not effectively spread the risk of loss as contemplated by rule 2a–7's diversification requirements and, as discussed in more detail below, data analyzed by our staff show that many money market funds have invested in affiliated entities to a greater extent than would be permitted if the exposures were aggregated.

We propose, therefore, to amend rule 2a–7's diversification requirements to require that money market funds limit their exposure to affiliated groups, rather than to discrete issuers in isolation. Specifically, we propose to require money market funds to aggregate their exposures to certain entities that are affiliated with each other when applying rule 2a–7's 5% issuer diversification limit.[845] Entities would be affiliated for this purpose if one controlled the other entity or was controlled by it or under common control with it.[846] For this purpose only, control would be defined to mean ownership of more than 50% of an entity's voting securities.[847] By using a more than 50% test (*i.e.,* majority ownership), we believe the alignment of economic interests and risks of the affiliated entities is sufficient to justify aggregating their exposures for purposes of rule 2a–7's 5% issuer diversification limit.[848]

This approach is consistent with some of the circumstances under which affiliated entities must be consolidated on financial statements prepared in accordance with GAAP, under which a parent generally must consolidate its majority-owned subsidiaries.[849] Majority-owned subsidiaries generally must be consolidated under GAAP for similar reasons—the operations of the group are sufficiently related such that they are presented under GAAP as if they ''were a single economic entity''—which appear to support consolidating them for purposes of rule 2a–7's 5% diversification requirements as well.[850]

A majority ownership test also should mitigate the costs to money markets funds of complying with the proposed amendment. Our understanding is that money market funds generally would be able to determine issuer affiliations, defined with a majority ownership test, as part of their evaluation of whether a security presents minimal credit risks, or that money market funds could readily obtain this information from issuers or the broker-dealers marketing the issuance. In this regard we note that, although some companies that sell their securities to money market funds will have a relatively large number of such affiliates, we expect that only a relatively small subset of these affiliates will be companies in which a money market fund could invest (*e.g.,* that have a requisite credit rating and issue short-term debt in U.S. dollars). We expect that in many cases affiliates under this

[842] *See* section 616 of the Dodd-Frank Act.

[843] *See, e.g.,* SEC Staff No-Action Letter to USAA Mutual Funds Trust (Oct. 22, 2008) (providing no-action assurances so that an affiliated person of the money market fund could purchase certain short-term notes issued by AIG Funding, Inc. based in part on representations that the securities' market values could soon decline below the securities' shadow prices); SEC Staff No-Action Letter to MainStay VP Cash Management Portfolio (Oct. 22, 2008) (providing the same relief for the purchase of notes issued by AIG Funding, Inc. based in part on representations that it would be advisable for the fund to sell the security but, ''due in large part to market concerns regarding the sponsoring entity of the Security and its affiliates,'' the adviser was unable to sell the security on behalf of the fund in then-current markets); SEC Staff No-Action Letter to Phoenix Opportunities Trust and Phoenix Edge Series Fund (Oct. 22, 2008) (providing no-action assurances so that an affiliated person of the money market funds could purchase certain securities issued by International Lease Finance Corporation, a subsidiary of American International Group, Inc., based in part on representations that the securities' market values had declined below the securities' amortized cost values); SEC Staff No-Action Letter to Penn Series Funds, Inc. (Oct. 22, 2008) (providing no-action assurances so that an affiliated person of the money market fund could purchase certain securities issued by Sun America Sponsored Trust and International Lease Finance Corporation, both affiliates of American International Group, Inc., based in part on representations that the securities' market values had declined below the securities' amortized cost values).

[844] *See supra* note 841.

[845] *See* proposed (FNAV and Fees & Gates) rule 2a–7(d)(3)(ii)(F).

[846] *Id.*

[847] *Id.*

[848] We previously have taken a similar approach in delineating affiliates. *See* Further Definition of ''Swap,'' ''Security-Based Swap,'' and ''Security-Based Swap Agreement''; Mixed Swaps; Security-Based Swap Agreement Recordkeeping, Exchange Act Release No. 67453 (July 18, 2012) [77 FR 48208 (Aug. 13, 2012)], at nn.797–803 and accompanying text.

[849] *See, e.g.,* FASB ASC, *supra* note 270, at paragraph 810–10–15–8 (''The usual condition for a controlling financial interest is ownership of a majority voting interest, and, therefore, as a general rule ownership by one reporting entity, directly or indirectly, of more than 50 percent of the outstanding voting shares of another entity is a condition pointing toward consolidation.'').

[850] *See, e.g., id.* at paragraph 810–10–10–1 (''The purpose of consolidated financial statements is to present, primarily for the benefit of the owners and creditors of the parent, the results of operations and the financial position of a parent and all its subsidiaries as if the consolidated group were a single economic entity. There is a presumption that consolidated financial statements are more meaningful than separate financial statements and that they are usually necessary for a fair presentation when one of the entities in the consolidated group directly or indirectly has a controlling financial interest in the other entities.'').

proposal—and especially affiliates in which money market funds are likely to invest—will have other readily observable characteristics that will help money market funds to discern their affiliations (*e.g.,* substantially similar names). We also understand that, because exposures to entities that are affiliated with each other can be expected to be highly correlated, most money market funds today consider their exposures to entities that are affiliated with each other for risk management purposes, although they may nonetheless choose to invest in affiliated entities to a greater extent than would be permitted under this proposal.

We also are concerned that the other approaches we considered could limit money market funds' investment flexibility unnecessarily and could be more difficult to apply. For example, we considered the approach we are proposing today but with the definition of ''control'' set at an ownership threshold lower than 50%.'' [851] We also considered requiring money market funds to aggregate exposures to a broader range of entities by requiring aggregation of ''affiliated persons,'' as defined in the Investment Company Act.[852] If we were to use that definition, a money market fund would have to aggregate its exposures to two issuers if, for example, one issuer owned directly or indirectly 5% of the other issuer's voting securities.

We are concerned that either of these alternative approaches could unnecessarily limit a money market fund's flexibility. Our goal is to require money market funds to limit their exposure to particular economic enterprises without unnecessarily limiting money market funds' investments in other persons whose connection to the economic enterprise may be sufficiently attenuated that they may not be highly correlated with the enterprise. We are concerned that either of these alternative approaches could restrict money market funds from investing in securities whose issuers had only an attenuated connection to the economic enterprise. For example, if a parent owned only 5% of the voting stock of one of its subsidiaries, the risks posed by investing in the parent and minority-owned subsidiary likely would be less correlated than if the parent owned more than 50% of the subsidiary's voting stock. These other approaches also could be more difficult to apply in that they would require a money market fund to conduct a more extensive analysis for each investment (*e.g.,* to ascertain the extent to which entities control one another or are under common control, where control could be established through more attenuated relationships or ownership levels).

We also considered proposing to require a money market fund to treat as affiliates *all* entities that must be consolidated on a balance sheet. This would include affiliated entities as we propose, as well as certain ''variable interest entities,'' which generally are entities in which the parent holds a controlling financial interest that is not based on the parent's ownership of a majority of the entity's voting stock.[853] An SPE issuing ABS could be a variable interest entity consolidated on the sponsor's balance sheet, for example. In light of the large variety of entities that may be variable interest rate entities and the diverse activities in which they may engage,[854] we believe, at this time, that it is more appropriate to address them (as needed) through more targeted reforms like our ABS diversification proposal. For these same reasons, and because we already are further tightening rule 2a–7's 10% limit on indirect exposures through our ABS and twenty-five percent basket diversification proposals, this proposal only addresses aggregation of exposures for purpose of rule 2a–7's 5% issuer diversification limit.

We request comment on our approach.

- Do commenters agree that the exposures to risks of issuers who would be treated as affiliates under this proposal would be highly correlated? Is our proposed approach to delineating affiliates too broad or too narrow and why? Do commenters believe that our proposed approach would limit money market funds' investment flexibility unnecessarily, and if so, to what extent? Should we, instead, use any of the alternative approaches to delineating a group of affiliates we discuss above? Are there other approaches we should consider? Should we, for example, require money market funds to aggregate exposures to parent companies and any of their ''majority-owned subsidiaries,'' as defined in the Investment Company Act? A parent's majority-owned subsidiaries under this definition would be any company ''50 per centum or more of the outstanding voting securities of which are owned by [the parent], or by a company which . . . is a majority-owned subsidiary of such person.'' [855]
- Do commenters agree that a more than 50% (*i.e.,* majority ownership) test rather than a lower threshold used to define ''control'' or a different threshold would make it more likely that there would be an alignment of economic interests of the affiliated entities that is sufficient to justify aggregating their exposures for purposes of rule 2a–7's 5% issuer diversification limit?
- Do commenters agree that money market funds generally would be able to determine these affiliations, defined with a majority ownership test, as part of their evaluation of whether a security

[851] This approach is reflected in other provisions of the federal securities laws. *See, e.g.,* section 2(a)(3) of the Investment Company Act (defining the term ''affiliated person''); section 202(a)(17) of the Advisers Act (defining the term ''person associated with an investment adviser''); Form ADV: Glossary of Terms (defining the term ''Related Person''); *see also* section 2(a)(9) of the Investment Company Act (providing that the term ''control'' means ''the power to exercise a controlling influence over the management or policies of a company, unless such power is solely the result of an official position with such company''); section 202(a)(12) (same definition of ''control'').

[852] *See* section 2(a)(3) of the Investment Company Act (''''Affiliated person' of another person means (A) any person directly or indirectly owning, controlling, or holding with power to vote, 5 per centum or more of the outstanding voting securities of such other person; (B) any person 5 per centum or more of whose outstanding voting securities are directly or indirectly owned, controlled, or held with power to vote, by such other person; (C) any person directly or indirectly controlling, controlled by, or under common control with, such other person; (D) any officer, director, partner, copartner, or employee of such other person; (E) if such other person is an investment company, any investment adviser thereof or any member of an advisory board thereof; and (F) if such other person is an unincorporated investment company not having a board of directors, the depositor thereof.'').

[853] *See, e.g.,* FASB ASC, *supra* note 270, at paragraph 810–10–05–8 (''The Variable Interest Entities Subsections clarify the application of the General Subsections to certain legal entities in which equity investors do not have the characteristics of a controlling financial interest or do not have sufficient equity at risk for the legal entity to finance its activities without additional subordinated financial support. Paragraph 810–10–10–1 states that consolidated financial statements are usually necessary for a fair presentation if one of the entities in the consolidated group directly or indirectly has a controlling financial interest in the other entities. Paragraph 810–10–15–8 states that the usual condition for a controlling financial interest is ownership of a majority voting interest. However, application of the majority voting interest requirement in the General Subsections of this Subtopic to certain types of entities may not identify the party with a controlling financial interest because the controlling financial interest may be achieved through arrangements that do not involve voting interests.'').

[854] *See, e.g., id.* at paragraph 810–10–05–11 (''VIEs often are created for a single specified purpose, for example, to facilitate securitization, leasing, hedging, research and development, reinsurance, or other transactions or arrangements. The activities may be predetermined by the documents that establish the VIEs or by contracts or other arrangements between the parties involved.'').

[855] *See* section 2(a)(24) of the Investment Company Act (''''Majority-owned subsidiary' of a person means a company 50 per centum or more of the outstanding voting securities of which are owned by such person, or by a company which, within the meaning of this paragraph, is a majority-owned subsidiary of such person.'').

presents minimal credit risks, or that money market funds could readily obtain this information from issuers or the broker-dealers marketing the issuance? Why or why not? We ask that money market funds responding to this request for comment describe the materials they typically review as part of their evaluation of whether a security presents minimal credit risks and how these materials would or would not allow a money market fund to determine affiliations under our proposal.

- Is our understanding that money market funds today attempt to identify and measure their exposure to entities that are affiliated with each other as part of their risk management or stress testing processes correct? If so, how do they determine affiliations for these purposes?
- Do commenters agree with our expectation that, although some issuers that sell their securities to money market funds will have a relatively large number of affiliates, only a relatively small subset of these affiliates will be companies in which a money market fund could invest? Why or not?
- Should we require a money market fund to treat as entities that are affiliated with each other those that must be consolidated on a balance sheet, including ''variable interest entities'' (in addition to majority-owned subsidiaries that would be treated as affiliates under our proposal)? Why or why not? Do commenters agree that, in light of the large variety of entities that may be variable interest rate entities, it is more appropriate to address them (as needed) through more targeted reforms? Should we, instead, require money market funds to treat entities that are affiliated with each other as if they were a single entity when applying rule 2a–7's 10% diversification limit (for providers of demand features and guarantees) as well? If so, should we use the same approach for determining when entities would be affiliated with each other as we propose for purposes of the rule's 5% issuer diversification limit (*i.e.,* with a majority-ownership test)? Why or why not? As discussed in more detail below, we are proposing to treat certain ABS sponsors as guarantors subject to the 10% limit, and also are proposing to remove the twenty-five percent basket. What would be the cumulative impact on money market funds' ability to acquire securities subject to guarantees or demand features (and issuers' ability to issue those securities) if, in addition to these other two proposals, we also were to require money market funds to aggregate their exposures to providers of demand features and guarantees that are affiliated with each other for purposes of the 10% limit?

We expect that this proposal, and our diversification proposals collectively, would provide a number of benefits. These proposals are designed to diversify the risks to which money market funds may be exposed and thereby reduce the impact of any single issuer's (or guarantor's or demand feature provider's) financial distress on a fund under either of our floating NAV or liquidity fees and gates proposals. Requiring money market funds to more broadly diversify their risks should reduce the volatility of fund returns (and hence NAVs) and limit the impact of an issuer's distress (or guarantor's or demand feature provider's distress) on fund liquidity. By reducing money market funds' volatility and making their liquidity levels more resilient, our diversification proposals are designed to mitigate the risk of heavy shareholder redemptions from money market funds in times of financial distress and promote capital formation by making money market funds a more stable source of financing for issuers of short-term credit instruments. Reducing money market funds' volatility and making their liquidity levels more resilient also should cause money market funds to attract further investments, increasing their role as a source of capital in the short-term financing markets for issuers. We are not able to quantify these benefits (although we do provide quantitative information concerning certain impacts), primarily because we believe it is impractical, if not impossible, to identify with sufficient precision the marginal decrease in risk and increase in stability we expect these diversification proposals would provide.

More fundamentally, this proposal is designed to more effectively achieve the diversification of risk contemplated by the rule's current 5% issuer diversification requirement. As noted above, we have explained that ''[d]iversification limits investment risk to a fund by spreading the risk of loss among a number of securities.'' [856] Requiring funds to purchase ''a number of securities'' rather than a smaller number of concentrated investments will only ''spread . . . the risk of loss'' if the performance of those securities is not highly correlated. That is, a fund's investments in Issuers A, B, and C are no less risky (or only marginally so) than a single investment in Issuer A if Issuers A, B, and C are likely to experience declines in value simultaneously and to approximately the same extent. This may indeed be likely if Issuers A, B, and C are affiliated with each other. Prime money market funds' concentrated exposures to financial institutions increase these concerns because prime money market funds' portfolios already appear correlated to some extent.[857] The risk posed by this sector concentration would be increased if a prime money market fund, in addition, had large correlated exposures to a particular financial services group through investments in various entities that are affiliated with each other.

We recognize, however, that this proposal could impose costs on money market funds and could affect competition, efficiency, and capital formation. To help us evaluate these effects, RSFI staff analyzed the diversification and concentration in the money market fund industry, as described in detail in RSFI's memo ''Issuances by Parents and Exposures by Parents in Money Market Funds,'' which will be placed in the comment file for this Release (''RSFI Diversification Memo''). That memo shows, among other things, that some money market funds invested more than 5% of their assets in the issuances of specific corporate groups, or ''parents'' (as defined in the RSFI Diversification Memo) between November 2010 and November 2012. For example, the analysis shows that the largest average fund-level exposure of at least 5% to the issuances of a single parent is 31. In other words, 31 money market funds, on average, invest at least 5% of their portfolios in the issuances of the largest parent. The analysis also shows that the largest average fund-level exposure of at least 7% to the issuances of one parent is 14 while the largest average fund-level exposure of at least 10% to the issuances of one parent is 3. We expect, therefore, that this proposal would increase the diversification of at least some money market funds. For example, a money market fund that had invested more than 5% of its assets in a parent or corporate group would, when those investments matured, have to reinvest

[856] *See supra* note 841. *See also, e.g.,* Occupy the SEC FSOC Comment Letter, *supra* note 42 (stating that rule 2a–7's current regulatory framework for diversification is inadequate, in part because ''issuer-level diversification limits do not directly address the potential for aggregate exposure across subsidiaries of the same firm, allowing for significant aggregation effects''); Better Markets FSOC Comment Letter, *supra* note 67 (''Limiting issuer concentration in MMF portfolios, broadening the definition of 'issuer' to include affiliates, and enhancing liquidity standards are plainly appropriate measures that will help stabilize MMFs.'').

[857] *See supra* notes 66–67 and accompanying text.

some of the proceeds in a different parent or corporate group (or in unrelated issuers).[858]

The effect of this reinvestment on competition, efficiency, or capital formation would depend in part on how money market funds choose to reinvest their assets. It seems reasonable to expect that a divestment by one money market fund (because its exposure to a particular group of affiliates is too great) might become a purchasing opportunity for another money market fund whose holdings in that affiliated group do not constrain it. If the credit qualities of the investments were similar, there should be no net effect on fund risk and yield, issuers, or the economy. It is possible, however, that some money market funds would reinvest some or all of their excess exposure in securities of higher risk, albeit within the restrictions in rule 2a–7. In these instances, funds' portfolio risk would increase, their NAVs and fund liquidity would likely become more volatile, and yields would rise. Money market funds in this instance could become less stable than they are today, investor demand for the funds could fall (to the extent increased volatility in money market funds is not outweighed by any increase in fund yield), and capital formation could be reduced. Alternatively, money market funds could reinvest excess exposure in securities of lower risk. In these instances, portfolio risk would fall, fund NAVs and liquidity would likely become less volatile, and yields would fall. In this scenario, money market funds would become more stable than they are today, investor demand for the funds could rise (to the extent increased stability in money market funds is not outweighed by any decrease in fund yield), and capital formation might be enhanced. We cannot predict how money market funds would invest in response to this proposal and we thus do not have a basis for determining money market funds' likely reinvestment strategies, and we accordingly seek comment on these issues below.

It also is important to note that money market funds' current exposures in excess of what our proposal would permit may reflect the overall risk preferences of their managers. To the extent that this proposal would reduce the concentration of issuer risk, fund managers that have particular risk tolerances or preferences may shift their funds' remaining portfolio assets, within rule 2a–7's restrictions, to higher risk assets. If so, portfolio risk, although more diversified, would increase (or remain constant), and we would expect portfolio yields to rise (or to remain constant). If yields were to rise, money market funds might be able to compete more favorably with other short-term investment products (to the extent the increased yield is not outweighed by any increased volatility).

At this time, we cannot predict or quantify the precise effects this proposal would have on competition, efficiency, or capital formation. The effects would depend on how money market funds, their investors, and companies who issue securities to money market funds would adjust on a long-term basis to our proposal. The ways in which these groups could adjust, and the associated effects, are too complex and interrelated to allow us to predict them with specificity or to quantify them at this time.

For example, if a money market fund must reallocate its investments under our proposal, whether that would affect capital formation would depend on whether there are available alternative investments the money market fund could choose and the nature of any alternatives. Assuming there are alternative investments, the effects on capital formation would depend on the amount of yield the issuers of the alternative investments would be required to pay as compared to the amount they would have paid absent our proposal. For example, this proposal could cause money market funds to seek alternative investments and this increased demand could allow their issuers to pay a lower yield than they would absent this increase in demand. This would decrease issuers' financing costs, enhancing capital formation. But it also could decrease the yield the money market fund paid to its shareholders, potentially making money market funds less attractive and leading to reduced aggregate investments by the money market fund which, in turn, could increase financing costs for issuers of short-term debt. The availability of alternative investments and the ease with which they could be identified could affect efficiency, in that money market funds might find their investment process less efficient if they were required to expend additional effort identifying alternative investments. These same factors could affect competition if more effort is required to identify alternative investments under our proposals and larger money market funds are better positioned to expend this additional effort or to do so at a lower marginal cost than smaller money market funds. These factors also could affect capital formation in other ways, in that money market funds could choose to invest in lower quality securities under our proposal if they are not able to identify alternative investments with levels of risk equivalent to the funds' current investments.

In addition to these effects, we recognize that this proposal could require money market funds to update the systems they use to monitor their compliance with rule 2a–7's 5% issuer diversification requirement in order to aggregate exposures to affiliates. Although we understand that most money market funds today consider their exposures to entities that are affiliated with each other for risk management purposes, any systems money market funds currently have in place for this purpose may not be suitable for monitoring compliance with a diversification requirement, as opposed to a risk management evaluation (which may entail less regular or episodic monitoring).

Because money market funds differ significantly in their current practices and systems, we do not have the information necessary to provide a point estimate of the costs associated with this proposal. But based on the activities typically involved in making systems modifications, and recognizing that money market funds' existing systems currently have varying degrees of functionality, we estimate that the one-time systems modifications costs (including modifications to related procedures and controls) for a money market fund associated with this proposal would range from approximately $600,000 to $1,200,000.[859] We do not expect that money market funds would incur material ongoing costs to maintain and modify their systems as a result of this proposal because we expect modifications required by this proposal would be incremental changes to existing systems that already perform similar functions (track exposures for purposes of monitoring compliance with rule 2a–7's 5% issuer diversification limit). We also note that, although we have estimated the costs that a single money market fund could incur as a result of this proposal, we

[858] Money market funds would not be required to sell any of their portfolio securities as a result of any of our diversification proposals because rule 2a–7's diversification limits are measured at acquisition. *See, e.g., supra* note 840.

[859] Staff estimates that these costs would be attributable to the following activities: (i) planning, coding, testing, and installing system modifications; (ii) drafting, integrating, and implementing related procedures and controls; and (iii) preparing training materials and administering training sessions for staff in affected areas. *See also supra* note 245 (discussing the bases of our staff's estimates of operational and related costs).

expect that these costs would be shared among various money market funds in a complex. To the extent money market funds use software or other solutions purchased or licensed from third-party vendors, the funds may be able to purchase any needed upgrades at a lower cost than would be required for the funds to modify their systems internally.

As we discuss above, we expect that money market funds generally would be able to determine affiliations under our proposal, which uses a majority ownership test, as part of their evaluation of whether a security presents minimal credit risks, or that money market funds could readily obtain this information from issuers or the broker-dealers marketing the issuance. We therefore do not expect that money market funds would be required to spend additional time determining affiliations under our proposal, or if an additional time commitment would be required, we expect that it would be minimal. We estimate that the costs of this minimal additional time commitment to a money market fund, if it were to occur, would range from approximately $5,000 to $105,000 annually.[860]

We request comment on this analysis, including the analysis contained in the RSFI Diversification Memo.

- Do commenters expect that they would incur operational costs in addition to, or that differ from, the costs we estimate above? Do commenters expect they would be required to expend additional time determining affiliations, or that they would incur additional or different costs in doing so?
- Do commenters expect that money market funds would encounter any difficulties in finding alternative investments under our proposal? Why or why not? In what types of assets are money market funds likely to invest if they are required to aggregate their investments in entities that are affiliated with each other as we propose? Are money market funds likely to reinvest excess exposure in assets that are similar, more risky or less risky than their original portfolios?
- How would this proposal (and our diversification proposals collectively) affect fund yields and the stability of fund NAVs and liquidity? How would they affect competition, efficiency, or capital formation?
- Do commenters expect this proposal would change the financing costs of companies who issue their securities to money market funds? If so, why, and to what extent? If financing costs increase, to what extent would that increase be passed on to money market fund investors in the form of higher yields? Would any higher yields then result in increased investments by money market funds in the aggregate? Would any aggregate increase offset or mitigate any increase in issuers' financing costs? Would the inverse occur if issuers' financing costs decreased because of increased demand from money market funds? How would any associated increases or decreases in money market funds' volatility affect investor demand for money market funds and, in turn, capital formation and issuers' financing costs?
- Are there any benefits, costs, or effects on competition, efficiency, and capital formation that we have not identified or discussed?

2. Asset-Backed Securities

In 2007, a number of money market funds were exposed to substantial losses resulting from investments in asset-backed commercial paper issued by structured investment vehicles (''SIVs''), a type of ABS.[861] As we described in some detail in the 2009 Proposing Release, SIVs suffered severe liquidity problems and significant losses in 2007 when risk-averse short-term investors (including money market funds), fearing increased exposure to liquidity risk and residential mortgage defaults, began to avoid the commercial paper the SIVs issued, causing the paper to decline in value.[862] The decline in value of the SIVs' commercial paper threatened to force a number of money market funds to re-price below their $1.00 stable share price, a result that was most likely avoided in part because many of the SIVs received support from their sponsors.[863]

Thus, in addition to being exposed to the SIVs directly, money market funds also were exposed to the risk that the SIVs' sponsors would no longer support the value of the funds' troubled SIV investments. In many cases, the sponsors were banks to which money market funds were already exposed because the funds owned securities issued by or subject to guarantees or demand features from the banks. Money market funds' reliance on and exposure to SIV sponsors regarding the SIVs' ABCP in 2007 suggests a potential weakness in the way in which rule 2a–7's diversification provisions apply to ABSs, potentially permitting money market funds to become overexposed to sponsors of SIVs and ABS sponsors more generally. We therefore propose to amend rule 2a–7's diversification provisions to limit the amount of exposure money market funds can have to ABS sponsors that provide express or implicit support for their ABSs.[864]

[860] In arriving at this estimate, we expect that any required additional work generally would be conducted each time a money market fund determined whether to add a new issuer to the approved list of issuers in which the fund may invest. The frequency with which a money market fund would make these determinations would depend on its size and investment strategy. To be conservative, and based on Form N–MFP data concerning the number of securities held in money market funds' portfolios, we estimate that a money market fund could be required to make such a determination between 33 and 339 times each year. This is based on our staff's review of data filed on Form N–MFP as of February 28, 2013, which showed that the 10 smallest money market funds by assets had an average of 33 investments and the 10 largest money market funds by assets had an average of 339 investments. The number of a money market fund's investments should be a rough proxy for the number of times each year that a money market fund could add an issuer to its approved list, although this will overstate the frequency of these determinations (*e.g.,* a fund may have a number of separate investments in a single issuer). We estimate that the additional time commitment imposed by this proposal, if any, would be an additional 1–2 hours of an analyst's time each time the fund determined whether to add an issuer to its approved list. The estimated range of costs, therefore, is calculated as follows: (33 evaluations x 1 hour of a junior business analyst's time at $155 per hour = $5,115) to (339 evaluations x 2 hours of a junior business analyst's time at $155 per hour = $105,090). Finally, we recognize that some money market funds do not use an approved list, but instead evaluate each investment separately. We believe that the number of a money market fund's investments also should be a rough proxy for the number of times such a money market fund would evaluate each investment. Such funds may be on the higher end of the range, however, because the extent to which a fund's average number of investments reflects the number of times such a fund purchases securities would depend on the rate of the fund's portfolio turnover. Whether any additional analysis would be required as a result of this proposal for such a fund also would depend on whether the fund invested proceeds from maturing securities in issuers for which a new credit risk analysis was required or in issuers of securities owned by the fund for which the analysis may already have been done.

[861] *See, e.g.,* 2009 Proposing Release, *supra* note 31, at sections I.D and II.A.4. ABCP is commercial paper issued by special purpose entities, or SPEs, to finance the purchase of various financial assets. Payments to ABCP investors are based on the financial assets, and ABCP is therefore a type of ABS. In some cases, the sponsor of the ABCP will provide explicit liquidity or credit support to the ABCP, whereas in other cases, such as the SIVs, the sponsors provide no explicit support.

[862] *Id.*

[863] *Id. See also, e.g.,* Dan Gallagher, *Citigroup says it will absorb SIV assets: Move bails out struggling investment vehicles but could hurt capital base,* MarketWatch, Dec. 17, 2007, *available at http://articles.marketwatch.com/2007-12-13/news/30731471_1_sivs-citigroup-capital-levels.* In some cases, where the SIVs' sponsors were unable or unwilling to support the SIVs, money market funds' sponsors themselves supported the money market funds by purchasing the SIV investments at their amortized cost or providing some form of credit support. *See* 2009 Proposing Release, *supra* note 31, at text accompanying n.41.

[864] *See also infra* notes 878–880 and accompanying text (describing the treatment under

In the 2009 Proposing Release, we expressed concern about the substantial number of money market funds that owned ABCP and other asset-backed debt securities issued by SIVs in 2007 and the stresses those SIV holdings placed on many money market funds' stable share prices.[865] We sought comment on these concerns in 2009, and asked whether we should require fund boards to consider particular factors when evaluating ABSs, to limit the types of ABSs in which funds could invest, or to further tighten rule 2a–7's diversification limitations.[866] Most commenters did not address these proposals, and those that addressed some of them generally did not support them.[867]

We are concerned that the experience with SIVs suggests a potential weakness in rule 2a–7's diversification requirements. The rule's diversification provisions require no diversification of exposure to ABS sponsors because special purpose entities (''SPEs'')—rather than the sponsors themselves—issue the ABS, and the support that ABS sponsors provide, implicitly or explicitly,[868] typically does not meet the rule's definition of a ''guarantee'' or ''demand feature.''[869] Nonetheless, we understand that money market funds investing in some types of ABCP (and potentially other types of ABSs that may be developed in the future for which sponsor support may be particularly relevant) rely on the ABCP sponsor for liquidity and other support and make investment decisions based, at least in part, on the presumption that the sponsor will take steps to prevent the ABCP from defaulting, including committing capital.[870] In the case of ABCP in particular, ABCP investors likely will be repaid from sources other than or in addition to the assets owned by the SPE, including potentially sponsor support, because the assets owned by the SPE issuing the ABCP generally will have greater maturities than the ABCP (*e.g.,* investors may be due payment on the ABCP in 30 days but the assets supporting the ABCP may mature in 90 days).[871] We have received a number of comment letters on unrelated rulemakings from representatives of participants in the ABSs markets explaining that ABCP investors analyze the structure of the ABCP programs and the financial wherewithal of their support providers more than asset-level information about the assets owned by the SPEs issuing the ABCP.[872]

Because under rule 2a–7 each SPE is considered a separate issuer and because money market funds are not required to diversify against implicit ABS sponsor support (and even some forms of explicit support), a money market fund's portfolio could consist entirely of commercial paper issued by multiple SPEs, all with a single sponsor on which the fund could seek to rely to provide liquidity and capital support, if necessary. Such a result is inconsistent with the purposes of rule 2a–7's diversification requirements and permits funds to assume a substantial concentration of risk to a single economic enterprise, which may be inconsistent with investors' expectations of the level of risks posed by a money market fund.[873]

We propose, therefore, to amend rule 2a–7 to provide that, subject to an exception, money market funds investing in ABSs, including ABCP, rely on the ABSs sponsors' financial strength or their ability or willingness to provide liquidity, credit, or other support to the

this proposal of ABS sponsors who may not provide support, explicit or implicit, for their ABSs).

[865] *See, e.g.,* 2009 Proposing Release, *supra* note 31, at section II.A.4 and nn.37–39 and accompanying text. *See also Perspectives on Money Market Mutual Fund Reforms,* Testimony of David S. Scharfstein, Professor of Finance, Harvard Business School before the Senate Committee on Banking, Housing, and Urban Affairs (June 21, 2012) (noting that in the summer of 2007 concerns about the quality of subprime loans underpinning ABCP caused the ABCP's interest rates to rise dramatically, and that ''[s]ome MMFs responded to this spike in market risk by actually *increasing* portfolio risk, taking on higher-yielding instruments like ABCP in an effort to boost returns and attract new investors'') (emphasis in original).

[866] *See* 2009 Proposing Release, *supra* note 31, at sections II.A.4 and II.D.

[867] *See, e.g.,* Comment Letter of the American Securitization Forum (Sept. 8, 2009) (available in File No. S7–11–09) (''ASF 2009 Comment Letter'') (opposing the proposal to require fund boards to consider particular factors when evaluating ABSs, noting that ''a list of mandatory items may inadvertently stifle innovation and unnecessarily limit the development of new financial products which may be needed in order to help the global short-term markets recover and regain vibrancy and vigor''); Comment Letter of the Independent Directors Council (Sept. 8, 2009) (available in File No. S7–11–09) (''IDC believes such detailed direction from the Commission [to consider specific factors when evaluating ABSs] could suggest that fund boards be involved in an inappropriate level of credit analysis, inconsistent with their oversight role. . . . IDC recommends that the Commission not adopt amendments requiring boards to evaluate such specific factors.'').

[868] Explicit support includes, for example, a liquidity facility provided by the ABS sponsor to the SPE issuing the ABS under which the sponsor is obligated to provide liquidity support to permit the SPE to make payments on the ABS if the SPE is unable to sell additional ABSs sufficient to cover the payments to investors. Implicit support refers to an ABS investor's expectation (or a sponsor's willingness) that the ABS sponsor will provide some form of support to permit an SPE issuing ABS to make payments on the ABS as due even if the sponsor is not formally obligated to do so, or that the sponsor will provide support in excess of what it may be formally obligated to provide.

[869] A money market fund must treat as an issuer of an ABS the SPE that issued it, as well as any person whose obligations constitute 10% or more of the principal amount of the qualifying assets of the ABS (a ''10% obligor'') and, if a 10% obligor is itself an SPE issuing ABS (''secondary ABS''), the fund also must treat as an issuer any 10% obligor of the secondary ABS. *See* rule 2a–7(c)(4)(ii)(D). In each case, the 10% obligor must be treated as the issuer of the portion of the ABS that its obligations represent. *Id. See also* rule 2a–7(a)(17) (definition of a guarantee); rule 2a–7(a)(9) (definition of a demand feature).

[870] *See, e.g.,* Frank J. Fabozzi & Vinod Kothari, Introduction to Securitization at 170 (2008) (''[T]here is almost necessarily an asset-liability mismatch [in an ABCP program], requiring the bank to provide liquidity support to the [ABCP] conduit''); Viral V. Acharya et al., *Securitization Without Risk Transfer,* National Bureau of Economic Research, Working Paper No. 15730 at 8–9 (Feb. 10, 2010) (noting that conduits issuing ABCP ''typically exhibit a significant maturity mismatch,'' in that they hold medium- to long-term assets but issue short term liabilities but are considered safe investments in part because ''the conduit's sponsor provides credit guarantees to the conduit, which ensures that the sponsor repays maturing asset-backed commercial paper in case the conduit is unable to repay itself''). The forms of support provided to ABCP programs vary, and not all ABCP programs are supported. *See, e.g.,* Covitz, *supra* note 71, at 8–9 (describing various types of ABCP programs and the types of support typically provided). The extent to which ABCP investors value the ABCP's support and its providers was demonstrated in the financial crisis when unsupported and less fully supported ABCP programs and those with weaker sponsors suffered disproportionate ''runs.'' *See id.* at 26–27.

[871] *See infra* note 872.

[872] *See, e.g.,* Comment Letter of the American Securitization Forum (Aug. 2, 2010) (available in File No. S7–08–10) (''ASF August 2010 Comment Letter'') (stating that ''ABCP investors understand that the payments on the financed assets may not be the source of payment on the short-term ABCP they are buying and that they must continuously monitor'' ''several factors, including the record of the program, the conduit sponsor's policies and experience, the creditworthiness of the financial institution(s) which provide liquidity and credit support, the conduit's investment guidelines, the maturity of the investor's portfolio, the conduit's disclosure practices and the circumstances in which the conduit may be prohibited from issuing ABCP''; opposing proposed asset-level disclosure requirements for ABCP because, among other reasons, ''ABCP investors focus less on asset-level information than investors do in other categories of asset-backed securities because an ABCP conduit's assets are not likely to be the primary source of payment of the ABCP—rather, ABCP is expected to be repaid from the proceeds of the issuance of additional ABCP or the proceeds of the credit and liquidity facilities that support the ABCP''); Comment Letter of the Securities Industry and Financial Markets Association (June 10, 2011) (available in File No. S7–14–11) (''[C]ustomer identity [*i.e.,* the customer whose assets are being financed] is irrelevant to the conduit investor, to whom the reputation of the sponsor and creditworthiness of the liquidity provider are of far greater interest.''). *See also* ASF 2009 Comment Letter, *supra* note 867 (explaining that ''most ABCP programs (and unsecured corporate CP programs) are supported by liquidity facilities'' and that ''ABCP investors cannot solely rely upon the cash flow from the financed assets to assure timely repayment of their securities since, in most cases, ABCP maturities are not match-funded to the underlying assets'').

[873] *See also supra* section III.J.1.

ABSs.[874] Subject to the exception, the amendments would require funds to treat the sponsor of an SPE issuing ABS as a guarantor of the ABS subject to rule 2a–7's diversification limitations applicable to guarantors and demand feature providers.[875] As a result, a fund could not invest in an ABS if, immediately after the investment, it would have invested more than 10% of its total assets in securities issued by or subject to demand features or guarantees from the ABS sponsor.[876]

As discussed above, we understand that money market funds investing in ABS, including some types of ABCP (and potentially other types of ABSs that may be developed in the future for which sponsor support may be particularly relevant), rely on sponsors' financial strength or their ability or willingness to provide liquidity, credit or other support to evaluate both the creditworthiness and liquidity of ABSs.

- Is our understanding correct? If not, is there a way to distinguish the situations described by the authors of the academic articles and comment letters we refer to above?
- If funds do not rely significantly on ABS sponsor support as described in these sources, why not, and what other factors do they consider? If funds do not receive any significant information about the underlying assets or obligors, which we understand they generally do not for ABCP, then on what are they relying other than the ABS sponsor's support? How do funds evaluate any mismatch between the time when the SPE's assets will be paid and the shorter duration of the ABCP issued by the SPE?
- This proposal assumes that, if an ABS has support (implicit or explicit), the support generally would be provided by the ABS sponsor.[877] Is this correct? Do persons other than ABS sponsor provide support for ABSs?
- Do money market funds today follow internal guidelines to limit their exposure to ABS sponsors beyond what rule 2a–7 requires?

We propose to require that, subject to an exception, all ABS sponsors be deemed to guarantee their ABSs. We have proposed to apply this requirement to all ABS sponsors because we are concerned that a proposal that applied only to sponsors of certain types of ABSs could become obsolete as new forms of ABSs are introduced. We recognize, however, that it may not be appropriate to require money market funds to treat ABS sponsors as guarantors in all cases. Accordingly, under our proposal, an ABS sponsor would not be deemed to guarantee the ABS if the money market fund's board of directors (or its delegate) determines that the fund is not relying on the ABS sponsor's financial strength or its ability or willingness to provide liquidity, credit, or other support to determine the ABS's quality or liquidity.[878] We believe that any incremental burden to make this determination should be minimal, as the money market fund would already have analyzed the security's credit quality and liquidity when assessing whether the security posed minimal credit risks and whether the fund could purchase the security consistent with rule 2a–7's limits on investment in ''illiquid securities.''[879] The exception would be analogous to current rule 2a–7's treatment of guarantees and demand features that a fund does not rely on and which may be disregarded under the rule.[880] We request comment on our approach and the proposed exception.

- Should we instead specify that only certain types of ABS sponsors, such as sponsors of ABCP, should be deemed to guarantee the ABS? If so, which kinds of ABS and why?
- Would the exception appropriately identify situations in which a money market fund should not be required to treat an ABS sponsor as a guarantor?
- Are there other exceptions we should consider? Should we, for example, provide that an ABS sponsor will not be deemed to guarantee the ABS if the fund's board of directors (or its delegate) determines that the sponsor's financial strength or its ability or willingness to provide liquidity, credit, or other support did not play a *substantial role* in the fund's assessment of the ABS's quality or liquidity?
- Do commenters agree that any incremental burden to determine if the fund is relying on the ABS sponsor's financial strength or its ability or willingness to provide liquidity, credit, or other support to determine the ABS's quality or liquidity should be minimal? If not, why not in light of the analysis the money market fund would be required to conduct of the ABS's credit quality and liquidity?
- Should we take a different approach, and require a money market fund to treat as a guarantor any provider of liquidity or credit support, whether to an ABS or any other type of security? Would a focus on the nature of any support, as opposed to the type of security subject to the support, be more effective than our proposed approach in requiring money market funds to treat as guarantors only providers of liquidity or credit support on which they rely in a way that is analogous to reliance on a guarantor? If we were to take this approach, should we include an exception under which some providers of liquidity or credit support would not be treated as guarantors? Should we use the same exception we propose for ABS sponsor support?

We discuss and seek comment on the economic effects of our ABS proposal together with the effects of our proposal

[874] Although persons other than the sponsor could support an ABS, we understand that, to the extent an ABS has explicit support, it typically is provided by the sponsor, and that investors in ABSs without explicit support may view the sponsor as providing implicit support. *See, e.g.,* ASF August 2010 Comment Letter, *supra* note 872 (''[T]he liquidity and credit support for the vast majority of ABCP conduits are provided by their financial institution sponsors.'').

[875] *See* proposed (FNAV and Fees & Gates) rule 2a–7(a)(16)(ii) (definition of guarantee). Under this proposal, the sponsor of an SPE for an ABS would be deemed to guarantee the entire principal amount of the ABS, with certain exceptions, unless the money market fund's board of directors (or its delegate) determines that the fund is not relying on the sponsor's financial strength or its ability or willingness to provide liquidity, credit or other support to determine the ABS's quality or liquidity and maintains a record of this determination. *Id.* Treating the ABS sponsor as a guarantor—as opposed to an issuer—recognizes that its support is more analogous to a guarantee, as the fund's exposure to the ABS sponsor is indirect and is not needed unless the assets underlying the ABS fail to pay in the timeframe required. The sponsor would not be deemed to have provided a guarantee for purposes of the following paragraphs of proposed (FNAV and Fees & Gates) rule 2a–7: (a)(11)(iii) (definition of eligible security); (d)(2)(ii) (credit substitution); (d)(3)(iv)(A) (fractional guarantees); and (e) (guarantees not relied on). We also propose a number of conforming amendments to other provisions of rule 2a–7 to implement the treatment of ABS sponsors as guarantors. *See* proposed (FNAV and Fees & Gates) rule 2a–7(a)(17)(ii) (defining a guarantee issued by a non-controlled person); proposed (FNAV and Fees & Gates) rule 2a–7(f)(4)(iii) (defining defaults for purposes of proposed rule 2a–7(f)(2) and (3) as applied to guarantees issued by ABS sponsors); proposed (FNAV) rule 2a–7(g)(6) and proposed (Fees & Gates) rule 2a–7(g)(8) (requiring periodic re-evaluations of any finding that the fund is not relying on the sponsor's financial strength or ability or willingness to provide support in determining an ABS's quality or liquidity); and proposed (FNAV and Fees & Gates) rule 2a–7(h)(6) (recordkeeping requirements for the periodic re-evaluations).

[876] *See* proposed (FNAV and Fees & Gates) rule 2a–7(d)(3)(iii) (diversification rules for demand features and guarantees). Rule 2a–7 currently applies a 10% diversification limitation on demand features and guarantees to 75% of funds' total assets. As discussed in *infra* section III. J.3, we propose to amend rule 2a–7 to apply the diversification limitation to all of a fund's assets rather than only 75%.

[877] *See, e.g., supra* note 874.

[878] *See* proposed (FNAV and Fees & Gates) rule 2a–7(a)(16)(ii). This determination must be documented and retained by the money market fund. *See id.;* and proposed (FNAV and Fees & Gates) rule 2a–7(h)(6).

[879] Proposed (FNAV and Fees & Gates) rule 2a–7(a)(11) (definition of ''eligible security'') and proposed (FNAV and Fees & Gates) rule 2a–7(d)(4) (portfolio liquidity).

[880] *See* rule 2a–7(c)(6).

to remove the twenty-five percent basket in section III.J.3, below, because both of these proposals would affect funds' investments in securities subject to guarantees (including ABS sponsors under our proposal) and demand features for purposes of rule 2a–7's 10% diversification requirement.

3. The Twenty-Five Percent Basket

We also propose to amend rule 2a–7 to tighten the diversification requirements applicable to guarantors and providers of demand features. The amendments would eliminate the so-called ''twenty-five percent basket,'' under which as much as 25% of the value of securities held in a fund's portfolio may be subject to guarantees or demand features from a single institution.[881]

Since 2007, a number of events have highlighted the risks to money market funds caused by their substantial exposure to providers of demand features and guarantees. For example, during the 2007–2008 financial crisis, many funds, particularly tax-exempt funds, were heavily exposed to bond insurers. In 2008, as much as 30% of the municipal securities held by tax-exempt money market funds were supported by bond insurance issued by monoline insurance companies.[882] This concentration led to considerable stress in the municipal markets when some of these bond insurers were downgraded during the financial crisis. For example, a lack of confidence in the bond insurers was a primary contributor to the market ''freeze'' that occurred in variable-rate demand notes in 2008 when money market funds and other investors reduced their purchases of these securities or sold them to the financial institutions that had provided demand features for the securities.[883] The freeze in turn strained the providers of the demand feature and also increased the interest the issuers of the securities were required to pay.[884] A lack of confidence in the creditworthiness of the bond insurers also caused dislocations in the market for tender option bonds, which use short-term borrowings from money market funds and others to finance longer-term municipal bonds.[885]

Some money market funds also were heavily exposed to a few major financial institutions that served as liquidity providers, including funds that owned variable-rate demand notes and tender option bonds as discussed above.[886] For example, some tax-exempt funds were significantly exposed to Dexia SA (''Dexia''), a European bank that provided demand features and guarantees for many municipal securities held by money market funds, when Dexia came under significant strain but ultimately received substantial support from various governments.[887] More recently, when Dexia again came under stress during the European debt crisis, many municipal issuers had to quickly find substitutes for demand features on which they relied to shorten their securities' maturities.[888] These events highlighted the risk a money market fund assumes when it relies heavily on a single guarantor or demand feature provider.[889] Our proposal to remove the twenty-five percent basket is designed to reduce this risk by limiting the extent to which a money market fund becomes exposed to a single guarantor or demand feature provider.

Our diversification proposals, including the proposal to remove the twenty-five percent basket,[890] are designed to provide a number of benefits, as discussed in more detail in section III.J.1 above. And although because we do not have the information necessary to provide a reasonable estimate, and thus are unable to quantify these benefits for the reasons discussed in that section, we have considered data filed on Form N–MFP in assessing the impacts of these proposals. Specifically, our staff's review of data filed on Form N–MFP suggests that our ABS and twenty-five percent basket diversification proposals (treating only ABCP sponsors as guarantors for purposes of this analysis)[891] would have little impact on the majority of money market funds, which do not make use of the twenty-five percent basket, and would likely

[881] Rule 2a–7 currently applies a 10% diversification limit on guarantees and demand features only to 75% of a money market fund's total assets. *See* rule 2a–7(c)(4)(iii)(A). The money market fund, however, may only use the twenty-five percent basket to invest in demand features or guarantees that are first tier securities issued by non-controlled persons. *See* rule 2a–7(c)(4)(iii)(B) and (C). Accordingly, in conforming amendments we would delete rule 2a–7(a)(10), which defines a demand feature issued by a non-controlled person, because the term is used only in connection with the twenty-five percent basket. We also propose certain amendments to clarify that a fund must comply with this 10% diversification limit immediately after it acquires a security directly issued by, or subject to guarantees or demand features provided by, the institution that issued the security or provided the demand feature or guarantee. *See* proposed (FNAV and Fees & Gates) rules 2a–7(d)(3)(i) and (iii). We believe this amendment reflects funds' current practices and is consistent with rule 2a–7's current requirements.

[882] *See, e.g.,* U.S. Securities and Exchange Commission Division of Trading and Market's Director Erik R. Sirri, Testimony before the Committee on Financial Services, U.S. House of Representatives (Mar. 12, 2008), *available at http://www.sec.gov/news/testimony/2008/ts031208ers.htm.* A monoline insurance company generally is an insurance company that only provides guarantees to issuers of securities.

[883] *See, e.g.,* Joan Gralla, *Variable-Rate Note Market Now Freezing-Sources,* Reuters, Feb. 26, 2008, *available at http://www.reuters.com/article/2008/02/26/sppage012-n25273728-oisbn-idUSN2527372820080226?sp=true* (''One of the main culprits causing the market for variable-rate demand notes to seize up is the troubled bond insurers that guarantee them. This is the same factor that has caused the $330 billion auction-rate note market to get hit with billions of dollars of failed auctions every day since late January.'').

[884] *Id.* (''I had heard there was tremendous stress in the variable-rate demand notes because money market (funds) and mutual investors have been putting back a lot of their variable-rate demand notes and dealers were getting overwhelmed on their balance sheets,' said Matt Fabian, managing director of Municipal Market Advisors, in Concord, Massachusetts.''); Liz Rappaport, *New Monkey, Same Backs: Another Debt Market For Governments Loses Buyers, and Rates Rise,* Wall St. J., Feb. 28, 2008 (''Just like many issuers of auction-rate securities whose interest costs soared after auctions for some of their debt failed, an increasing number of municipalities are being hit with sharply higher interest on their variable-rate demand notes because dealers of the debt are having trouble selling it.'').

[885] Tom Lauricella and Liz Rappaport, *How the Crunch Has Hit Corner Of Muni Market: 'Tender Option Bonds' Lose Investor Favor; Aberrations in Yield,* Wall St. J., Jan. 31, 2008 (noting that the lack of buyers for some tender option bonds caused in part by a lack of confidence in the bond insurers caused billions of dollars of the bonds to accumulate at banks and broker-dealers; caused some hedge funds to suffer ''double-digit losses''; caused the yield on the bonds to increase significantly; and ''caused dislocations in the wider municipal-bond market'').

[886] *See, e.g., supra* notes 883–885 and accompanying text; Markus K. Brunnermeier, *Deciphering the Liquidity and Credit Crunch 2007–2008,* 23 J. Econ. Perspectives 77, 87, Winter 2009.

[887] *See, e.g.,* Bob Ivry, *Why a Foreign Bank Feasted on Fed Funds,* Bloomberg Businessweek, Apr. 7, 2011, *available at http://www.businessweek.com/magazine/content/11_16/b4224038555674.htm* (''If Dexia had gone 'bankrupt, it could have been a catastrophe for municipal finance and money funds.' ''). Dexia was the ''biggest recipient of funds from the Federal Reserve discount window during the financial crisis,'' borrowing ''as much as $37 billion.'' *Id.* (describing the support Dexia received from various governments around the world and explaining Dexia's significance in the municipal market and that ''[d]emands to back up muni bonds sapped Dexia so much that it was 'two days from bankruptcy.' '').

[888] *See, e.g.,* Michael Corkery, *Global Economic Turmoil: Dexia's Troubles Cross Atlantic, Cost U.S. Cities, Towns,* Wall St. J., Oct. 5, 2011.

[889] Although we determined to further restrict funds' ability to acquire second tier securities in the 2010 Adopting Release, we did not at that time consider eliminating the twenty-five percent basket. *See* 2010 Adopting Release, *supra* note 92, at n.59.

[890] *See supra* note 881.

[891] Our staff assumed when reviewing the Form N–MFP data that any fully or partially supported ABCP owned by a fund would result in the sponsor guaranteeing the ABCP. For this purpose, our staff considered an ABCP program to be fully supported when the program's investors are protected against asset performance deterioration and primarily rely on the ABCP sponsor to provide credit, liquidity, or some other form of support to ensure full and timely repayment of ABCP, and considered an ABCP program to be partially supported when the ABCP sponsor, although not fully supporting the program, provided some form of credit, liquidity, or other form of support. *See also infra* note 893.

have a minimal impact on those funds that do. Approximately 109 funds, or 19% of all funds submitting Form N–MFP for February 28, 2013, reported that they made use of the twenty-five percent basket for guarantees and demand features, even when we treat sponsors of ABCP as guarantors (and thus subject to a 10% diversification limitation).[892] Thus, most money market funds do not use the twenty-five percent basket. Those funds that do use the twenty-five percent basket do not make significant use of it. The 109 funds that used the twenty-five percent basket had, on average, 3.9% of their assets invested in excess of the 10% diversification limitation we propose today (*i.e.,* in the twenty-five percent basket).[893] And although we understand that money market funds may have made greater use of the twenty-five percent basket in the past (and might do so in the future if we do not adopt this proposal), we are concerned that funds were exposed to concentrated risks inconsistent with the purposes of rule 2a–7's diversification requirements in the past as discussed above. Money market funds' current relatively limited use of the basket suggests that this is an opportune time to remove it.

The principal effect of the amendments may be to restrain some managers of money market funds from making use of the twenty-five percent basket in the future, under perhaps different market conditions.[894] Our diversification proposals would deny fund managers some flexibility in managing fund portfolios and could decrease the fund yields. To assess these proposals' effect on yield, we examined whether the 7-day gross yields of funds that use the twenty-five percent basket were higher than the 7-day gross yields for those funds that do not.[895] We found: (i) for national tax-exempt funds, the average yield for funds using the twenty-five percent basket was the same (0.16%) as the average yield for national tax-exempt funds that did not use the twenty-five percent basket; (ii) for single state funds, the average yield for funds using the twenty-five percent basket was the same (also 0.16%) as the average yield for single state funds that did not use the twenty-five percent basket; and (iii) for prime money market funds, the average yield for funds using the twenty-five percent basket was 0.27% as compared to the average yield for prime money market funds that did not use the twenty-five percent basket of 0.25%.[896] The prime money market fund yield differences may not, of course, be caused by the use of the twenty-five percent basket, but may instead reflect the overall risk tolerance of fund managers that take advantage of the twenty-five percent basket.

Eliminating the twenty-five percent basket also may increase the costs of monitoring the credit risk of funds' portfolios or make that monitoring less efficient, to the extent they are more diversified under our proposal and money market fund advisers must expend additional effort to monitor the credit risks posed by a greater number of guarantors and demand feature providers. We are unable to quantify these costs, however, because we do not have the information necessary to provide a reasonable estimate to predict whether funds would be required to expend more effort under our proposals (or if so, how much more). A money market fund that could not acquire a particular guarantee or demand feature under our proposal could, for example, be able to acquire a guarantee or demand feature from another institution in which the fund already was invested, at no additional monitoring costs to the fund.

Our proposed amendments would require funds that use the twenty-five percent basket, or that would use it in the future, to either choose not to acquire certain demand features or guarantees (if the fund could not assume additional exposure to the provider of the demand feature or guarantee) or to acquire them from different institutions. Funds that choose the latter course could thereby increase demand for providers of demand features and guarantees and increase competition among their providers. If new entrants do not enter the market for demand features and guarantees in response to this increased demand, eliminating the twenty-five percent basket could result in money market funds acquiring guarantees and demand features from lower quality providers than those the funds use today. If new entrants do enter the market (or if current participants increase their participation), the effect on money market funds would depend on whether these new entrants (or current participants) are of high or low credit quality as compared to the providers money market funds would use absent our proposal.

Although we recognize that money market funds could use lower credit quality guarantors and demand feature providers under our proposals, our data show that most funds do not use the twenty-five percent basket (and funds that use it do so to a limited extent) and thus we believe that this negative effect is unlikely to occur. And under our proposals, money market funds would not be required to include more than 10 guarantors or demand feature providers in their portfolios, suggesting it is unlikely that they would be forced to resort to low credit quality guarantors or demand feature providers. Indeed, our staff's review of Form N–MFP data shows that, as of February 28, 2013, the assets in money market funds' twenty-five percent baskets (*i.e.,* amounts in excess of the rule's 10% diversification limit for guarantor and demand feature providers) were invested in securities subject to demand features and guarantees from only 13 institutions, but there were a total of 98 first tier guarantors (including ABCP sponsors) and demand feature providers held by money market funds collectively as of that date.

[892] Based on our review, only prime funds (which tend to have relatively concentrated positions in ABSs) and tax-exempt funds (which tend to have relatively concentrated positions in securities subject to demand features) used the twenty-five percent basket.

[893] This estimate likely overstates the number of funds and the amount of money market funds' assets that could be affected by our ABS proposals for three reasons. First, it assumes that any fully or partially supported ABCP owned by a fund would result in the sponsor guaranteeing the ABCP. Under our proposal, however, an ABCP (or other ABS) sponsor would not be deemed to guarantee the ABCP if the board (or its delegate) determines the fund is not relying on the sponsor's financial strength or its ability or willingness to provide support to determine the ABCP's quality or liquidity. We did not assume sponsors of other types of ABSs guaranteed those ABSs because we understand that other forms of ABS offered to money market funds either do not typically have sponsor support or, if they are supported, the support typically is in the form of a guarantee or demand feature, which would already be included in our calculation of exposure to providers of demand features and guarantees. Second, Form N–MFP data does not differentiate between funds that would have had exposure in excess of 10% upon the acquisition of a demand feature or guarantee (which would not be permitted under our proposed amendments) and those funds that were under that level of exposure at the time of acquisition but the fund later decreased in size, increasing the fund's exposure above the 10% limit (which would be permitted under our proposed amendments). Third, where a fund owned securities issued by or subject to demand features or guarantees from affiliated institutions, we treated the separate affiliated institutions as single institutions for purposes of these estimates.

[894] If we were to adopt the proposed amendments, funds with investments in excess of those permitted under the revised rule would not be required to sell the excess investments to come into compliance. The proposed amendments would require a fund to calculate its exposure to issuers of demand features and guarantees as of the time the fund acquires a demand feature or guarantee or a security directly issued by the issuer of the demand feature or guarantee. *See* proposed (FNAV and Fees & Gates) rule 2a–7(d)(3)(i) and (iii).

[895] We assumed that any fully or partially supported ABCP owned by a fund would result in the sponsor guaranteeing the ABCP. *See supra* note 893.

[896] These averages are derived from Form N–MFP data as of February 28, 2013, weighted by money market funds' assets under management.

Issuers also could incur costs if they were required to engage different providers of demand features or guarantees under our proposal, which could negatively affect capital formation. This could occur because an issuer might otherwise have sought a guarantee or demand feature from a particular bank, but might choose not to use that bank because the money market funds to which the issuer hoped to market its securities could not assume additional exposure to the bank. If issuers were unable to receive demand features or guarantees from banks (or other institutions) to which they would have turned absent our amendments, they would have to engage different banks, which could make the offering process less efficient and result in higher costs if the different banks charged higher rates. Issuers of securities with guarantees or demand features (*e.g.,* issuers of longer-term securities that can be sold to money market funds only with a demand feature) also could be required to broaden their investor base or seek out different providers of guarantees or demand features under our proposals, which could make their offering process less efficient or more costly.

We request comment on the impact on portfolio management of our proposed elimination of the twenty-five percent basket together with our proposal to remove the twenty-five percent basket.

- As noted above, our review of Form N–MFP data suggests that most funds do not use the twenty-five percent basket. Is this correct?
- Would our proposals increase demand for providers of demand features and guarantees?
- Would there be a significant impact on fund yield, and if so, how significant? Our review of Form N–MFP data also suggests that our proposal would have very little impact on funds that use the twenty-five percent basket today. Is this correct?
- To what extent might a money market fund use lower credit quality or higher cost guarantors and demand feature providers in order to meet the stricter diversification requirements that we propose? Are there enough guarantors and demand feature providers to allow money market funds to meet these diversification limitations?
- As discussed in section III.E above, concerns about the creditworthiness of guarantors and demand feature providers have reduced the amount of VRDNs outstanding since 2010, and this trend is likely to continue irrespective of changes in the money market fund industry because of potential downgrades to credit and liquidity enhancement providers and potential bank regulatory changes may increase the cost to financial institutions of providing such guarantees.[897] How would these factors affect money markets funds' ability to acquire demand features and guarantees under our proposal, and the cost and quality of those guarantees and demand features?
- How should we evaluate the tradeoff between providing funds flexibility and limiting the risks to funds posed by concentrated exposures and how might we quantify it? We request commenters asserting that we retain the twenty-five percent basket provide data to help us evaluate these competing considerations. We also request those commenters to address the extent to which their assets exceed the limits our proposals would establish, and what difficulties they would encounter in identifying alternative securities with credit qualities comparable to their existing investments.
- To what extent would issuers of securities with guarantees or demand features (*e.g.,* issuers of longer-term securities that can be sold to money market funds only with a demand feature) be required to broaden their investor base or seek out different providers of guarantees or demand features under our proposal? To what extent would this increase issuers' costs or reduce the efficiency of the offering process? Would some issuers reduce their reliance on guarantees and demand features? Would issuers incur higher underwriting fees if placing securities without guarantees or demand features requires more effort? What effect on capital formation would occur if issuers are unable to find alternative investors and/or have to sell their securities at less favorable rates? Would our proposals make offerings less efficient if issuers need to spend more time and effort identifying purchasers of their securities, and if so, to what extent?
- Would eliminating the twenty-five percent basket make it difficult for issuers of ABSs and securities subject to demand features or guarantees to find money market fund investors to purchase their securities? As noted above, most funds do not use the twenty-five percent basket and, in addition, many money market funds as of February 28, 2013, had invested only a small portion of their assets in ABSs and securities subject to demand features or guarantees, suggesting that issuers have a ready supply of money market fund investors eligible to purchase their securities. Indeed, Form N–MFP data as of February 28, 2013, shows that over 99% of total money market fund assets are not in funds' twenty-five percent baskets. To the extent issuers or underwriters believe they would have any difficultly in identifying money market investors as a result of our proposal, we request that they explain why and quantify any resulting costs. As noted above, data on Form N–MFP shows that many funds would be eligible to purchase ABSs and securities subject to demand features and guarantees under our proposals.
- In assessing the impacts of our ABS proposal and our proposal to eliminate the twenty-five percent basket we have considered, as noted above, that some funds had investments as of February 28, 2013 in excess of the limits our proposals would impose. We request comment from any funds with investments in excess of these limits on whether their investments exceeded these limits upon acquisition (which would not be permitted under our proposed amendments) or if the funds' investments were below the limits at the time of acquisition but the fund later decreased in size (which would be permitted under our proposed amendments). For example, under our proposal, a fund would not be permitted to acquire ABCP sponsored by a bank if immediately thereafter more than 10% of its assets were invested in securities issued by or subject to demand features or guarantees from that bank. But the investment would be permitted if immediately after the investment the fund was below the 10% limit, even if the fund later decreased in size and the investment later exceeded the 10% limit.
- Although our proposal would remove the twenty-five percent basket, we are not proposing to change the application of rule 2a–7's 5% issuer limit to single state funds, which today applies only to 75% of a single state fund's total assets.[898] We historically have applied the issuer diversification limitation differently to single state funds, recognizing that ''single state funds face a limited choice of very high quality issuers in which to invest'' and, therefore, that there is a risk that ''too stringent a diversification standard could result in a net reduction in safety for certain single state funds.'' [899] The

[897] *See, e.g., supra* notes 601–602 and accompanying text.

[898] *See* rule 2a–7(c)(4)(i)(B).

[899] *See* 1996 Adopting Release, *supra* note 247, at text following n.38.

market for demand features and guarantees, in contrast, is national and may not be subject to the same supply constraints as is the market for issuers in which single state funds may directly invest. Should we nonetheless continue to permit single state funds to continue to use the twenty-five percent basket for the same reasons that we historically have applied rule 2a–7's issuer diversification limit differently to those funds? Why or why not? Would single state funds under our proposal have difficulties in identifying high quality issuers in which to invest even though we do not propose to change rule 2a–7's issuer diversification limit as applied to those funds? Why or why not?

We do not expect that our ABS and twenty-five percent basket diversification proposals would result in operational costs for funds. We understand that money market funds generally have systems to monitor their exposures to guarantors (among other things) and to monitor the funds' compliance with rule 2a–7's current 10% demand feature and guarantee diversification limit. We expect that money market funds could use those systems to track exposures to ABS sponsors under our proposal and could continue to track the funds' compliance with a 10% demand feature and guarantee diversification limit. To the extent a money market fund did have to modify its systems as a result of our ABS and 25% basket diversification proposals, we expect that the money market fund would make those modifications when modifying its systems in response to our proposal to require money market funds to aggregate exposure to affiliated issuers for purposes of rule 2a–7's 5% diversification limit, for which we provide cost estimates above.[900] Because the costs estimated above are those associated with activities typically involved in making systems modifications, we expect they also would cover any systems modifications associated with our ABS and 25% basket diversification proposals.

Finally, we note that Investment Company Act rule 12d3–1 also refers to the twenty-five percent basket. That rule generally permits investment companies to purchase certain securities issued by companies engaged in securities-related activities notwithstanding section 12(d)(3)'s limitations on these kinds of transactions. Among other things, rule 12d3–1 provides that the acquisition of a demand feature or guarantee as defined in rule 2a–7 will not be deemed to be an acquisition of the securities of a securities-related business provided that ''immediately after the acquisition of any Demand Feature or Guarantee, the company will not, with respect to 75 percent of the total value of its assets, have invested more than ten percent of the total value of its assets in securities underlying Demand Features or Guarantees from the same institution.'' [901]

- Should we revise rule 12d3–1 to apply this diversification requirement with respect to all of an investment company's total assets, rather than just 75% of them, for consistency with our amendments to rule 2a–7?
- Would conforming rule 12d3–1 to rule 2a–7 as we propose to amend it affect investment companies other than money market funds, which also may use rule 12d3–1? If so, how and to what extent?

4. Additional Diversification Alternatives Considered

We could require money market funds to be more diversified by reducing rule 2a–7's current 5% and 10% diversification limits.[902] We are concerned that reducing these limits, particularly in light of today's diversification proposals, could lead money market funds to invest in relatively lower quality securities.[903] Doing so could increase the likelihood of a default or other credit event affecting a money market fund while diminishing the impact of such an event on the fund. We also recognize that lowering the diversification limits would not necessarily eliminate the possibility of a default triggering shareholder redemptions: The Reserve Primary Fund held only 1.2% of its assets in Lehman Brothers commercial paper.[904] Any amendments would need to balance the potential benefits of greater diversification that would result from our reducing rule 2a–7's current 5% and 10% diversification limits with the potential negative effects that could result from doing so and particularly that lower limits could lead funds to assume additional credit risk.

Nonetheless, there could be benefits in reducing these limits. For example, the 10% limit permits a money market fund to have twice as much exposure to a single provider of a demand feature or guarantee than if the fund were to invest in securities directly issued by the provider, which direct investments would be subject to the rule's 5% limit. Rule 2a–7 permits a money market fund to take on greater indirect exposures to providers of demand features and guarantees (as opposed to direct investments in them) because, rather than looking solely to the issuer, the money market fund would have two potential sources of repayment—the issuer whose securities are subject to the demand features or guarantees and the providers of those features if the issuer defaults. Both the issuer and the demand feature provider or guarantor would have to default at the same time for the money market fund to suffer a loss. And if a guarantor or demand feature provider were to come under stress, the issuer may be able to obtain a replacement.[905]

As discussed in more detail in section III.K below, however, rule 2a–7 permits a money market fund, when determining if a security subject to a guarantee meets the rule's credit quality standards, to rely exclusively on the credit quality of the guarantor.[906] That the money market fund has two sources of repayment—the issuer and the guarantor—therefore may not meaningfully reduce the risks of the investment in all cases because the issuer of the guaranteed securities need not satisfy rule 2a–7's credit quality requirements. If the issuer of the guaranteed securities is of lesser credit quality, allowing the money market fund to have up to 10% of its assets indirectly exposed to the guarantor may not be justified.

And although an issuer could attempt to obtain a substitute guarantor or demand feature provider if its current provider came under stress, there is no assurance the issuer would be successful. Certain providers of

[900] *See supra* note 859 and accompanying text.

[901] Rule 12d3–1(d)(7)(v). We are proposing to amend rule 12d3–1 to update cross references in the rule to rule 2a–7's definitions of the terms ''demand feature'' and ''guarantee.'' *See infra* note 967.

[902] *See, e.g.,* FSOC Proposed Recommendations, *supra* note 114, at 55–57 (seeking comment on reducing the rule 2a–7's 5% issuer limit (and consolidating exposures to affiliated entities) in connection with a reform option under which money market funds also would have risk-based NAV buffers).

[903] *See, e.g.,* 2009 Proposing Release, *supra* note 31, at section II.D (noting that ''[e]ven a diversification limitation of one percent would not preclude a fund from breaking a buck if the security should sustain sufficient losses as did the securities issued by Lehman Brothers,'' and that ''such a diversification limit may force funds to invest in relatively lower quality securities.''

[904] *See, e.g.,* 2009 Proposing Release, *supra* note 31, at text following n.221.

[905] *See, e.g.,* 1993 Proposing Release, *supra* note 54, at n.83 and accompanying text (observing that, if the guarantor of one of the money market fund's securities comes under stress, ''issuers or investors generally can either put the instrument back on short notice or persuade the issuer to obtain a substitute for the downgraded institution'').

[906] Rule 2a–7(c)(3)(iii) (''A security that is subject to a Guarantee may be determined to be an Eligible Security or a First Tier Security based solely on whether the Guarantee is an Eligible Security or First Tier Security, as the case may be.'').

guarantees or demand features may limit themselves to providing such features for only specific types of securities, such as a state that only provides these features for certain bonds within the state. If a state came under stress, the issuers of bonds within the state may be unable to obtain substitute guarantors. That certain providers of guarantees or demand features may limit themselves to providing such features for only specific types of securities also may create further concentration risk, under which the risks of the provider of the features may be correlated with the risks of the underlying securities.

We also considered proposing industry concentration limits.[907] Our proposal to require money market funds to aggregate their exposures to affiliated issuers is designed to reduce the risks to which a fund would be exposed if it became overexposed to the group collectively, but securities issued by separate groups of affiliates in the same industry also could come under stress at the same time. For example, a financial crisis or other event that affected the financial sector disproportionately likely would cause securities issued by financial institutions generally to decline in value even where the financial institutions are not affiliated with each other. This is relevant to prime money market funds in particular because, as a group, they invest a large percentage of their assets in securities issued by financial institutions.

Defining various industry sectors with sufficient precision for a new industry diversification requirement could be difficult, however. In deciding not to propose industry concentration limits today, we also considered the comments we received in response to our request for comment in 2009 on whether to reduce rule 2a–7's current diversification limits and whether to introduce new industry diversification requirements.[908] Most commenters opposed these reforms. Commenters opposed reducing rule 2a–7's current 5% and 10% diversification limits because, among other reasons, the reductions could increase risks to funds by requiring the funds to invest in relatively lower quality securities.[909] Commenters opposed industry diversification requirements because they would be impractical, among other reasons.[910] At least one commenter argued that our concerns could be better addressed through what were then proposals to further limit certain risks in funds' portfolios and to increase their liquidity.[911]

We are proposing enhancements to money market funds' stress testing processes, as discussed in more detail in section III.L, below. Those enhancements are designed, together with all of the other changes we propose today, to address some of the risk that may result from a money market fund concentrating its investments in particular industries, or having exposures within the rule's 5% and 10% diversification limits. For example, we propose to require money market funds' advisers to assume as part of their stress testing that the funds' portfolio securities will present correlated risks. Our structural reforms are designed to better position a money market fund to bear a credit loss. Our liquidity fees and gates proposal is designed to provide the fund with tools to mitigate the harm that can result from a credit event. Our floating NAV proposal is designed to more fairly apportion such a loss, thereby reducing the incentive to redeem in anticipation of it.

We request comment on the alternative approaches we considered.

- Should we reduce rule 2a–7's current 5% diversification limits? If so, to what extent? Would lower diversification limits increase the likelihood of a default or other credit event affecting a money market fund while diminishing the impact of such an event on the fund? We request that commenters address the tradeoffs of lower diversification limits for different types of money market funds.
- Should we reduce rule 2a–7's current 10% diversification limits on securities with a guarantee or demand feature from any one provider? Would lowering this limit increase the likelihood of a default or other credit event affecting a money market fund or diminish the impact of such an event on the fund?
- Should we continue to distinguish between a fund's exposure to guarantors and demand feature providers and direct issuers by providing different diversification limitations for these exposures? Does the difference in the nature of a fund's exposure to a guarantor or demand feature provider as opposed to a direct issuer warrant disparate diversification requirements? If we were to adopt a single diversification limitation that aggregated direct investments and guarantees and demand features, should we use the rule's current 5% threshold for direct investments? If not, should it be higher or lower? At what level and why? Should we continue to apply different diversification limitations but use limitations other than 5% (direct investments) and 10% (securities subject to demand features and guarantees)?
- What types of providers that are not affiliated with the issuer of a security provide such guarantees or demand features? To what extent do providers of guarantees and demand features limit themselves to providing features for

[907] *Id. See also, e.g.,* Robert Comment FSOC Comment Letter, *supra* note 67 (explaining that his review of a sample of 50 prime funds showed that ''bank issued money market instruments of all types (notes, commercial paper, large CDs, time-deposits and repo), comprised 53% of the holdings of prime funds in mid-2008 and 8% in mid-2012 (46% and 45%, respectively, excluding repo),'' with much of this issued by non-U.S. banks, and concluding that ''[s]ector diversification apparently is not relevant to funds' compliance with the diversification provisions of rule 2a–7, but it plainly should be'').

[908] *See* 2009 Proposing Release, *supra* note 31, at section II.D.

[909] *See, e.g.,* ICI 2009 Comment Letter, *supra* note 281 (''Further restricting the diversification limits would only heighten this problem by forcing money market funds to use institutions they may be less comfortable with to meet new diversity requirements.''); Schwab 2009 Comment Letter, *supra* note 350 (stating that it ''would not support any changes to the diversification requirements set forth in the current rule, as more stringent diversification requirements may force a fund to invest in lower quality securities than those in which it might have otherwise invested''); Comment Letter of Stradley Ronon (Sept. 8, 2009) (available in File No. S7–11–09) (''Stradley Ronon 2009 Comment Letter'') (''We understand that a fund might find it necessary to ease its quality standards if it had to satisfy more stringent diversification standards. This easing could threaten share stability and increase the risk that the fund will hold a defaulted security.''). *But see, e.g.,* Comment Letter of James J. Angel (Sept. 8, 2009) (available in File No. S7–11–09) (noting that ''[i]f a fund never holds more than ½ of one percent of its assets in any paper issued by any one issuer, then even a complete loss from that one issuer would not result in that fund breaking the buck,'' but stating that he is ''not, however, proposing that all funds be reduced to a maximum exposure of ½ of 1% to any issuer: This could be problematic for smaller funds that might find it overly expensive to buy smaller quantities of commercial paper'').

[910] *See, e.g.,* Stradley Ronon 2009 Comment Letter, *supra* note 909 (stating that ''[a] more stringent industry concentration requirement would not provide a meaningful method to mitigate risk'' because ''[d]ifferent fund groups define industries in a variety of ways, especially given the erosion of boundaries between industries and the lack of guidance from the Commission in this area''; also stating that ''an industry concentration provision to limit exposure to the financial sector is not practical, because a significant proportion of money market investments carries exposure to the financial sector (including municipal securities, certificates of deposit, repurchase agreements, commercial paper and asset-backed commercial paper).''); Invesco 2009 Comment Letter, *supra* note 195 (''We also do not believe an industry concentration limit in rule 2a–7 would be an effective risk management control given the inconsistency of industry classifications, which currently can differ between advisers.'').

[911] *See* Invesco 2009 Comment Letter, *supra* note 195 (''The Commission's proposals to limit portfolio quality risk and increase available liquidity are stronger and more appropriate tools [than industry diversification requirements] for the Commission to employ in reducing the risk of redemption pressures to money market fund shareholders.'').

specific types of securities? Does this limitation pose any particular risks? If so, what are they?

• Should we impose industry diversification requirements on money market funds? If so, what level of concentration in a single industry would be appropriate? How would we define industries for this purpose?

• We request that commenters address how any risks that may result from a money market fund concentrating its investments to an extent in particular industries, or from having exposures within the rule's 5% and 10% diversification limits, would (or would not) be mitigated by the other amendments that we propose today.

• If we were to reduce rule 2a–7's current diversification limits, could that result in more homogeneity and increased correlation among money market fund portfolios? If so, what effect, if any, would there be on systemic risk?

*K. Issuer Transparency*

In 2008, monoline insurers that provided bond insurance to municipal issuers were downgraded, forcing some advisers to tax-exempt money market funds to quickly obtain information about issuers of VRDNs and other municipal securities they held to determine whether the securities continued to present minimal credit risks (and whether to exercise demand features).[912] Two years later, in 2010, we amended our rules to improve the transparency of information about VRDNs to advisers to money market funds and other investors by prohibiting broker-dealers from underwriting VRDNs unless the issuer had committed to provide ongoing information about itself and the securities, including financial data, through the Municipal Securities Rulemaking Board's Electronic Municipal Market Access system.[913] Last year, we reported our concern that issuers' compliance with their continuing contractual disclosure obligations has been inconsistent, at times leaving money market fund and investors exposed.[914] We recommended that Congress give us greater authority to require municipal issuers to provide the market with better information, but such authority, if forthcoming, could not be implemented for some time.[915]

Rule 2a–7 permits a money market fund when determining if a security subject to a guarantee meets the rule's credit quality standards to rely exclusively on the credit quality of the guarantor.[916] As a result of this and the rule's treatment of exposures to guarantors and demand feature providers for diversification purposes (the 10% limit on providers of guarantees and demand features compared to the 5% issuer limit), a money market fund can have greater indirect exposure to a guarantor than the money market fund could assume if it were investing in the guarantor directly,[917] and may have minimal information about the issuer subject to the guarantee. We request comment on whether we should require money market funds to obtain financial data on the underlying issuers whose securities are subject to guarantees.[918]

• If we were to require money market funds to obtain financial data about the issuers of securities subject to guarantees, should we specify in detail the data a fund must obtain? If the security is an ABS, what kind of information should we require funds to obtain about the assets held by the SPE that issued the ABS? Should we only require a money market fund to obtain the financial data when the security is subject to a guarantee from a guarantor to which the fund has a greater than 5% exposure?

• Should we require money market funds to obtain this data only when it is available? Such an approach would prevent money market funds from forgoing investment opportunities solely because financial data is not available. Should we specify when financial data would be available for this purpose? If so, in what circumstances do commenters expect financial data would be readily available? In what ways could they make better use of that data? Should we specify, for example, that financial data would be available for this purpose if it were available on the Municipal Securities Rulemaking Board's Electronic Municipal Market Access system? Have money market funds found data currently available on that system to be helpful? If so, in what ways do money market funds use that data?

• Should we specify how current any financial data must be? Should we specifically require money market funds to review the data when the fund acquires the security or simply to retain it for use should there be a problem with the guarantor? Would money market funds have to hire additional credit analysts to meet such a requirement? What costs would this impose?

• Would requiring money market funds to have financial data about these issuers support our continuing to provide different diversification limitations for direct and indirect exposures, as discussed above? Would the data be useful to money market funds if a guarantor came under stress? Should we adopt a more stringent diversification limit (*e.g.,* a single 5% limit that included direct and indirect exposures) and also require money market funds to obtain financial data about the issuers whose securities are guaranteed?

[912] To our knowledge, none of these funds experienced difficulty in maintaining their stable net asset value or received support from an affiliate. A monoline insurance company generally is an insurance company that only provides guarantees to issuers of securities. *See supra* note 882.

[913] *See* Amendment to Municipal Securities Disclosure, Exchange Act Release No. 62184A (May 26, 2010) [75 FR 33100 (June 10, 2010) (''Municipal Disclosure Release''), at nn.110–111 (noting that ''most holders of [variable rate demand notes] are money market funds'' and that the ''availability of continuing disclosure information should facilitate the fulfillment'' of the funds' ''obligation to monitor the securities in their funds''). *See also* Comment Letter of the Investment Company Institute (Sept. 8, 2009) (available in File No. S7–15–09) ([T]he availability of continuing disclosure information regarding [variable rate demand notes] would greatly benefit investors by enhancing their ability to make and monitor their investment decisions and protect themselves from misrepresentations and questionable conduct in this segment of the municipal securities market.'').

[914] *See* U.S. Securities and Exchange Commission, Report on the Municipal Securities Market (July 31, 2012), at 62, *available at http://www.sec.gov/news/studies/2012/munireport073112.pdf.*

[915] *See id.* at section V (legislative recommendations).

[916] Rule 2a–7(c)(3)(iii) (''A security that is subject to a Guarantee may be determined to be an Eligible Security or a First Tier Security based solely on whether the Guarantee is an Eligible Security or First Tier Security, as the case may be.''). *See also* Technical Revisions to the Rules and Forms Regulating Money Market Funds, Investment Company Act Release No. 22921 (Dec. 2, 1997) [62 FR 64968 (Dec. 9, 1997)] (''1997 Adopting Release''), at section I.B.1.b. A guarantee includes an unconditional demand feature that is not provided by the issuer of the underlying security. Rule 2a–7(a)(17).

[917] As discussed above, a money market fund could invest not more than 5% of its assets in securities directly issued by a bank, but could invest up to 10% of its assets in securities issued by or subject to guarantees provided by the bank. *See supra* notes 838–840 and accompanying text.

[918] This data could be important to a money market fund if a guarantor came under stress, putting the fund and its adviser in a better position to evaluate the underlying issuer's creditworthiness, and whether to dispose of the security by exercising any demand feature. *See also* rule 2a–7(c)(7)(i)(C) (''In the event that after giving effect to a rating downgrade, more than 2.5% of the fund's Total Assets are invested in securities issued by or subject to Demand Features from a single institution that are Second Tier Securities, the fund shall reduce its investment in securities issued by or subject to Demand Features from that institution to no more than 2.5% of its Total Assets by exercising the Demand Features at the next succeeding exercise date(s), absent a finding by the board of directors that disposal of the portfolio security would not be in the best interests of the money market fund.'').

*L. Stress Testing*

In 2010, we adopted amendments to rule 2a–7 that, for the first time, required the board of directors of each money market fund to adopt procedures providing for periodic stress testing of the money market fund's portfolio, which we refer to as the stress testing requirements.[919] We adopted this requirement based on our belief that ''stress testing procedures would provide money market fund boards a better understanding of the risks to which the fund is exposed and would give managers a tool to better manage those risks.'' [920]

Under these amendments, we required that the fund adopt procedures providing for periodic testing of the fund's ability to maintain a stable price per share based on (but not limited to) certain hypothetical events.[921] These hypothetical events include a change in short-term interest rates, an increase in shareholder redemptions, a downgrade of or default on portfolio securities, and the widening or narrowing 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.[922] At the time, we declined to specify further tests that a money market fund should conduct to fully assess its ability to maintain a stable value, leaving it to the fund's board (and the fund manager) to establish additional scenarios or assumptions on which the tests should be based and to tailor the tests, as appropriate, for different market conditions and different money market funds.[923]

Since 2010, we and our staff have continued to monitor the stress testing requirement and how different fund groups are approaching its implementation in the marketplace. Through our staff's examinations of money market fund stress testing procedures, we have observed disparities in the quality and comprehensiveness of stress tests, the types of hypothetical circumstances tested, and the effectiveness of materials produced by the fund's manager to explain the stress testing results to the board. For example, although some funds actively embrace the spirit of the requirement by testing a variety of additional hypothetical events and tailoring their stress testing to the particular market conditions and potential risks that they may face, other funds test only for the events specifically listed in the rule. Some funds test for combinations of events, as well as for correlations between events and between portfolio holdings, whereas others do not. We also have examined how funds share information about stress testing results with their boards.

Since adopting the stress testing requirement in 2010, we have had several opportunities to assess its effectiveness during periods of market stress, including the 2011 Eurozone debt crisis and the 2011 U.S. debt ceiling impasse. Our staff observed, for example, that during the 2011 Eurozone debt crisis, funds that had strong stress testing procedures were able to use the results of those tests to better manage their portfolios and minimize the risks associated with the crisis.

After considering this information and experience, we believe that certain enhancements to our stress testing requirements may be warranted. We also note that our floating NAV proposal and our liquidity fees and gates proposal may have different implications regarding the need for and nature of stress testing of a money market fund's portfolio. Accordingly, we are proposing a variety of amendments and enhancements to our stress testing requirements. The amendments and enhancements we are proposing to the stress testing requirements would largely be identical under either reform alternative we might adopt, except that for floating NAV money market funds we would remove the standard to test against preserving a stable share price if we were to adopt the floating NAV alternative, as further discussed below.

1. Stress Testing Under the Floating NAV Alternative

As discussed above, we acknowledge that requiring that money market funds transact with a floating NAV mitigates but does not eliminate the possibility of heavy shareholder redemptions. We understand that in times of broad financial market stress, shareholders in floating NAV money market funds may still have an incentive to redeem shares because of funds' limited internal liquidity or because of overall flights to quality, liquidity, or transparency. Accordingly, stress testing the liquidity of floating NAV funds could enhance a fund board's understanding of risks and fund management of those risks.

If we adopt the floating NAV alternative, we propose to amend the current stress testing requirement as it would apply to floating NAV money market funds to require that such funds test the impact of certain market conditions on fund liquidity, instead of requiring that they test the fund's ability to maintain a stable price per share.[924] More specifically, we are proposing that each floating NAV money market fund stress test its ability to avoid having its weekly liquid assets fall below 15% of all fund assets. This requirement also would be in accord with the proposed requirement, discussed in the next section, that would require funds to stress test their ability to avoid crossing the same 15% weekly liquid asset threshold because it could trigger fees or gates. We selected this 15% weekly liquid asset test for similar reasons that we selected that threshold under our liquidity fees and gates alternative—that a money market fund falling below this liquidity threshold can indicate stress on the fund.[925] Funds that go below the 15% weekly liquid asset threshold may face significant adverse consequences, and thus fund boards and advisers should understand and be aware of what could cause a fund to cross such a threshold. We understand that when a fund tests its ability to maintain a stable price (the metric that stress tests currently require), a fund also tests its ability to avoid crossing liquidity thresholds, such as the 15% weekly liquid asset test that we are proposing today. Accordingly, because we understand that funds already test their ability to avoid crossing a 15% weekly liquid asset threshold as part of their current stress tests, we do not expect that replacing the stable NAV test for floating NAV money market funds with a liquidity test will impose significant costs on funds.

For a money market fund that would be exempt from the floating NAV requirement under our proposal (a government or retail money market fund), we propose requiring that it stress test for both its ability to avoid having its weekly liquid assets fall below 15% of its total assets and its ability to maintain a stable share price.[926] This would augment the current testing that these funds conduct to test not just against stresses that could cause these

[919] *See* 2010 Adopting Release, *supra* note 92, at section II.C.4.

[920] *See* 2009 Proposing Release, *supra* note 31, at section II.C.3.

[921] *See* rule 2a–7(c)(10)(v)(A).

[922] *Id.*

[923] *See* 2010 Adopting Release, *supra* note 92, at nn.260–261 and accompanying text.

[924] Proposed (FNAV) rule 2a–7(g)(7)(i).

[925] *See supra* section III.B. We note that we have also proposed a 15% weekly liquid assets trigger for use of rule 22e–3 (permitting suspension of redemptions when liquidating of a fund) under our liquidity fees and gates and floating NAV alternatives. *See supra* sections III.A.5 and III.B.1—III.B.4.

[926] *See* proposed (FNAV) rule 2a–7(g)(7)(i).

funds to ''break the buck'' but also for liquidity stresses.

We request comment on this proposed amendment to the stress-testing requirement for money market funds under the floating NAV alternative.

- Should we continue to require funds with a floating NAV to stress test their portfolio? If not, why not?
- Is the level of weekly liquid assets an appropriate measure of risk for floating NAV funds to stress test against? Should it also (or alternatively) stress test against the level of daily liquid assets? If so, what daily liquid asset threshold should be tested: 5%, 2%, or some other number?
- Is the threshold of 15% weekly liquid assets the right level to test stress on the fund? Should it be higher or lower, such as 10% weekly liquid assets or 20%?
- Should we require that government and retail money market funds test against both their ability to maintain a stable share price and falling below 15% weekly liquid assets? Are there other stress testing factors that would be more appropriate for these exempt funds?
- Are we correct in concluding that funds already stress test their liquidity when testing their ability to maintain a stable NAV? Would there be any costs for a fund to switch to using a weekly liquid asset test instead?

Instead of amending the current stress testing requirement to test liquidity, we could require a floating NAV money market fund to stress test its ability to meet other or additional metrics or standards. For example, we could require testing a floating NAV fund's ability to meet its investment objective, avoid significant losses, or maintain low volatility. If we were to require stress testing for a fund's ability to meet its investment objectives, funds might be able to craft tests that are particularly suited to their particular circumstances. On the other hand, funds investment objectives may be too general for an appropriate test to be created. In addition, requiring testing against investment objectives may create significant disparities in stress tests between similar funds. Requiring testing against the ability for a fund to avoid significant losses or maintaining low volatility may have the advantage of directly testing for the circumstances with which fund investors may be most concerned, but may create difficulties in establishing the appropriate metrics applicable to all funds. We expect that a floating NAV fund might regularly experience minor fluctuations in its NAV, and establishing a meaningful stress test standard related to losses or volatility while still accommodating these potential fluctuations may not be workable.

We request comment on whether instead of amending the current stress testing requirement for floating NAV money market funds to focus only on liquidity, we should replace it (or supplement it) with a requirement to stress test to a different or additional metric or standard.

- Are there alternative or additional metrics or standards other than liquidity that would provide sufficient guidance for a fund to run effective stress tests?
- Should we instead use a metric, such as the ability for a floating NAV fund to avoid losses greater than 25 or 50 basis points in a certain period of time? If we were to use a different metric, what should it be and how should it be set? Are there any other potential metrics or standards that we could use? The fund's ability to minimize principal volatility or losses?

We also are proposing that money market funds include factors such as correlations among securities returns and concurrences of events in their stress tests.[927] Our staff's review of money market fund stress testing and its use during periods of market stress, as well as recent evidence on portfolio asset return correlations provided by the staff, indicates many money market funds face significant correlated risk in their portfolios. We note that some commenters have agreed that correlations among securities and concurrences of events are important factors to consider when stress testing.[928] Others have highlighted the correlations among many money market fund portfolio securities, and noted the relevance of such correlations when examining money market fund risk.[929]

As noted above, we observe that although some funds test for likely concurrences of events and potential correlations among securities returns, others do not. We believe that an evaluation of such correlations and concurrences is an important part of a fund's stress testing, and accordingly are proposing to require that they be included as part of the required stress testing procedures.[930] Specifically, we propose to require that stress testing procedures provide for testing of ''[c]ombinations of these and any other events the adviser deems relevant, assuming a positive correlation of risk factors . . . .'' [931] Such testing should include an evaluation of the effect of hypothetical events on issuers that operate in a similar industry, are based in a similar geographic region, or have other related attributes. It should include an evaluation of the likelihood that one event may influence or lead to another event. It should also test the effect of correlations of issuer and guarantor exposures on liquidity.

As part of our effort to ensure that funds consider portfolio correlations, we also propose to revise the stress testing requirement relating to the effect of downgrades or defaults of portfolio securities to require an evaluation of the effect that such an event could have on other securities held by the fund.[932] Security downgrades and defaults often occur in tandem with downgrades and defaults of other similar securities, and evaluating the effect of a single security event in isolation may not provide a sufficient picture of the effect of such a downgrade or default on the other securities held by the fund.[933]

We also are proposing to require that funds test not just for increases in redemptions in isolation, but also reflect how the fund will likely meet the redemptions, taking into consideration assumptions regarding the prices for which portfolio securities could be sold, historical experience in handling redemptions, the relatively liquidity of the fund's securities, and any other relevant factors.[934] We designed this

[927] Proposed (FNAV) rule 2a–7(g)(7)(i).

[928] *See, e.g.,* Comment Letter of Chris Barnard (Jan. 4, 2013) (available in File No. FSOC–2012–0003) (''I would recommend that regulators specifically emphasize [sic] the importance of considering dependencies and correlations under stress testing, particularly as typically observed and expected dependencies may not apply in the tail conditions and events that underlie many stress conditions and scenarios.'').

[929] *See, e.g.,* Robert Comment FSOC Comment Letter, *supra* note 67 (noting the correlated credit risk in money market funds); Harvard Business School FSOC Comment Letter, *supra* note 24 (same).

[930] In our 2009 Proposing Release, we stated ''Boards should, for example, consider procedures that require the fund to test for the concurrence of multiple hypothetical events, *e.g.,* where there is a simultaneous increase in interest rates *and* substantial redemptions.'' *See* 2009 Proposing Release, *supra* note 31, text following n.209; rule 2a–7(c)(10)(v).

[931] In full, under the proposed new requirement, funds would test for: ''Combinations of these and any other events the adviser deems relevant, assuming a positive correlation of risk factors (*e.g.,* assuming that a security default likely will be followed by increased redemptions) and taking into consideration the extent to which the fund's portfolio securities are correlated such that adverse events affecting a given security are likely to also affect one or more other securities (*e.g.,* a consideration of whether issuers in the same or related industries or geographic regions would be affected by adverse events affecting issuers in the same industry or geographic region).'' Proposed (FNAV) rule 2a–7(g)(7)(i)(F).

[932] Proposed (FNAV) rule 2a–7(g)(7)(i)(C).

[933] For example, a default by one financial institution may lead to a re-examination of other similar companies that may result in additional downgrades or defaults.

[934] Proposed (FNAV) rule 2a–7(g)(7)(i)(B).

requirement to help assist funds in taking into account consequences of how the fund responds to shareholder redemptions.

In addition to the enhancements described above, we also are proposing certain clarifications of our stress testing requirements, based on our experience in money market fund use of these requirements since 2010, that would enhance the usefulness of stress testing as a monitoring tool for funds. First, we propose to clarify that a fund is required only to stress test for increases (rather than changes) in the general level of short-term interest rates.[935] Although a decrease in short-term interest rates might cause a fund's price per share to rise above $1.00, the fund's board can return the fund to its desired stable price by distributing the gains to shareholders. As a result, we are proposing to amend the provision to clarify that a fund is required only to stress test for increases in the general level of short-term interest rates.

Second, we propose to require that funds stress test for the ''widening or narrowing of spreads among the indexes to which interest rates of portfolio securities are tied.'' [936] This requirement would compel funds to stress test their entire portfolios for a broad range of risks that may affect specific asset classes of portfolio securities (*e.g.,* a change in the shape of the yield curve or a change in the interest rates of particular asset classes). The current rule requires stress testing for ''widening or narrowing of spreads between yields on an appropriate benchmark the fund has selected for overnight interest rates and commercial paper and other types of securities held by the fund.'' *See* rule 2a–7(c)(10)(v)(A). However, this stress test gives similar results to the current requirement that funds test for a change in the level of short-term interest rates. The proposed clarification would better enable funds to test for changes in spreads that may affect specific asset classes held by the fund, rather than for just short-term interest rate changes.

Finally, we are proposing to add another related hypothetical event for funds to test, namely ''[o]ther movements in interest rates that may affect fund portfolio securities, such as parallel and non-parallel shifts in the yield curve.'' [937] This new requirement could help funds better understand the exposure of various floating rate portfolio securities to changes in interest rates.

We do not intend the enhancements and clarifications to stress testing procedures that we are proposing today to serve as a comprehensive list of events to consider when funds engage in stress testing, but as a minimum set. Funds should carefully consider if any other events not described in the rule may affect their ability to maintain at least 15% weekly liquid assets, and test for those as well.[938]

We request comment on our proposed enhancements and clarifications to money market fund stress testing procedures.

- Are the proposed clarifications appropriate? Are there other clarifying changes that we should consider?
- Should we include any other required hypothetical events in the rule? If so, which other events should we include and why?
- Should we require funds to test for combinations of hypothetical events in their stress testing? Instead of leaving it to the discretion of the fund, should we specify which events should be combined (*e.g.,* increases in shareholder redemptions and increases in short-term interest rates, or increases in shareholder redemptions and a default or downgrade of a portfolio security (or security correlated to a portfolio asset class), or both)? What additional costs would funds incur for testing a combination of hypothetical events?
- Should we make any other changes to the stress testing requirements, such as requiring a minimum frequency that funds should conduct their stress tests?

In addition to the enhancements to the specific hypothetical events that money market funds' stress testing would have to include, we are proposing a clarification to the requirement that a fund's adviser provide the fund's board an assessment of the results of the stress tests. We propose to require that the adviser provide not only such an assessment, but also ''such information as may reasonably be necessary for the board of directors to evaluate the stress testing conducted by the adviser and the results of the testing.'' [939] We are proposing this requirement because we have observed that in some cases advisers have not provided sufficient context and additional information for fund boards as part of this assessment to effectively evaluate the stress test results and take appropriate action. For example, a fund's stress testing showing the effects of various levels of redemptions may not be meaningful to the fund's board without sufficient context such as fund shareholder concentrations levels and historical redemption activity. We designed this proposed change to assist fund boards to seek out and receive any additional information that they may need to effectively evaluate and make use of money market fund stress tests. We request comment on this proposed change.

- Are fund boards receiving sufficient context and necessary information about money market funds' stress testing? Is there additional information that they should receive?
- How many funds would need to change their stress test information dissemination procedures to their boards?

Finally, we are requesting comment on certain aspects of money market fund stress testing as it relates to our obligation under section 165(i)(2) of the Dodd-Frank Act to specify certain stress testing requirements for financial companies [940] that have total consolidated assets of more than $10 billion and are regulated by a primary federal financial regulatory agency. Under this section of the Dodd-Frank Act, among other matters, we must ''establish methodologies for the conduct of stress tests . . . that shall provide for at least three different sets of conditions, including baseline, adverse, and severely adverse.'' [941] Although we expect to propose these stress testing requirements in detail in a separate rulemaking, we request general comment at this time on the methodologies we should consider proposing regarding this stress testing requirement as it may relate to money market funds with over $10 billion in total consolidated assets, and in particular on the different scenarios that we must establish for such stress testing. In connection with this request for

[935] Proposed (FNAV) rule 2a–7(g)(7)(i)(A).

[936] Proposed (FNAV) rule 2a–7(g)(7)(i)(D).

[937] Proposed (FNAV) rule 2a–7(g)(7)(i)(E).

[938] Funds should consider concurrences of such additional events and correlations of any additional factors as well as the ones described above.

[939] Proposed (FNAV) rule 2a–7(g)(7)(ii)(B).

[940] For a definition of ''nonbank financial companies'' for these purposes, see *Definition of ''Predominantly Engaged in Financial Activities'' and ''Significant'' Nonbank Financial Company and Bank Holding Company,* Board of Governors of the Federal Reserve System, [78 FR 20756 (Apr. 5, 2013)].

[941] Under this section of the Dodd-Frank Act, we also must define the term ''stress test'' for purposes of that section, establish the form and content of the report to the Federal Reserve Board and the Commission regarding such stress testing, and require companies subject to this requirement to publish a summary of the results of the required stress tests. We note that under this section of the Dodd-Frank Act, we must design stress testing not just for certain money market funds, but also other types of funds and investment advisers that we regulate and that meet the $10 billion total consolidated assets test.

comment, we note that we could consider the approach taken by the U.S. banking regulators for stress testing of banks, in which the Board of Governors of the Federal Reserve System annually publishes a set of hypothetical economic scenarios, including baseline, adverse, and severely adverse scenarios, that are to be used in bank stress testing, with appropriate modifications.[942]

- How should we define what set of events qualify as baseline, adverse, or severely adverse? Should we require funds to use or look to the scenarios published annually by the Federal Reserve?
- Are the scenarios published by the Federal Reserve appropriate for money market funds? Should we specify more or fewer or different scenarios than the 3 scenarios specified in section 165(i)(2) of the Dodd-Frank Act?
- To what extent should we provide guidance regarding what might reasonably constitute each of these scenarios with regards to money market funds?
- How should such a stress testing requirement be specifically tailored to money market funds as opposed to banks or other types of funds? Should money market funds have to assess the impact of such a scenario given the fund's investment profile and its historical pattern of shareholder redemptions?

2. Stress Testing Under the Liquidity Fees and Gates Alternative

If we adopt our liquidity fees and gates alternative proposal, we are proposing that money market funds stress test against the potential for a money market fund's level of weekly liquid assets to fall below 15% of its total assets, in addition to stress testing against the fund's ability to maintain a stable share price.[943] If we adopt this alternative, we would also adopt the same enhancements and clarifications to the stress testing provisions of rule 2a–7 discussed above under our floating NAV proposal.[944]

Money market funds currently must stress test their ability to maintain a stable NAV per share, because failing to maintain such stability may result in significant adverse consequences for its investors, as discussed above.[945] Under our liquidity fees and gates alternative, if a fund's level of weekly liquid assets falls below 15%, we would require a fund to impose liquidity fees (unless the board determines otherwise) and a fund may impose a gate. Much like the inability to maintain a stable price, the triggering of such fees or gates may result in significant consequences for a fund and its shareholders. Accordingly, we are proposing an additional metric against which the fund would have to stress test: the fund's level of weekly liquidity assets falling below 15%. Requiring funds to stress test their ability to avoid crossing this threshold should help inform boards and fund managers of the circumstances that could cause a fund to trigger fees or gates and provide them a tool to help avoid doing so.

Generally, we expect that a fund would use similar hypothetical circumstances when testing its ability to avoid triggering fees and gates that it uses when stress testing its ability to maintain a stable price. However, some funds may identify different circumstances that are more relevant to testing one standard than another, and thus may use different versions of the hypothetical scenarios, or weigh them differently for each. For example, certain events, such as significant shareholder redemptions in a short time period, may more strongly affect the ability of a fund to avoid crossing the 15% weekly liquid asset threshold than the ability to maintain a stable price. Other events, such as a credit default in a portfolio security, may more strongly affect the ability of a fund to maintain a stable price than avoid crossing the liquidity threshold. Stress tests should thus account for a variety of circumstances that affect the ability of a fund to meet each standard.

We request comment on our proposed inclusion of a fund's ability to maintain at least 15% weekly liquid assets as an additional stress testing metric.

- Should we include this additional metric? Why or why not? Would the proposed requirement help fund managers better manage the risks of a stable price fund with standby liquidity fees and gates? Should we include any other metrics or standards for stress testing? If so, which ones and why?
- Should a fund also (or alternatively?) stress test against the level of daily liquid assets? If so, what daily liquid asset threshold should be tested: 5%, 2%, or some other number?
- Is the threshold of 15% weekly liquid assets the right level to test stress on for a fund? Should it be higher or lower, such as 10% weekly liquid assets or 20%?

If we were to adopt the liquidity fees and gates alternative, we would also adopt the same enhancements and clarifications to the stress testing requirements described in our floating NAV alternative.[946] We believe that the amendments and enhancements to the stress testing requirements that we are proposing under the floating NAV alternative would provide the same benefits as under our liquidity fees and gates alternative and would help funds with fees and gates better test their portfolios for risks. As discussed in detail above, these enhancements include (among others) requirements to test for concurrences of events and correlations among returns, the ability of a fund to meet redemptions, and other revised and additional hypothetical events.[947]

We request comment on whether we should include these enhancements to a fund stress testing procedures if we were to adopt our liquidity fees and gates alternative.

- Should we revise any of the proposed enhancements to account for the circumstances of a fund with standby liquidity fees and gates? If so, how? Should we include any additional enhancements? Should we eliminate any of the proposed enhancements?
- Should we adopt these enhancements even if we do not add the additional liquidity metric? Should we adopt these enhancements even if we do not adopt the liquidity fees and gates or floating NAV proposals at all? Why or why not?

3. Economic Analysis

As previously discussed, we expect that the costs and benefits of the proposed stress testing amendments would be largely identical under both alternatives.[948] Our baseline for the economic analysis we discuss below is

[942] *See Annual Company-Run Stress Test Requirements for Banking Organizations With Total Consolidated Assets Over $10 Billion Other Than Covered Companies,* Board of Governors of the Federal Reserve System [77 FR 62396 (Oct. 12, 2012)]; *Supervisory and Company-Run Stress Test Requirements for Covered Companies,* Board of Governors of the Federal Reserve System [77 FR 62378 (Oct. 12, 2012)].

[943] *See* Proposed (Fees & Gates) rule 2a–7(g)(9)(i). We discuss our proposed changes to MMF stress testing requirements under the floating NAV alternative above.

[944] Proposed (Fees & Gates) rule 2a–7(g)(9)(i)(A)–(F).

[945] *See* rule 2a–7(c)(10)(v)(A).

[946] *See supra* section III.L.1.

[947] Proposed (Fees & Gates) rule 2a–7(g)(9)(i).

[948] We expect that the costs and benefits of our proposed new liquidity metric and other enhancements to fund stress testing would be similar under either our floating NAV or liquidity fees and gates alternative, except that some funds under the floating NAV alternative may realize minor savings in avoiding have to test for the ability maintain a stable share price. The only substantive difference between the proposals is that we would eliminate the requirement for floating NAV money market funds to test for the ability to maintain a stable share price under our floating NAV alternative.

the current stress testing requirements for money market funds. The costs and benefits, and effects on competition, efficiency, and capital formation are measured in increments over the current stress testing requirement baseline. The benefits of the proposed stress test requirements will depend in part on the extent to which funds already engage in stress tests that are similar to the proposed requirements. For example, the staff understands that most money market funds currently test for changes in general levels of short-term interest rates. We do not, therefore, anticipate that the proposed requirement to test for increases in general levels of short-term interest rates will confer many additional benefits on funds, although funds may experience negligible savings because the proposed amendment would be limited to increases (rather than changes) in short-term interest rates. Similarly, many funds, including those that use a service provider to conduct their stress testing, already test for effects on portfolios of spread changes among indexes to which interest rates of portfolio securities are tied and other factors as well. In this case, we anticipate the proposed changes will confer benefits only on those funds that currently do not perform these types of stress tests.[949] The additional information generated from the stress test should help fund managers, advisers, and boards monitor, evaluate, and manage fund risk, and thus better protect the fund and its investors from the adverse consequences that may result in failing to maintain a stable price per share or crossing the 15% weekly liquid assets threshold. We cannot quantify the expected benefits of our proposed stress testing requirements because we do not have sufficient data as to the extent to which funds already include these factors in their stress tests today.

Because funds are currently required to meet a stress testing requirement, we do not anticipate significant additional costs to funds under either proposed requirement. We note, however, that under our floating NAV alternative, we would replace the requirement to test for a stable NAV for floating NAV money market funds and replace it with a liquidity test, but under our liquidity fees and gates alternative funds would be required to test for both conditions. The cost of the proposed requirement therefore, would depend on the difference in cost of stress testing for liquidity rather than NAV. We ask below for comment on differences in cost. We believe that there likely would be no difference in costs in testing to either metric.

Generally, we expect that funds would use similar hypothetical circumstances when testing their ability to avoid going below 15% weekly liquid assets that they use when stress testing their ability to maintain a stable price. We understand that although some funds currently test for all the new and amended hypothetical circumstances we are proposing today, others do not. Funds that would need to alter their stress testing procedures to include the new and amended hypothetical circumstances we are proposing would incur some additional costs. For example, we understand that some funds do not currently stress test for correlations among portfolio securities returns and concurrences of events. These funds may incur greater costs in modifying their stress testing procedures and systems to add such tests, than those who already include those circumstances in their tests.[950] Below we estimate a range of operational costs that funds may incur in implementing the amendments and enhancements to fund stress testing that we are proposing.

The staff estimates that a fund that currently already tests for all of the amendments and enhancements to the hypothetical circumstances that we are proposing today would incur no new additional costs to comply. On the other hand, the staff estimates that a fund that does not currently stress test for any of the new and amended hypothetical circumstances would incur one-time costs to implement our proposed amendments. These paper-related costs are discussed in greater detail in section IV below. As we discuss there, our staff estimates that the proposed amendments to stress testing would involve 8,464 burden hours, at an average one-time cost of $3.9 million for all money market funds and funds would not incur any additional ongoing costs.[951]

At this time, we believe any new costs for stress testing would be so small as compared to the fund's overall operating expenses, that any effect on competition would be insignificant. This new requirement may increase allocative efficiency if the information it provides to the fund manager, adviser, and board of directors improves the fund manager's and adviser's ability to manage the fund's risk and the board's oversight of fund risk management. Money market fund investors also may view positively enhanced stress testing requirements, and this could increase investors' demand for money market funds and correspondingly the level of the funds' investment in the short-term financing markets. We do not have the information necessary to provide a reasonable estimate of the effects the proposed amendments would likely have on capital formation because we do not know to what extent these proposed changes would result in increases or decreases in investments in money market funds or in money market funds' allocation of investments among different types of short-term debt securities.

We request comment on our assumptions about the costs of implementing our proposed changes to money market fund stress testing procedures and the effects of the proposed stress testing amendments on efficiency, competition, and capital formation.

- Would there be any increase in costs for firms to stress test against a liquidity metric instead of a stable share price test? If so, what would they be?
- Are our estimates for the range of operational costs of adding the new and amended hypothetical circumstances to a funds stress testing procedures correct? Are they too high or too low, and if so, why? Would these costs only be one-time costs as we estimate or would there also be ongoing costs? If there are ongoing costs, what would they be?
- How many funds would need to change their stress tests for:
  - weekly liquidity levels,
  - factors such as correlations among securities returns and concurrences of events,
  - hypothetical events that might occur to issuers that operate in a similar industry, are based in a similar geographic region, or have other related attributes,
  - the effect of downgrades or defaults of portfolio securities on the performance of other securities held by the fund,
  - shareholder redemptions,
  - risks that may affect specific asset classes of portfolio securities (*e.g.,* a change in the shape of the yield curve

[949] Although as we have discussed previously, money market funds can experience the risk of general heavy redemption contagion, and accordingly improved stress testing that reduces the risks of a single fund may correspondingly have some benefits in reducing the risks of contagion across all funds.

[950] Staff estimates that these costs would be attributable to the following activities: (i) planning, coding, testing, and installing system modifications; (ii) drafting, integrating, and implementing related procedures and controls; and (iii) preparing training materials and administering training sessions for staff in affected areas. *See also supra* note 245 (discussing the bases of our staff's estimates of operational and related costs).

[951] *See infra* sections IV.A.1.e and IV.B.1.e.

or a change in the interest rates of particular asset classes), as well as other movements in interest rates that may affect fund portfolio securities, such as parallel and non-parallel shifts in the yield curve?

• What impact would amending this requirement have on efficiency, competition, or capital formation?

4. Combined Approach

Finally, we note that in section III.C we request comment on whether we should combine our floating NAV and liquidity fees and gates proposals. This raises the question of what we would require regarding stress testing if we combined these alternatives, given that under the floating NAV alternative we have proposed stress testing for a loss of liquidity for floating NAV funds, whereas under the liquidity fees and gates alternative we have proposed to include a liquidity test as well as a test relating to maintaining the current stable price. If we were to pursue a combined approach, we would likely not include any stress testing requirements related to maintaining a stable price for floating NAV funds. Instead, we would only require those funds to stress test against their ability to avoid imposing liquidity fees and redemption gates under a number of hypothetical scenarios. We would also expect to adopt the enhancements and clarifications to fund stress testing procedures discussed previously.

We request comment on what we should require regarding stress testing under a combined approach.

• If we were to adopt a combined approach, would funds stress testing liquidity be useful? Should we instead not require funds to stress test at all? If so, why not?

• Alternatively, under a combined approach should we require floating NAV funds to also stress test their ability to minimize principal volatility or losses or against some other additional metric or standard? If so, to what extent and against which metric or standard?

*M. Clarifying Amendments*

Since our adoption of amendments to rule 2a–7 in 2010, a number of questions have arisen regarding the application of certain of those amendments. We are taking this opportunity to propose a number of amendments to clarify the operation of these provisions. In addition, we are also proposing an additional amendment to state more clearly a limit we imposed on money market funds' investments in second tier securities in 2010.[952] These clarifying amendments would apply under either our floating NAV alternative or the standby liquidity fees and gates alternative. We note that the Commission could choose to adopt these clarifying amendments even if it does not adopt the other reforms to money market fund regulation proposed in this Release.

1. Definitions of Daily Liquid Assets and Weekly Liquid Assets

We are proposing amendments to clarify certain characteristics of instruments that qualify as a ''daily liquid asset'' or ''weekly liquid asset.'' First, we are proposing to make clear that money market funds cannot use the maturity-shortening provisions in current paragraph (d) of rule 2a–7 regarding interest rate readjustments [953] when determining whether a security satisfies the maturity requirements of a daily liquid asset or weekly liquid asset,[954] which include securities that will mature within one or five business days, respectively.[955] Using an interest rate readjustment to determine maturity as permitted under current paragraph (d) for these purposes would allow funds to include as daily or weekly liquid assets securities that the fund would not have a legal right to convert to cash in one or five business days. This would not be consistent with the purposes of the minimum daily and weekly liquidity requirements, which are designed to increase a fund's ability to pay redeeming shareholders in times of market stress when the fund cannot rely on the market or a dealer to provide immediate liquidity.[956]

Second, we propose to require that an agency discount note with a remaining maturity of 60 days or less qualifies as a ''weekly liquid asset'' only if the note is issued without an obligation to pay additional interest on the principal amount.[957] Our proposed amendment would clarify that interest-bearing agency notes that are issued at a discount do not qualify.[958] We understand that these interest-bearing agency notes issued at a discount are extremely rare. We do not believe that interest bearing agency notes are among the very short-term agency discount notes that appeared to be relatively liquid during the 2008 market events and that we determined could qualify as weekly liquid assets.[959]

Finally, we propose to include in the definitions of daily and weekly liquid assets amounts receivable that are due unconditionally within one or five business days, respectively, on pending sales of portfolio securities.[960] These receivables, like certain other securities that qualify as daily or weekly liquid assets, provide liquidity for the fund because they give a fund the legal right to receive cash in one to five business days. We would expect that a fund (or its adviser) would include these receivables in daily and weekly liquid assets only if the fund (or its adviser) has no reason to believe that the buyer might not perform.

We understand that the instruments that most, if not all, money market funds currently hold as daily and weekly liquid assets currently conform

[952] In addition, we are proposing technical, conforming amendments to rule 419(b)(2)(iv) under the Securities Act of 1933 (17 CFR 230.419(b)(2)(iv), which references certain paragraphs in rule 2a–7 the location of which would change under our proposed amendments. Specifically, we propose to replace references to ''paragraphs (c)(2), (c)(3), and (c)(4)'' with ''paragraph (d)''.

[953] *See* rule 2a–7(d) (providing a number of exceptions to the general requirement that the maturity of a portfolio security be deemed to be the period remaining (from the trade date) until the date on which, in accordance with the terms of the security, the principal amount must unconditionally be paid; the exceptions generally provide that a fund may shorten the maturity date of certain securities to the period remaining until the next readjustment of the interest rate *or* the period remaining until the principal amount can be recovered through demand).

[954] Proposed (FNAV and Fees & Gates) rule 2a–7(a)(8); proposed (FNAV and Fees & Gates) rule 2a–7(a)(31). As proposed, the amended definitions would require funds to determine a security's maturity in the same way they must calculate for purposes of determining WAL under proposed (FNAV and Fees & Gates) rule 2a–7(d)(1)(iii).

[955] Rule 2a–7(a)(8) defines ''daily liquid assets'' to include (i) cash, (ii) direct obligations of the U.S. government, or (iii) securities that will mature or are subject to a demand feature that is exercisable and payable within one business day. Rule 2a–7(a)(32) defines ''weekly liquid assets'' to include (i) cash; (ii) direct obligations of the U.S. government; (iii) securities that will mature or are subject to a demand feature that is exercisable and payable within five business days; or (iv) Government securities (as defined in section 2(a)(16) of the Act) that are issued by a person controlled or supervised by and acting as an instrumentality of the U.S. government that are issued at a discount to the principal amount to be repaid at maturity and have a remaining maturity date of 60 days or less.

[956] *See* 2010 Adopting Release, *supra* note 92, at text following n.213.

[957] Proposed (FNAV and Fees & Gates) rule 2a–7(a)(31)(iii).

[958] We understand that an interest-bearing agency note might be issued at a discount to facilitate a rounded coupon rate (*i.e.,* 2.75% or 3.5%) when yield demanded on the note would otherwise require a coupon rate that is not rounded.

[959] *See* 2010 Adopting Release, *supra* note 92, at text accompanying and following nn.251–55. Our determination was informed by average daily yields of 30 day and 60 day agency discount notes during the fall of 2008. We believe that interest-bearing agency notes issued at a discount were not included the indices of the agency discount notes on which we based our analysis or if they were included, there were too few to have affected the indices' averages.

[960] Proposed (FNAV and Fees & Gates) rule 2a–7(a)(8)(iv); proposed (FNAV and Fees & Gates) rule 2a–7(a)(31)(v).

to the amendments we are proposing and that these practices would be consistent with positions our staff has taken in informal guidance to money market funds.[961] The proposed amendments are designed to clarify that securities with maturities determined according to interest rate resets and interest bearing agency notes issued at a discount do not qualify as daily or weekly liquid assets, as applicable. Because both of these types of securities are less liquid than the limited types of instruments that do qualify, any funds that alter their future portfolio investments to conform to these requirements would benefit from increased liquidity and ability to absorb larger amounts of redemptions. The proposal to include certain receivables as daily and weekly assets should benefit funds because it will appropriately increase the types of assets that can satisfy those liquidity requirements. Because we believe that most funds already comply with our proposed amendments, we have not quantified any potential benefits to funds and shareholders.

We do not believe there would be any costs associated with our proposed amendments to the definitions of daily and weekly liquid assets. We do not anticipate that there would be operational costs for any funds that currently hold securities that would no longer qualify as daily or weekly assets because those securities likely would mature before the proposed compliance date for our proposal.[962] Because these amendments would clarify assets that qualify as daily and weekly liquid assets and, we believe, most money market funds are currently complying with these proposed amendments, we do not anticipate that they will have any effect on efficiency or capital formation. To the extent that some funds' practices do not already conform, however, the proposed clarifications may eliminate any competitive advantages that may have resulted from those practices. We request comment on the proposed amendments and the benefits we have described.

- Do the proposed amendments comport with current fund practices?
- Would there be any costs to funds that may not conform to these proposed amendments?
- Would the amendments have any effect on efficiency, competition, or capital formation?

2. Definition of Demand Feature

We are proposing to amend the definition of demand feature in rule 2a–7 to mean a feature permitting the holder of a security to sell the security at an exercise price equal to the approximate amortized cost of the security plus accrued interest, if any, at the time of exercise, paid within 397 calendar days of exercise.[963] Our proposed amendment would eliminate the requirement that a demand feature be exercisable at any time on no more than 30 calendar days' notice.[964]

Eliminating the requirement that a demand feature be exercisable at any time on no more than 30 days' notice would clarify the operation of rule 2a–7 by removing a provision that has become obsolete. In 1986, the Commission expanded the notice period from seven days to 30 days for all types of demand features and emphasized that the notice requirement was at least in part designed to ensure that money market funds maintain adequate liquidity.[965] Because, as discussed in section II.D.1 above, the 2010 amendments added significant new provisions to enhance the liquidity of money market funds, we believe it is unnecessary to continue to require that demand features be exercised at any time on no more than 30 days' notice.[966] As proposed, the demand feature definition would focus on funds' ability to receive payment within 397 calendar days of exercise of the demand feature.

Eliminating the 30-day notice requirement may improve efficiency by simplifying the operation of rule 2a–7 regarding demand features and providing issuers with more flexibility. Our proposed amendment may also promote competition between issuers and facilitate capital formation by permitting funds to purchase securities with demand features from a larger pool of issuers. We do not expect that our proposed amendment would impose costs on funds.[967]

We request comment on our proposed amendment to eliminate the 30-day notice requirement and specific reference to asset-backed securities.

- Do commenters agree that the 30-day notice requirement is unnecessary when considering the enhanced liquidity requirements adopted as part of our 2010 amendments? Why or why not?
- Do commenters agree with our economic analysis? Would our proposal have other economic effects, other than those we describe above? If so, please describe.

3. Short-Term Floating Rate Securities

We are also proposing to clarify the method for determining WAL for short-term floating rate securities.[968] WAL is similar to a fund's WAM, except that WAL is determined without reference to interest rate readjustments.[969] Under current rule 2a–7, a short-term *variable* rate security, the principal of which

[961] *See* Staff Responses to Questions About Money Market Fund Reform, (revised Nov. 24, 2010) (*http://www.sec.gov/divisions/investment/guidance/mmfreform-imqa.htm*) (''Staff Responses to MMF Questions''), Questions II.1, II.2, II.4.

[962] An eligible security must have a remaining maturity of no more than 397 days. Rule 2a–7(a)12)(i).

[963] Proposed (FNAV and Fees & Gates) rule 2a–7(a)(9).

[964] A demand feature is currently defined to mean (i) a feature permitting the holder of a security to sell the security at an exercise price equal to the approximate amortized cost of the security plus accrued interest, if any, at the time of exercise. A Demand Feature must be exercisable either: (a) At any time on no more than 30 calendar days' notice; or (b) At specified intervals not exceeding 397 calendar days and upon no more than 30 calendar days' notice; or (ii) A feature permitting the holder of an Asset-Backed Security unconditionally to receive principal and interest within 397 calendar days of making demand. *See* rule 2a–7(a)(9).

[965] *See* Acquisition and Valuation of Certain Portfolio Instruments by Registered Investment Companies, Investment Company Act Release No. 14983 (Mar. 12, 1986) [51 FR 9773 (Mar. 21, 1986)] (''The Commission still believes that some limit must be placed on the extent to which funds relying on the rule will have to anticipate their cash and investment needs more than seven days in advance. However, the Commission believes that funds should be able to invest in the demand instruments that are being marketed with notice periods of up to 30 days, as long as the directors are cognizant of their responsibility to maintain an adequate level of liquidity.''). Liquidity was also a concern when the Commission added the definition of demand feature for asset-backed securities and noted that it was done, in part, to make clear the date on which there was a binding obligation to pay (and not just the scheduled maturity). *See* 1996 Adopting Release, *supra* note 247, at accompanying nn.151–52.

[966] Our proposal today would also be consistent with a position our staff has taken in the past. *See, e.g.,* SEC No-Action Letter to Citigroup Global Markets, Inc. (May 28, 2009), *available at http://www.sec.gov/divisions/investment/noaction/2009/citigroupglobal052809-2a7.htm.*

[967] We note that demand features and guarantees are referenced in rule 12d3–1(d)(7)(v) (providing that, subject to a diversification limitation, the acquisition of a demand feature or guarantee is not an acquisition of securities of a securities related business (that would otherwise be prohibited pursuant to section 12(d)(3) of the Act)) and rule 31a–1(b)(1) (requiring that a fund's detailed records of daily purchase and sale records include the name and nature of any demand feature provider or guarantor). We do not believe that our proposed amendment would provide any benefits or impose any costs with respect to these rules, other than those described above. We also propose to update the cross references to the definition of the terms ''demand feature'' and ''guarantee'' in rule 12d3–1(d)(7)(v), which defines these terms by reference to rule 2a–7 (replacing the references to ''rule 2a–7(a)(8)'' and ''rule 2a–7(a)(15)'' with ''§ 270.2a–7(a)(9)'' and ''§ 270.2a–7(a)(16)'') and rule 31a–1(b)(1) (replacing the references to ''rule 2a–7(a)(8)'' and ''rule 2a–7(a)(15)'' with ''§ 270.2a–7(a)(9)'' and ''§ 270.2a–7(a)(16)'').

[968] *See* rule 2a–7(d)(4).

[969] *See* rule 2a–7(c)(2)(iii).

must unconditionally be paid in 397 calendar days or less, is ''deemed to have a maturity equal to the earlier of the period remaining until the next readjustment of the interest rate or the period remaining until the principal amount can be recovered through demand.'' [970] A short-term *floating* rate security, the principal amount of which must unconditionally be paid in 397 calendar days or less, is ''deemed to have a maturity of one day'' because the interest rate for a floating rate security will change on any date there is a change in the specified interest rate.[971]

Despite the difference in wording of the maturity-shortening provisions for floating rate and variable rate securities, the Commission has always intended for these provisions to work in parallel and provide the same results.[972] The omission of an explicit reference to demand features in the maturity-shortening provision for short-term floating rate securities, however, has created uncertainty in determining the maturity of short-term floating rate securities with a demand feature for purposes of calculating a fund's WAL.[973] Therefore, we are proposing to amend rule 2a–7(d)(4) to provide that, for purposes of determining WAL, a short-term floating rate security shall be deemed to have a maturity equal to the period remaining until the principal amount can be recovered through demand.[974]

We understand that most money market funds currently determine maturity for short-term floating rate securities consistent with the proposed amendment.[975] Accordingly, we believe that our proposed amendment would likely not result in costs to funds. Any funds that currently limit or avoid investments in short-term floating rate securities because they would look to the security's stated final maturity date rather than the demand feature for purposes of determining WAL (which could significantly increase the WAL), may benefit if they increase investments in short-term floating rate securities that are higher yielding than alternative investments in the fund's portfolio. To the extent that those funds may have experienced any competitive yield disadvantage because they limited or avoided these investments, the proposed amendments should address those effects. Because we believe that most funds interpret the maturity requirements as we propose, we do not believe our proposed changes would produce quantifiable benefits or result in a significant, if any, impact on capital formation. We request comment on our proposed amendment to clarify the method for determining WAL for short-term floating rate securities.

- Is our assumption that money market funds currently determine maturity for short-term floating rate securities consistent with our proposed amendment correct? If so, would our proposed amendment have any impact on fund efficiency? If not, how would our proposed amendment affect efficiency?
- Do commenters agree that our proposed amendment would likely not result in a cost to funds? Is our analysis of costs and benefits, including the effects on competition and capital formation accurate?

4. Second Tier Securities

In 2010, we amended rule 2a–7 to limit money market funds to acquiring second tier securities with remaining maturities of 45 days or less.[976] As we explained then, ''[s]ecurities of shorter maturity will pose less credit spread risk and liquidity risk to the fund because there is a shorter period of credit exposure and a shorter period until the security will mature and pay cash.'' [977] We also explained that second tier securities with shorter maturities are less likely to be downgraded—and the data underlying this analysis looked at final legal maturities (and not maturities reflecting interest rate readjustments).[978] Finally, we referenced the fact that the market typically demanded that second tier securities be issued at shorter legal maturities than first tier securities.[979] Accordingly, all of our analysis in adopting this requirement was focused primarily on second tier securities' credit risk, credit spread risk, and liquidity, all of which are more appropriately measured by the security's final legal maturity, rather than its maturity recognizing interest rate readjustments, which focuses on interest rate risk. Thus to state more clearly the way in which this limitation operates, we propose to amend rule 2a–7 to state specifically that the 45-day limit applicable to second tier securities must be determined without reference to the maturity-shortening provisions in rule 2a–7 for interest rate readjustments.[980]

We understand that most money market funds currently determine the remaining maturity for second tier securities consistent with the proposed amendment. Accordingly, we believe that our proposed amendment would likely not result in costs to funds or impact competition, efficiency, or capital formation. Any funds that currently hold securities that would no longer qualify as second tier securities would not incur costs because those securities likely would mature before the proposed compliance date for our proposal.[981] We request comment on our proposal to state more explicitly the way in which the 45-day limit on second tier securities operates.

*N. Proposed Compliance Date*

Currently, we anticipate the following compliance dates for our proposed amendments as set forth below.[982] With respect to any proposed amendments requiring certain historical disclosures, we propose that funds would be required only to disclose events that occur following the respective compliance date.[983] Generally, we are proposing a compliance period of 2 years for the proposed floating NAV alternative, 1 year for the liquidity fees and gates alternative, and 9 months for the other proposed amendments that are not specifically related to the implementation of either alternative.

[970] *See* rule 2a–7(d)(2).

[971] *See* rule 2a–7(d)(4). Rule 2a–7 distinguishes between floating rate and variable rate securities based on whether the securities' interest rate adjusts (i) when there is a change in a specified interest rate (floating rate securities), or (ii) on set dates (variable rate securities); rule 2a–7(a)(15) (defining ''floating rate security''); rule 2a–7(a)(31) (defining ''variable rate security'').

[972] *See* 1996 Adopting Release, *supra* note 247, at n.154 (the maturity of a floating rate security subject to a demand feature is the period remaining until principal can be recovered through demand).

[973] Long-term floating rate securities that are subject to a demand feature are deemed to have a maturity equal to the period remaining until the principal amount can be recovered through demand. Rule 2a–7(d)(5).

[974] Proposed (FNAV and Fees & Gates) rule 2a–7(i)(4).

[975] Such a determination would be consistent with informal guidance that the staff has provided. *See* Investment Company Institute, Request for Interpretation under rule 2a–7 (Aug. 10, 2010) (incoming letter and response) at *http://www.sec.gov/divisions/investment/noaction/2010/ici081010.htm.*

[976] *See* 2010 Adopting Release, *supra* note 92, at nn.65–69 and accompanying text.

[977] *Id.* at text preceding n.67.

[978] *Id.* at n.67 and accompanying text.

[979] *Id.* at n.68 and accompanying text.

[980] *See* proposed (FNAV and Fees & Gates) rule 2a–7(d)(2)(ii).

[981] *See supra* note 962.

[982] We expect to provide more nuanced guidance on the compliance periods for each particular amended provision in the adopting release once commenters have had a chance to provide input and a particular alternative has been chosen.

[983] *See, e.g.,* proposed (FNAV) Item 16(g) of Form N–1A (Historical Disclosure of Financial Support Provided to Money Market Funds); proposed (Fees & Gates) Item 16(g)(2) of Form N–1A (Historical Disclosure of Financial Support Provided to Money Market Funds); proposed (Fees & Gates) Item 16(g)(1) of Form N–1A (Historical Disclosure of Imposition of Fees and/or Gates).

1. Compliance Period for Amendments Related to Floating NAV

If we were to adopt our floating NAV proposal, we expect that 2 years should provide an adequate period of time for money market funds, intermediaries, and other service providers [984] to conduct the requisite operational changes to their systems to implement the floating NAV and for fund sponsors to restructure or establish new money market funds if they chose to rely on any available exemptions. It would also provide an extended length of time for money market fund shareholders [985] to consider the reforms and make any corresponding changes to their investments and for any resulting impacts on the short-term financing markets and capital formation to be gradually absorbed.

Accordingly, if we were to adopt the floating NAV alternative, the compliance date would be 2 years after the effective date of the adoption with respect to any amendments specifically related to the floating NAV proposal,[986] including any related amendments to disclosure. We therefore propose that the compliance date would be 2 years after the effective date of adoption of new rule 30b1–8, new Form N–CR, and the proposed amendments to rule 2a–7, rule 30b1–7, rule 482, Form N–MFP and Form N–1A under the floating NAV alternative.

2. Compliance Period for Amendments Related to Liquidity Fees and Gates

If we were to adopt the standby liquidity fees and gates alternative, we expect that 1 year should allow sufficient time for money market funds and their sponsors and service providers to conduct the requisite operational changes to their systems to implement these provisions, in particular the ability to impose standby liquidity fees and gates, and for fund sponsors to restructure or establish new money market funds if they chose to rely on any exemptions available. It would also provide a substantial amount of time for money market fund shareholders to consider the reforms and make any corresponding changes to their investments and for any resulting impacts on the short-term financing markets and capital formation to be gradually absorbed.

Accordingly, if we were to adopt our standby liquidity fees and redemption gates alternative, the compliance date would be 1 year after the effective date of the adoption with respect to any amendments specifically related to the standby liquidity fees and gates alternative,[987] including any related amendments to disclosure. We therefore propose that the compliance date would be 1 year after the effective date of the adoption of new rule 30b1–8 and new Form N–CR and the amendments to rule 2a–7, rule 30b1–7, rule 482, Form N–MFP and Form N–1A under the liquidity fees and redemption gates alternative.

3. Compliance Period for Other Amendments to Money Market Fund Regulation

With respect to any amendments not specifically related to either of the two proposed alternatives, we expect that 9 months should allow sufficient time for money market funds and their sponsors and service providers to implement any applicable disclosure requirements and conduct any applicable requisite operational changes to their systems to implement these provisions.

Accordingly, except as otherwise discussed above, we propose a general compliance date of 9 months after the effective date of adoption for all other proposed amendments to money market fund regulation not specifically related to either proposed alternative.

4. Request for Comment

We request comment on the proposed compliance period for money market funds to comply with the proposed amendments.

- Should we provide a longer or shorter compliance period with respect to any of our proposed amendments? If so, why and of what length? How long would it take to implement each provision of our proposed amendments? Are there any provisions that should go into effect immediately? Others that should be provided an even longer compliance period?
- Would our proposed compliance periods and transition times provide sufficient time for fund groups to determine their preferred approach to implementing any regulatory changes and conduct any necessary operational changes?
- Would our anticipated compliance dates and transition times allow investors sufficient time to evaluate the changes and determine their preferred course of action?
- If any of the proposed amendments were to result in investors substantially reallocating capital, are there other steps we could take that we have not considered to mitigate any adverse effects on the short-term financing markets and capital formation during the transition?

*O. Request for Comment and Data*

The Commission requests comment on the amendments proposed in this Release. Commenters are requested to provide empirical data to support their views. The Commission also requests suggestions for additional changes to existing rules or forms, and comments on other matters that might have an effect on the proposals contained in this Release.

We specifically request comment on the feasibility of any alternatives to our proposed amendments that would minimize reporting and recordkeeping burdens on funds, the utility and necessity of the additional information we propose to require in relation to the associated costs and in view of the public benefits derived, and the effects that additional recordkeeping requirements would have on internal compliance policies and procedures.[988]

*Consideration of Impact on the Economy.* For purposes of the Small Business Regulatory Enforcement Fairness Act of 1996, or ''SBREFA,'' [989] the Commission must advise OMB whether a proposed regulation constitutes a ''major'' rule. Under SBREFA, a rule is considered ''major'' where, if adopted, it results in or is likely to result in: (1) An annual effect on the economy of $100 million or more; (2) a major increase in costs or prices for consumers or individual industries; or (3) significant adverse effects on competition, investment or innovation.

We request comment on the potential impact of our proposals on the economy on an annual basis. Commenters are requested to provide empirical data and other factual support for their views to the extent possible.

## IV. Paperwork Reduction Act Analysis

Certain provisions of the proposed amendments contain ''collections of information'' within the meaning of the Paperwork Reduction Act of 1995 (''PRA'').[990] The titles for the existing collections of information are: ''Rule 2a–7 under the Investment Company Act of 1940, ''Money market funds'' (Office of Management and Budget (''OMB'') Control No. 3235–0268); ''Rule 12d3–1 under the Investment Company Act of

[984] *See supra* section III.A.9.

[985] *Id.*

[986] *See supra* section III.A (Floating NAV Alternative).

[987] *See supra* section III.B (Standby Liquidity Fees and Gates).

[988] *See* sections 30(c)(2)(A), 30(c)(2)(B), and 31(a)(2) of the Investment Company Act.

[989] Public Law 104–121, Title II, 110 Stat. 857 (1996) (codified in various sections of 5 U.S.C., 15 U.S.C. and as a note to 5 U.S.C. 601).

[990] 44 U.S.C. 3501–3521.

1940, Exemption of acquisitions of securities issued by persons engaged in securities related businesses'' (OMB Control No. 3235–0561); ''Rule 18f–3 under the Investment Company Act of 1940, Multiple class companies'' (OMB Control No. 3235–0441); ''Rule 22e–3 under the Investment Company Act of 1940, Exemption for liquidation of money market funds'' (OMB Control No. 3235–0658); ''Rule 30b1–7 under the Investment Company Act of 1940, Monthly report for money market funds'' (OMB Control No. 3235–0657); ''Rule 31a–1 under the Investment Company Act of 1940, Records to be maintained by registered investment companies, certain majority-owned subsidiaries thereof, and other persons having transactions with registered investment companies'' (OMB Control No. 3235–0178); ''Rule 34b–1(a) under the Investment Company Act of 1940, Sales Literature Deemed to be Misleading'' (OMB Control No. 3235–0346); ''Rule 204(b)–1 under the Investment Advisers Act of 1940, Reporting by investment advisers to private funds'' (OMB Control No. 3235–0679); ''Rule 482 under the Securities Act of 1933, Advertising by an Investment Company as Satisfying Requirements of Section 10'' (OMB Control No. 3235–0565); ''Form N–1A under the Securities Act of 1933 and under the Investment Company Act of 1940, Registration statement of open-end management investment companies'' (OMB Control No. 3235–0307); ''Form N–MFP, Monthly schedule of portfolio holdings of money market funds'' (OMB Control No. 3235–0657); and ''Form PF, Reporting Form for Investment Advisers to Private Funds and Certain Commodity Pool Operators and Commodity Trading Advisers'' (OMB Control No. 3235–0679). We are also submitting new collections of information for new rule 30b1–8 and new Form N–CR under the Investment Company Act of 1940.[991] The Commission is submitting these collections of information to the OMB for review in accordance with 44 U.S.C. 3507(d) and 5 CFR 1320.11. An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless it displays a currently valid control number.

We are proposing two alternatives as part of our money market reform proposal, discussed separately below. Under the first alternative, we are proposing to require that certain money market funds have a floating NAV. Under the second alternative, we propose to require money market funds whose liquidity levels fell below a specified threshold to impose a liquidity fee unless the fund's board of directors determines such a fee would not be in the best interest of the fund, and permit the funds to suspend redemptions temporarily, *i.e.,* to ''gate'' the fund. Certain of the amendments we are proposing today would apply under either alternative.

*A. Alternative 1: Floating Net Asset Value*

1. Rule 2a–7

Under our floating NAV proposal, money market funds (other than government and retail money market funds) would no longer be permitted to use amortized cost or penny-rounding to maintain a stable price per share; instead, money market funds would be required to compute their share price by rounding the fund's current price per share to the fourth decimal place (in the case of a fund with a $1.0000 share price). Under this first alternative, we are proposing to amend rule 2a–7 (and consequently, amend or establish new collection of information burdens) by: (a) Requiring that retail money market funds seeking to rely on the exemption from our floating NAV proposal implement policies and procedures reasonably designed to allow the conclusion that Omnibus Account Holders do not permit beneficial owners of the fund from redeeming more than the permissible daily amount; (b) requiring money market funds to be diversified with respect to the sponsors of asset-backed securities by deeming the sponsor to guarantee the asset-backed security unless the fund's board of directors makes a special finding otherwise; (c) replacing the requirement that funds promptly notify the Commission via electronic mail of defaults and other events with disclosure on new Form N–CR; (d) eliminating the required procedure that money market funds' boards adopt written procedures that include shadow pricing; (e) amending the stress testing requirements; and (f) amending the disclosures that money market funds are required to post on their Web sites. Unless otherwise noted, the estimated burden hours discussed below are based on estimates of Commission staff with experience in similar matters. Several of the proposed amendments would create new collection of information requirements. The respondents to these collections of information would be money market funds, investment advisers and other service providers to money market funds, including financial intermediaries, as noted below. The currently approved burden for rule 2a–7 is 517,228 hours.

a. Retail Exemption From Floating NAV

Under our floating NAV proposal, retail money market funds would be exempt from floating their price per share; instead, retail funds would be permitted to maintain a stable price per share by computing its current price per share using the penny-rounding method. A retail money market fund would mean a money market fund that does not permit any shareholder of record to redeem more than $1 million each business day.[992] Our proposed amendment would permit a shareholder of record to redeem more than $1 million on any one business day if the shareholder of record is a broker, dealer, bank, or other person that holds securities issued by the money market fund in nominee name (''Omnibus Account Holder'') and the fund (or others in the intermediary chain) has policies and procedures reasonably designed to allow the conclusion that the Omnibus Account Holder does not permit any beneficial owner of the fund's shares, directly or indirectly, to redeem more than the daily permitted amount.[993] This requirement is a collection of information under the PRA, and is designed to address operational difficulties presented by Omnibus Account Holders and ensure that the $1 million daily redemption limit is not circumvented. The new collections of information would be mandatory for money market funds that rely on the exemption in proposed rule 2a–7(c)(3), and to the extent that the Commission receives confidential information pursuant to this collection of information, such information would be kept confidential, subject to the provisions of applicable law.[994]

For purposes of the PRA, staff estimates that approximately 100 money market fund complexes would rely on the proposed retail fund exemption and

[991] We also are proposing additional amendments that do not affect the relevant rules' paperwork collections (*e.g.,* we propose to amend Investment Company Act rule 12d3–1 solely to update cross references in that rule to provisions of rule 2a–7).

[992] *See* Proposed (FNAV) rule 2a–7(c)(3)(i).

[993] *See* Proposed (FNAV) rule 2a–7(c)(3)(ii).

[994] *See, e.g.,* 5 U.S.C. 552 (Exemption 4 of the Freedom of Information Act provides an exemption for ''trade secrets and commercial or financial information obtained from a person and privileged or confidential.'' 5 U.S.C. 552(b)(4). Exemption 8 of the Freedom of Information Act provides an exemption for matters that are ''contained in or related to examination, operating, or condition reports prepared by, or on behalf of, or for the use of an agency responsible for the regulation or supervision of financial institutions.'' 5 U.S.C. 552(b)(8)).

therefore be required to adopt written policies and procedures to ensure that Omnibus Account Holders apply the daily redemption limit to beneficial owners.[995] Staff estimates that it would take approximately 12 hours of a fund attorney's time to prepare the procedures and one hour for a board to adopt the procedures, at a time cost of approximately $8,548 per fund complex.[996] Therefore, staff estimates the one-time burden to prepare and adopt these procedures would be approximately 1,300 hours [997] at $854,800 in total time costs for all fund complexes.[998] Amortized over a three-year period, this would result in an average annual burden of approximately 433 hours and time costs of $284,933 for all funds.[999] Staff estimates that there would be no external costs associated with implementing this collection of information.

b. Asset-Backed Securities

Under the proposed amendments, funds would be required to treat the sponsor of an SPE issuing ABS as a guarantor of the ABS subject to rule 2a–7's diversification limitations applicable to guarantors and demand feature providers, unless the fund's board of directors (or its delegate) determines that the fund is not relying on the sponsor's financial strength or its ability or willingness to provide liquidity.[1000] The board of directors would be required to adopt written procedures requiring periodic evaluation of this determination.[1001] Furthermore, for a period of not less than three years from the date when the evaluation was most recently made, the fund must preserve and maintain in an easily accessible place a written record of the evaluation.[1002] This requirement is a collection of information under the PRA, and is designed to help ensure that the objectives of the diversification limitations are achieved. This new collection of information would be mandatory for money market funds that rely on rule 2a–7, and to the extent that the Commission receives confidential information pursuant to this collection of information, such information would be kept confidential, subject to the provisions of applicable law.[1003]

Based on its review of reports on Form N–MFP, Commission staff estimates that approximately 183 money market funds hold asset-backed securities and would be required to adopt written procedures regarding the periodic evaluation of determinations made by the fund as to ABS not subject to guarantees. Staff estimates that it would take approximately eight hours of a fund attorney's time to prepare the procedures and one hour for a board to adopt the procedures. Therefore, staff estimates the one-time burden to prepare and adopt these procedures would be approximately nine hours per money market fund, at a time cost of approximately $7,032 per fund.[1004] Therefore, staff estimates the one-time burden to prepare and adopt these procedures would be approximately 1,647 hours [1005] at $1.2 million in total time costs for all money market funds.[1006] Amortized over a three-year period, this would result in an average annual burden of approximately 549 hours and time costs of $400,000 for all funds.[1007] Commission staff further estimates that the 183 money market funds we estimate would adopt such written procedures would spend, on an annual basis, (i) two hours of a fund attorney's time to prepare materials for the board's review of new and existing determinations, (ii) one hour for the board to review those materials and make the required determinations, and (iii) one hour of a fund attorney's time per year, on average, to prepare the written records of such determinations.[1008] Therefore, staff estimates that the average annual burden to prepare materials and written records for a board's required review of new and existing determinations would be approximately four hours per fund [1009] at a time cost of approximately $5,137 per fund.[1010] Therefore, staff estimates the annual burden would be approximately 732 burden hours [1011] and $940,071 in total time costs for all money market funds.[1012] Amortized over a three-year period, this would result in an average annual burden of approximately 244 hours and time costs of $313,357 for all funds.[1013] There would be no external costs associated with this collection of information.

c. Notice to the Commission

Rule 2a–7 currently requires that money market funds promptly notify the Commission by electronic mail of any default or event of insolvency with respect to the issuer of one or more portfolio securities (or any issuer of a demand feature or guarantee) where immediately before the default the securities comprised one half of one percent or more of the fund's total assets.[1014] In addition, money market funds must also provide notice to the Commission of any purchase of its securities by an affiliated person in

[995] For purposes of the PRA, staff estimates that those money market funds that self-reported as ''retail'' funds as of February 28, 2013 (based on iMoney.net data) would likely rely on the proposed retail exemption from our floating NAV proposal.

[996] This estimate is based on the following calculation: ([12 hours × $379 per hour for an attorney = $4,548] + [1 hour × $4,000 per hour for a board of 8 directors = $4,000] = $8,548). All estimated wage figures discussed here and throughout section IV of this Release are based on published rates have been taken from SIFMA's Management & Professional Earnings in the Securities Industry 2012, *available at http://www.sifma.org/research/item.aspx?id=8589940603*, modified by Commission staff to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits, and overhead.

[997] This estimate is based on the following calculation: 12 burden hours to prepare written procedures + 1 burden hour to adopt procedures = 13 burden hours per money market fund complex; 13 burden hours per fund complex × 100 fund complexes = 1,300 total burden hours for all fund complexes.

[998] This estimate is based on the following calculation: 100 fund complexes × $8,548 in total costs per fund complex = $854,800.

[999] This estimate is based on the following calculation: 1,300 burden hours ÷ 3 = 433 average annual burden hours; $854,800 burden costs ÷ 3 = $284,933 average annual burden cost.

[1000] Proposed (FNAV) rule 2a–7(a)(16)(ii).

[1001] Proposed (FNAV) rule 2a–7(g)(6).

[1002] Proposed (FNAV) rule 2a–7(h)(6).

[1003] *See supra* note 994.

[1004] This estimate is based on the following calculation: [8 hours × $379 per hour for an attorney = $3,032] + [1 hour × $4,000 per hour for a board of 8 directors = $4,000] = $7,032.

[1005] This estimate is based on the following calculation: 8 burden hours to prepare written procedures + 1 burden hour to adopt procedures = 9 burden hours per money market fund required to adopt procedures; 9 burden hours per money market fund × 183 funds expected to adopt procedures = 1,647 total burden hours.

[1006] This estimate is based on the following calculation: 183 money market funds × $7,032 in total costs per fund complex = $1.2 million.

[1007] This estimate is based on the following calculations: 1,647 burden hours ÷ 3 = 549 average annual burden hours; $1.2 million burden costs ÷ 3 = $400,000 average annual burden cost.

[1008] This estimate includes documenting, if applicable, the fund board's determination that the fund is not relying on the fund sponsor's financial strength or its ability or willingness to provide liquidity or other credit support to determine the ABS's quality or liquidity. *See* proposed (FNAV) rule 2a–7(a)(16)(ii) and proposed (FNAV) rule 2a–7(h)(6).

[1009] This estimate is based on the following calculation: 2 hours to adopt + 1 hour for board review + 1 hour for record preparation = 4 hours per year.

[1010] This estimate is based on the following calculations: [3 hours × $379 per hour for an attorney = $1,137] + [1 hour × $4,000 per hour for a board of 8 directors = $4,000] = $5,137.

[1011] This estimate is based on the following calculation: 4 burden hours per money market fund × 183 funds = 732 total burden hours.

[1012] This estimate is based on the following calculation: 183 money market funds × $5,137 in total costs per fund complex = $940,071.

[1013] This estimate is based on the following calculation: 732 burden hours ÷ 3 = 244 average annual burden hours; $940,071 burden costs ÷ 3 = $313,357 average annual burden cost.

[1014] Rule 2a–7(c)(7)(iii)(A) (requiring that the notice include a description of the actions the money market fund intends to take in response to the event).

reliance on rule 17a–9 under the Investment Company Act.[1015] Based on conversations with individuals in the mutual fund industry, staff has previously estimated that the burden associated with these requirements is (1) .5 burden hours of professional legal time per response for each notification of an event of default or insolvency, and (2) 1.0 burden hours of professional legal time per response for each notification of the purchase of a money market fund's portfolio security by certain affiliated persons in reliance on rule 17a–9. The new collection of information would be mandatory for money market funds that rely on rule 2a–7, and to the extent that the Commission receives confidential information pursuant to this collection of information, such information would be kept confidential, subject to the provisions of applicable law.[1016]

We are proposing to eliminate the rule 2a–7 requirements that money market funds provide electronic notice of any event of default or insolvency of a portfolio security and any purchase by a fund of a portfolio security by an affiliate in reliance on rule 17a–9.[1017] Staff estimates that elimination of these requirements would reduce the current annual burden by 0.5 hours for notices of default or insolvency and 1 hour for notices of purchases in reliance on rule 17a–9. Based on our prior estimate of 20 money market funds per year that would be required to provide the notification of an event of default or insolvency, staff estimates that the proposed amendment would reduce the current collection of information by approximately 10 hours annually, at a total time cost savings of $3,790.[1018] Based on our prior estimate of 25 money market fund complexes per year that would be required to provide the notification of a purchase of a portfolio security in reliance on rule 17a–9, staff estimates that the proposed amendment would reduce the current collection of information by approximately 25 hours annually, at a total time cost savings of $9,475.[1019] There would be no external cost savings associated with these proposed amendments to the collection of information burdens.

d. Required Procedures

Rule 2a–7 currently requires that money market funds establish written procedures designed to stabilize the fund's NAV [1020] and guidelines and procedures relating to the board's delegation of authority.[1021] Based on conversations with individuals in the mutual fund industry, staff has previously estimated that the burden associated with these requirements is a one-time 15.5 burden hours per response for each new money market fund to formulate and establish these written procedures and guidelines.[1022] The new collection of information would be mandatory for money market funds that rely on rule 2a–7, and to the extent that the Commission receives confidential information pursuant to this collection of information, such information would be kept confidential, subject to the provisions of applicable law.[1023]

The Commission is proposing to eliminate the requirement that money market funds establish written procedures providing for the board's periodic review of the fund's shadow price, the methods used for calculating the shadow price, and what action, if any, the board should initiate if the fund's shadow price exceeds amortized cost by more than ½ of 1%.[1024] Staff estimates that elimination of this requirement would eliminate the current one-time 15.5 burden hours for each new money market fund to formulate and establish these written procedures and guidelines. Based on our prior estimate of 10 new money market funds per year that would be required to formulate and establish these written procedures and guidelines, staff estimates that the proposed amendments would reduce the current collection of information by approximately 155 hours, at a total time cost savings of $60,940.[1025] There would be no external cost savings associated with these proposed amendments to the collection of information burdens.

e. Stress Testing

We are proposing to amend the stress testing provision of rule 2a–7 to enhance the hypothetical events for which a fund (or its adviser) is required to stress test, including: (i) Increases (rather than changes) in the general level of short-term interest rates; (ii) downgrades or defaults of portfolio securities, and the effects these events could have on other securities held by the fund; (iii) ''widening or narrowing of spreads among the indexes to which interest rates of portfolio securities are tied''; (iv) other movements in interest rates that may affect the fund's portfolio securities, such as shifts in the yield curve; and (v) combinations of these and any other events the adviser deems relevant, assuming a positive correlation of risk factors.[1026] Floating NAV money market funds would be required to replace their current stress test for the ability to maintain a stable price per share with a test of the fund's ability to maintain 15% of its total assets in weekly liquid assets. Funds that are exempt from our floating NAV requirement would continue to test the fund's ability to maintain a stable share price as well. A written copy of the procedures, and any modifications thereto, must be maintained and preserved for a period of not less than six years following the replacement of such procedures with new procedures, the first two years in an easily accessible place.[1027] This requirement is a collection of information under the PRA, and is designed to address disparities in the quality and comprehensiveness of stress tests. The new collection of information would be mandatory for money market funds that rely on rule 2a–7, and to the extent that the Commission receives confidential information pursuant to this collection of information, such information would be kept confidential, subject to the provisions of applicable law.[1028]

We understand that most money market funds, in their normal course of risk management, include the elements we are proposing in their stress testing. Nevertheless, some smaller funds that perform their own stress testing (rather than use a third party service provider) may incur a one-time internal burden to reprogram an existing system to provide the required reports of stress testing results based on our proposed amendments. Staff estimates that each

[1015] Rule 2a–7(c)(7)(iii)(B) (requiring that the notice include identification of the security, its amortized cost, the sale price, and the reasons for the purchase).

[1016] *See supra* note 994.

[1017] These requirements are being replaced by new disclosure required on proposed Form N–CR. *See* Section IV.A.4 below.

[1018] This estimate is based on the following calculations: 20 funds × 0.5 reduction in hours per fund = reduction of 10 hours; 10 burden hours × $379 per hour for an attorney = $3,790.

[1019] This estimate is based on the following calculations: 25 fund complexes × 1 reduction in hours per fund = reduction of 25 hours; 25 hours × $379 per hour for an attorney = 9,475.

[1020] *See* rule 2a–7(c)(8)(ii).

[1021] *See* rule 2a–7(e)(1).

[1022] The 15.5 hours is comprised of: 0.5 hours of the board of directors' time; 7.2 hours of professional legal time; and 7.8 hours of support staff time.

[1023] *See supra* note 994.

[1024] *See* rule 2a–7(c)(8)(ii).

[1025] This estimate is based on the following calculations: 10 funds × 15.5 reduction in hours per fund = reduction of 155 hours; 10 funds × ([0.5 hours × $4,000 per hour for board time] + [7.2 hours × $379 per hour for an attorney] + [7.8 hours × $175 for a Paralegal]) = $60,940.

[1026] Proposed (FNAV) rule 2a–7(g)(7).

[1027] Proposed (FNAV) rule 2a–7(h)(8).

[1028] *See supra* note 994.

fund that would have to implement the proposed stress testing changes would incur an average one-time burden of 92 hours at a time cost of $42,688.[1029] Based on an estimate of 92 funds that would incur this one-time burden,[1030] staff estimates that the aggregate one-time burden for all money market funds to implement the proposed amendments to stress testing would be 8,464 hours at a total time cost of $3.9 million.[1031] Amortized over a three-year period, this would result in an average annual burden of 2,821 burden hours and $1.3 million total time cost for all funds.[1032] There would be no external costs associated with this collection of information.

f. Web Site Disclosure

We are proposing four amendments to the information money market funds are required to disclose on their Web sites. These amendments would promote transparency to investors of money market funds' risks and risk management by:

- Harmonizing the specific portfolio holdings information that rule 2a–7 currently requires funds to disclose on the fund's Web site with the corresponding portfolio holdings information proposed to be reported on Form N–MFP [1033];
- Requiring that a fund disclose on its Web site a schedule, chart, graph, or other depiction showing the percentage of the fund's total assets that are invested in daily and weekly liquid assets, as well as the fund's net inflows or outflows, as of the end of each business day during the preceding six months (which depiction must be updated each business day as of the end of the preceding business day) [1034];
- Requiring that a fund disclose on its Web site a schedule, chart, graph, or other depiction showing the fund's daily current NAV per share,[1035] as of the end of each business day during the preceding six months (which depiction must be updated each business day as of the end of the preceding business day) [1036]; and
- Requiring a fund to disclose on its Web site substantially the same information that the fund is required to report to the Commission on Form N–CR regarding the provision of financial support to the fund.[1037]

These new collections of information would be mandatory for money market funds that rely on rule 2a–7, and to the extent that the Commission receives confidential information pursuant to these collections of information, such information would be kept confidential, subject to the provisions of applicable law.[1038]

i. Disclosure of Portfolio Holdings Information

Because the new information that a fund would be required to disclose on its Web site overlaps with the information that a fund would be required to disclose on Form N–MFP, we anticipate that the burden for each fund to draft and finalize the disclosure that would appear on its Web site would largely be incurred when the fund files Form N–MFP.[1039] Commission staff estimates that a fund would incur an additional burden of 1 hour each time that it updates its Web site to include the new disclosure. Using an estimate of 586 money market funds that would be required to include the proposed new portfolio holdings disclosure on the fund's Web site,[1040] staff estimates that each fund would incur 12 additional hours of internal staff time per year (1 hour per monthly filing), at a time cost of $2,484,[1041] to update the Web site to include the new disclosure, for a total of 7,032 aggregate hours per year,[1042] at a total aggregate time cost of $1,455,624.[1043] There would be no external costs associated with this collection of information.

ii. Disclosure of Daily Liquid Assets and Weekly Liquid Assets

The burdens associated with the proposed requirement for a fund to disclose on its Web site a schedule, chart, graph, or other depiction showing the percentage of the fund's total assets that are invested in daily and weekly liquid assets, as well as the fund's net inflows or outflows, include one-time burdens as well as ongoing burdens. Commission staff expects that each money market fund would incur a one-time burden of 70 hours,[1044] at a time cost of $20,150,[1045] to design the required schedule, chart, graph, or other depiction, and to make the necessary software programming changes to the fund's Web site to disclose the percentage of the fund's total assets that are invested in daily liquid assets and weekly liquid assets, as well as the fund's net inflows or outflows, as of the end of each business day during the preceding six months. Using an estimate of 586 money market funds,[1046] staff estimates that money market funds would incur, in aggregate, a total one-time burden of 41,020 hours,[1047] at a

[1029] Staff estimates that these systems modifications would include the following costs: (i) project planning and systems design (24 hours × $291 (hourly rate for a senior systems analyst) = $6,984); (ii) systems modification integration, testing, installation, and deployment (32 hours × $282 (hourly rate for a senior programmer) = $9,024); (iii) drafting, integrating, implementing procedures and controls (24 hours × $327 (blended hourly rate for assistant general counsel ($467), chief compliance officer ($441), senior EDP auditor ($273) and operations specialist ($126)) = $7,848); and (iv) preparation of training materials ((8 hours × $354 (hourly rate for an assistant compliance director)) + (4 hours (4 hour training session for board of directors) × $4,000 (hourly rate for board of 8 directors)) = $18,832). Therefore, staff estimates an average one-time burden of 92 hours (24 + 32 + 24 + 8 + 4), at a total cost per fund of $42,688 ($6,984 + $9,024 + $7,848 + $18,832).

[1030] This estimate is based on staff experience and discussions with industry.

[1031] This estimate is based on the following calculations: 92 funds × 92 hours per fund = 8,464 hours; 92 funds × $42,688 = $3.9 million.

[1032] This estimate is based on the following calculations: 8,464 hours ÷ 3 = 2,821 burden hours; $3.9 million ÷ 3 = $1.3 million burden cost.

[1033] Proposed (FNAV) rule 2a–7(h)(10)(i).

[1034] Proposed (FNAV) rule 2a–7(h)(10)(ii).

[1035] *See supra* notes 644 and 645 and accompanying text for discussion of the definition of ''current NAV.''

[1036] Proposed (FNAV) rule 2a–7(h)(10)(iii).

[1037] Proposed (FNAV) rule 2a–7(h)(10)(v).

[1038] *See supra* note 994.

[1039] *See* section IV.A.3 below.

[1040] This estimate is based on a staff review of reports on Form N–MFP filed with the Commission for the month ended February 28, 2013.

[1041] This estimate is based on the following calculation: 12 hours × $207 per hour for a webmaster = $2,484.

[1042] This estimate is based on the following calculation: 12 hours per year × 586 money market funds = 7,032 hours.

[1043] This estimate is based on the following calculation: 7,032 hours × $207 per hour for a webmaster = $1,455,624.

[1044] In the economic analysis sections of this Release, Commission staff estimates that the lower bound of the range of the initial, one-time hour burden to design and present the historical depiction of daily and weekly liquid assets and the fund's net inflows and outflows would include the following: 16 hours (project assessment) + 40 hours (project development, implementation, and testing) = 56 hours. Commission staff estimates that the upper bound of the range of the initial, one-time hour burden to design and present the historical depiction of daily and weekly liquid assets and the fund's net inflows and outflows would include the following: 24 hours (project assessment) + 60 hours (project development, implementation, and testing) = 84 hours.

Because we do not have the information necessary to provide a point estimate, we are unable to estimate the costs to modify a particular fund's systems and thus have provided ranges of estimated costs in our economic analysis. *See* section III.F.2.b and accompanying notes. Likewise, for purposes of our estimates for the PRA analysis, we have taken the midpoint of the range discussed above (mid-point of 56 hours and 84 hours = 70 hours).

[1045] This estimate is based on the following calculations: (20 hours (mid-point of 16 hours and 24 hours for project assessment) × $290 (blended rate for a compliance manager and a compliance attorney) = $5,800) + (50 hours (mid-point of 40 hours and 60 hours for project development, implementation, and testing) × $287 (blended rate for a Senior Systems Analyst and senior programmer) = $14,350) = $20,150 per fund.

[1046] *See supra* note 1040.

[1047] This estimate is based on the following calculation: 70 hours × 586 money market funds = 41,020 hours.

time cost of $11,807,900,[1048] to comply with these Web site disclosure requirements. Commission staff estimates that each fund would incur an ongoing annual burden of 32 hours,[1049] at a time cost of $9,184,[1050] to update the depiction of daily and weekly liquid assets and the fund's net inflows or outflows on the fund's Web site each business day during that year; in aggregate, staff estimates that money market funds would incur an average ongoing annual burden of 18,752 hours,[1051] at a time cost of $5,381,824,[1052] to comply with this disclosure requirement. Amortizing these hourly and cost burdens over three years results in an average annual increased burden of 26,175 burden hours [1053] at a time cost of $7,523,849.[1054] There would be no external costs associated with this collection of information.

iii. Disclosure of Daily Current NAV

The burdens associated with the proposed requirement for a fund to disclose on its Web site a schedule, chart, graph, or other depiction showing the fund's daily current NAV [1055] as of the end of the previous business day include one-time burdens as well as ongoing burdens. Commission staff expects that these one-time and ongoing burdens will be substantially similar to the burdens associated with the proposed requirement regarding Web site disclosure of daily liquid assets and weekly liquid assets, discussed above. This is because staff expects the core activities associated with both of these Web site disclosure requirements (designing the required schedule, chart, graph, or other depiction; making necessary software programming changes; and updating the Web site disclosure each day) would be identical for each requirement, and expects that the burdens associated with these activities will not vary substantially based on the substance of the disclosure necessitated by each requirement. As discussed below, staff believes that funds will incur no additional burden obtaining current NAV data for purposes of the proposed requirement regarding Web site disclosure of the fund's daily current NAV.

Commission staff expects that each money market fund would incur a one-time burden of 70 hours,[1056] at a time cost of $20,150,[1057] to design the required schedule, chart, graph, or other depiction, and to make the necessary software programming changes to the fund's Web site to disclose the fund's daily current NAV as of the end of each business day during the preceding six months. Using an estimate of 586 money market funds,[1058] Commission staff estimates that money market funds would incur, in aggregate, a total one-time burden of 41,020 hours,[1059] at a time cost of $11,807,900,[1060] to comply with these Web site disclosure requirements. Commission staff estimates that each fund would incur an annual ongoing burden of 32 hours,[1061] at a time cost of $9,184,[1062] to update the depiction of the fund's daily current NAV on the fund's Web site each business day during that year; in aggregate, staff estimates that money market funds would incur an ongoing annual burden on 18,752 hours,[1063] at a time cost of $5,381,824,[1064] to comply with this disclosure requirement. Amortizing these hourly and cost burdens over three years results in an average annual increased burden of 26,175 burden hours [1065] at a time cost of $7,523,849.[1066] There would be no external costs associated with this collection of information.

Because floating NAV money market funds would be required to calculate their redemption price each day, these funds should incur no additional burdens in obtaining this data for purposes of the proposed disclosure requirements. Stable price money market funds (including government money market funds and retail funds if

[1048] This estimate is based on the following calculation: $20,150 per fund × 586 money market funds = $11,807,900.

[1049] Commission staff estimates that the lower bound of the range of the ongoing annual hour burden to update the required Web site information would be 21 hours per year (5 minutes per day × 252 business days in a year = 1,260 minutes, or 21 hours). Commission staff estimates that the upper bound of the range of the ongoing annual hour burden to update the required Web site information would be 42 hours per year (10 minutes per day × 252 business days in a year = 2,520 minutes, or 42 hours).

Because we do not have the information necessary to provide a point estimate of the costs to modify a particular fund's systems we thus have provided ranges of estimated costs in our economic analysis. *See* section III.F.2.b and accompanying notes. Likewise, for purposes of our estimates for the PRA analysis, we have taken the mid-point of the range discussed above (mid-point of 21 hours and 42 hours = 32 hours).

[1050] This estimate is based on the following calculation: 32 hours (mid-point of 21 hours and 42 hours) × $287 (blended rate for a senior systems analyst and senior programmer) = $9,184.

[1051] This estimate is based on the following calculation: 32 hours × 586 money market funds = 18,752 hours.

[1052] This estimate is based on the following calculation: $9,184 per fund × 586 money market funds = $5,381,824.

[1053] This estimate is based on the following calculation: (41,020 burden hours (year 1) + 18,752 burden hours (year 2) + 18,752 burden hours (year 3)) ÷ 3 = 26,175 hours.

[1054] This estimate is based on the following calculation: ($11,807,900 (year 1 monetized burden hours) + $5,381,824 (year 2 monetized burden hours) + $5,381,824 (year 3 monetized burden hours)) ÷ 3 = $7,523,849.

[1055] *See supra* notes 644 and 645 and accompanying text for discussion of the definition of ''current NAV.''

[1056] Commission staff estimates that the lower bound of the range of the initial, one-time hour burden to design and present the historical depiction of the fund's daily current NAV would include the following: 16 hours (project assessment) + 40 hours (project development, implementation, and testing) = 56 hours. Commission staff estimates that the upper bound of the range of the initial, one-time hour burden to design and present the historical depiction of daily liquid assets and weekly liquid assets would include the following: 24 hours (project assessment) + 60 hours (project development, implementation, and testing) = 84 hours.

Because we do not have the information necessary to provide a point estimate of the costs to modify a particular fund's systems we thus have provided ranges of estimated cost in our economic analysis. *See supra* section III.F.3.b and accompanying notes. Likewise, for purposes of our estimates for the PRA analysis, we have taken the midpoint of the range discussed above (mid-point of 56 hours and 84 hours = 70 hours).

[1057] This estimate is based on the following calculations: (20 hours (mid-point of 16 hours and 24 hours for project assessment) × $290 (blended rate for a compliance manager and a compliance attorney) = $5,800) + (50 hours (mid-point of 40 hours and 60 hours for project development, implementation, and testing) × $287 (blended rate for a senior systems analyst and senior programmer) = $14,350) = $20,150 per fund.

[1058] *See supra* note 1040.

[1059] This estimate is based on the following calculation: 70 hours × 586 money market funds = 41,020 hours.

[1060] This estimate is based on the following calculation: $20,150 per fund × 586 money market funds = $11,807,900.

[1061] Commission staff estimates that the lower bound of the range of the ongoing annual hour burden to update the required Web site information would be 21 hours per year (5 minutes per day × 252 business days in a year = 1,260 minutes, or 21 hours). Commission staff estimates that the upper bound of the range of the ongoing annual hour burden to update the required Web site information would be 42 hours per year (10 minutes per day × 252 business days in a year = 2,520 minutes, or 42 hours).

Because we do not have the information necessary to provide a point estimate of the costs to modify a particular fund's systems we thus have provided ranges of estimated costs in our economic analysis. *See supra* section III.F.3.b and accompanying notes. Likewise, for purposes of our estimates for the PRA analysis, we have taken the mid-point of the range discussed above (mid-point of 21 hours and 42 hours = 32 hours).

[1062] This estimate is based on the following calculation: 32 hours (mid-point of 21 hours and 42 hours) × $287 (blended rate for a senior systems analyst and senior programmer) = $9,184.

[1063] This estimate is based on the following calculation: 32 hours × 586 money market funds = 18,752 hours.

[1064] This estimate is based on the following calculation: $9,184 × 586 money market funds = $5,381,824.

[1065] This estimate is based on the following calculation: 41,020 burden hours (year 1) + 18,752 burden hours (year 2) + 18,752 burden hours (year 3) ÷ 3 = 26,175 hours.

[1066] This estimate is based on the following calculation: $11,807,900 (year 1 monetized burden hours) + $5,381,824 (year 2 monetized burden hours) + $5,381,824 (year 3 monetized burden hours) ÷ 3 = $7,523,849.

we adopt the floating NAV proposal, and all money market funds if we adopt the fees and gates proposal), which would be required to calculate their current NAV per share daily pursuant to proposed amendments to rule 2a–7, likewise should incur no additional burdens in obtaining this data for purposes of the proposed disclosure requirements.[1067]

iv. Disclosure of Financial Support Provided to Money Market Funds

Commission staff estimates that the Commission would receive 40 reports per year filed in response to an event specified on Part C (''Provision of financial support to Fund'') of Form N–CR.[1068] Because the required Web site disclosure overlaps with the information that a fund must disclose on Form N–CR when the fund receives financial support from a sponsor or fund affiliate, we anticipate that the burdens a fund would incur to draft and finalize the disclosure that would appear on its Web site would largely be incurred when the fund files Form N–CR.[1069] Commission staff estimates that a fund would incur an additional burden of 1 hour, at a time cost of $207,[1070] each time that it updates its Web site to include the new disclosure. Accordingly, Commission staff estimates that the requirement to disclose information about financial support received by a money market fund on the fund's Web site would result in a total aggregate burden of 40 hours per year,[1071] at a total aggregate time cost of $8,280.[1072] There would be no external costs associated with this collection of information.

v. Change in Burden

The aggregate additional annual burden associated with the proposed Web site disclosure requirements discussed above is 59,422 hours [1073] at a time cost of $16,511,602.[1074] Amortized over a three-year period, this would result in an average annual burden of 19,807 burden hours and $5,503,867 total time cost for all funds.[1075] There would be no change in the external cost burden associated with this collection of information.

g. Total Burden for Rule 2a–7

The currently approved burden for rule 2a–7 is 517,228 hours. The net aggregate additional burden hours associated with the proposed amendments to rule 2a–7 would increase the burden estimate to 540,892 hours annually for all funds.[1076]

2. Rule 22e–3

Rule 22e–3 under the Investment Company Act exempts money market funds from section 22(e) of the Act to permit them to suspend redemptions and postpone payment of redemption proceeds in order to facilitate an orderly liquidation of the fund, provided that certain conditions are met.[1077] Rule 22e–3 is intended to facilitate an orderly liquidation, reduce the vulnerability of shareholders to the harmful effects of a disorderly fund liquidation, and minimize the potential for market disruption.

The rule requires a money market fund to provide prior notification to the Commission of its decision to suspend redemptions and liquidate.[1078] This requirement is a collection of information under the PRA, and is designed to assist Commission staff in monitoring a money market fund's suspension of redemptions. The new collection of information would be mandatory for any fund that holds itself out as a money market fund in reliance on rule 2a–7 and any conduit funds that rely on the rule,[1079] and to the extent that the Commission receives confidential information pursuant to this collection of information, such information would be kept confidential, subject to the provisions of applicable law.[1080]

The current approved annual aggregate collection of information for rule 22e–3 is approximately 30 minutes to provide the required notification under the rule. To provide shareholders with protections comparable to those currently provided by the rule while also updating the rule to make it consistent with our proposed amendments to rule 2a–7, we are proposing to amend rule 22e–3 under our floating NAV proposal to allow a money market fund to invoke the exemption in rule 22e–3 if: (1) The fund, at the end of a business day, has invested less than 15% of its total assets in weekly liquid assets; or (2) in the case of a fund relying on the exemption for government money market funds or retail money market funds, the money market fund's price per share has deviated from the stable price established by the board of directors or the fund's board of directors, including a majority of directors who are not interested persons of the fund, determines that such a deviation is likely to occur.[1081]

These amendments are designed to permit a money market fund to suspend redemptions under our floating NAV proposal when the fund is under significant stress, as the funds may do today under rule 22e–3. We do not expect that money market funds would invoke the exemption provided by rule 22e–3 more frequently under our floating NAV proposal than they do today because, although we propose to change the circumstances under which a money market fund may invoke the exemption provided by rule 22e–3, the rule as we propose to amend it still

[1067] *See supra* section III.F.5 (discussing the proposed requirement for stable price money market funds to calculate their current NAV per share daily, as well as the operational costs associated with this proposed daily calculation requirement).

[1068] Commission staff estimates this figure based in part by reference to our estimate of the average number of notifications of security purchases in reliance on rule 17a–9 that money market funds currently file each year. *See supra* note 1019 and accompanying text. Because money market funds would be required to file a report in response to an event specified on Part C of Form N–CR if the fund receives any form of financial support from the fund's sponsor or other affiliated person (which support includes, but is not limited to, a rule 17a–9 security purchase), staff estimates that the Commission would receive a greater number of Form N–CR Part C reports than the number of notifications of rule 17a–9 security purchases that it currently receives.

[1069] *See infra* section IV.A.4.

[1070] This estimate is based on the following calculation: 1 hour per Web site update × $207 per hour for a webmaster = $207.

[1071] This estimate is based on the following calculation: 1 hour per Web site update × 40 Web site updates made by money market funds = 40 hours.

[1072] This estimate is based on the following calculation: 40 hours per year × $207 per hour for a webmaster = $8,280.

[1073] This estimate is based on the following calculation: 7,032 hours (annual aggregate burden for disclosure of portfolio holdings information) + 26,175 (annual aggregate burden for disclosure of daily liquid assets and weekly liquid assets) + 26,175 (annual aggregate burden for disclosure of daily current NAV) + 40 hours (annual aggregate burden for disclosure of financial support provided to money market funds) = 59,422 hours.

[1074] This estimate is based on the following calculation: $1,455,624 (annual aggregate costs associated with disclosure of portfolio holdings information) + $7,523,849 (annual aggregate costs associated with disclosure of daily liquid assets and weekly liquid assets) + $7,523,849 (annual aggregate costs associated with disclosure of daily current NAV) + $8,280 (annual aggregate costs associated with disclosure of financial support provided to money market funds) = $16,511,602.

[1075] This estimate is based on the following calculation: 59,422 hours ÷ 3 = 19,807 burden hours; $16,511,602 ÷ 3 = $5,503,867 burden cost.

[1076] This estimate is based on the following calculation: 517,228 hours (currently approved burden) + 433 hours (retail exemption) + (549 hours + 244 hours) (ABS determination & recordkeeping) − (10 hours + 25 hours) (notice to the Commission) − 155 hours (required procedures) + 2,821 hours (stress testing) + 19,807 hours (Web site disclosure) = 540,892 hours.

[1077] Rule 22e–3(a).

[1078] Rule 22e–3(a)(3).

[1079] The rule permits funds that invest in a money market fund pursuant to section 12(d)(1)(E) of the Act (''conduit funds'') to rely on the rule, and requires the conduit fund to notify the Commission of its reliance on the rule. *See* rule 22e–3(b).

[1080] *See supra* note 994.

[1081] Proposed (FNAV) rule 22e–3(a)(1).

would permit a money market fund to invoke the exemption only when the fund is under significant stress, and our staff estimates that a money market fund is likely to experience that level of stress and choose to suspend redemptions in reliance on rule 22e–3 with the same frequency that funds today may do so.

Therefore, we are not revising rule 22e–3's current approved annual collection of information. The rule's current approved annual aggregate burden is approximately 30 minutes, as discussed above, and is based on our staff's estimates that: (1) on average, one money market fund would break the buck and liquidate every six years; [1082] (2) there are an average of two conduit funds that may be invested in a money market fund that breaks the buck; [1083] and (3) each money market fund and conduit fund would spend approximately one hour of an in-house attorney's time every six years to prepare and submit the notice required by the rule.[1084] There is no change in the external cost burden associated with this collection of information.

3. Rule 30b1–7 and Form N–MFP

Rule 30b1–7 under the Investment Company Act currently requires money market funds to file electronically a monthly report on Form N–MFP within five business days after the end of each month. The information required by the form must be data-tagged in XML format and filed through EDGAR. The rule is designed to improve transparency of information about money market funds' portfolio holdings and facilitate Commission oversight of money market funds. Preparing a report on Form N–MFP is a collection of information under the PRA.[1085] This new collection of information would be mandatory for money market funds that rely on rule 2a–7, and to the extent that the Commission receives confidential information pursuant to these collections of information, such information would be kept confidential, subject to the provisions of applicable law.[1086] The Commission staff estimates that 586 money market funds are required to file reports on Form N–MFP on a monthly basis.[1087]

a. Discussion of Proposed Amendments

For the reasons discussed in detail in section III.H above, we are proposing a number of amendments to Form N–MFP which would include new and amended collections of information. These changes include:

*Structural Changes to Form N–MFP.* The proposed amendments would renumber the items of Form N–MFP to separate the items into four separate sections to allow Commission staff to reference, add or delete items in the future without having to re-number all subsequent items in the form.[1088] We expect that these modifications would be made regardless of what action, if any, we take regarding the proposed alternatives to money market reform.

*Amendments Related to Rule 2a–7 Reforms.* The proposed amendments would make a number of conforming changes to reflect the proposed amendments to rule 2a–7 under either alternative proposal. Our proposed amendments would also delete or modify items related to amortized cost and shadow prices that would no longer be applicable under either proposal.

*New Reporting Requirements.* We are proposing a number of new reporting requirements designed to improve the Commission's and others ability to monitor money market funds. The proposed amendments would amend Form N–MFP to require the following new items: (1) The Legal Entity Identifier (''LEI'') of the registrant (if available); (2) contact information for the person authorized to receive information and respond to questions about Form N–MFP; (3) in addition to the CUSIP for each security, the LEI that corresponds to each security and at least one other security identifier; (4) the level measurement (level 1, level 2, level 3) each security valuation is based upon in the fair value hierarchy under U.S. GAAP, the amount of cash held, the total value of the fund's ''daily liquid assets'' and ''weekly liquid assets'' reported as of the close of business on each Friday during the month reported, the weekly gross subscriptions and weekly gross redemptions for each share class as of the close of business for each Friday during the month reported, and whether a security is a ''daily liquid asset'' or ''weekly liquid asset;'' (5) whether any person paid for or waived all or part of the fund's operating expenses or management fees and the total percentage of shares outstanding held by the 20 largest shareholders of record; and (6) additional information about certain types of securities held by the fund. Finally, the proposed amendments would include new disclosure items regarding each security held by the fund series, and sold by the fund series, reported separately for each lot purchased. We expect that these modifications would be made regardless of what action, if any, we take regarding the proposed alternative to money market reform.

*Clarifying Amendments.* The proposed amendments to Form N–MFP would also include amendments to the current instructions and items of Form N–MFP designed to: (1) Clarify in the general instructions to Form N–MFP that a fund may report information on Form N–MFP as of the last business day or any later calendar day of the month; (2) clarify in the definition of ''master-feeder fund'' that ''Feeder Fund'' includes unregistered funds; (3) cross reference WAM and WAL as used in Form N–MFP with those terms as defined in rule 2a–7; (4) clarify that disclosure in Part B (Class-Level Information about the Fund) is required for each class of the series, regardless of the number of shares outstanding in the class; (5) clarify the required disclosure related to repurchase agreements, and (6) remove the reference to disclosure of the coupon or yield from the requirement that funds disclose the title of the issue. We expect that these modifications would be made regardless of what action, if any, we take regarding the proposed alternative to money market reform.

b. Current Burden

The current approved collection of information for Form N–MFP is 45,214 annual aggregate hours and $4,424,480 in external costs.

[1082] This estimate is based upon the Commission's experience with the frequency with which money market funds have historically required sponsor support. Although many money market fund sponsors have supported their money market funds in times of market distress, for purposes of this estimate Commission staff conservatively estimates that one or more sponsors may not provide support.

[1083] These estimates are based on a staff review of filings with the Commission. Generally, rule 22e–3 permits conduit funds to suspend redemptions in reliance on rule 22e–3 and requires that they notify the Commission if they elect to do so. *See supra* note 1079.

[1084] This estimate is based on the following calculations: (1 hour ÷ 6 years) = 10 minutes per year for each fund and conduit fund that is required to provide notice under the rule. 10 minutes per year × 3 (combined number of affected funds and conduit funds) = 30 minutes. The estimated costs associated with the estimated burden hours ($189) are based on the following calculations: $378/hour (hourly rate for an in-house attorney) × 30 minutes = $189.

[1085] For purposes of the PRA analysis, the current burden associated with the requirements of rule 30b1–7 is included in the collection of information requirements of Form N–MFP.

[1086] *See supra* note 994.

[1087] This estimate is based on a staff review of reports on Form N–MFP filed with the Commission for the month ended February 28, 2013.

[1088] *See* Proposed Form N–MFP. The proposed four sections are: (i) general information; (ii) information about each series of the fund; (iii) information about each class of the fund; and (iv) information about portfolio securities.

c. Change in Burden

Staff understands that approximately 35% of the 586 [1089] (for a total of 205 [1090]) money market funds that report information on Form N–MFP license a software solution from a third party that is used to assist the funds to prepare and file the required information. Staff also understands that approximately 65% of the 586 [1091] (for a total of 381) money market funds that report information on Form N–MFP retain the services of a third party to provide data aggregation and validation services as part of the preparation and filing of reports on Form N–MFP on behalf of the fund. Staff estimates that, in the first year, each fund (regardless of whether the fund licenses the software or uses a third-party service provider) will incur an additional average annual burden of 85 hours, at a time cost of $22,045 per fund,[1092] to prepare and file the report on Form N–MFP (as proposed) and an average of approximately 60 additional burden hours (five hours per fund, per filing), at a time cost of $15,562 per fund [1093] each year thereafter.

Staff also understands that software service providers (whether provided by a licensor or third-party service provider) are likely to incur additional external costs to modify their software and may pass those costs down to money market funds in the form of higher annual licensing fees. Although we do not have the information necessary to provide a point estimate of the external costs or the extent to which the software service providers will pass down any external costs to funds, we can estimate a range of costs, from 5% to 10% of current annual licensing fees. Accordingly, staff estimates that 35% of funds (205 funds) would pay $336 in additional external licensing costs each year and 65% of funds (381 funds) would pay $800 in additional external licensing costs each year because of our proposed amendments.[1094]

Staff therefore estimates that our proposed amendments to Form N–MFP would result in a first-year aggregate additional 49,810 burden hours [1095] at a total time cost of $12.9 million [1096] plus $373,680 in total external costs [1097] for all funds, and 35,160 burden hours [1098] at a total time cost of $9.1 million [1099] plus $373,680 in total external costs [1100] for all funds each year hereafter. Amortizing these additional hourly and cost burdens over three years results in an average annual aggregate burden of approximately 40,043 hours at a total time cost of $10.4 million plus $373,680 in external costs for all funds.[1101] Finally, staff estimates that our proposed amendments to Form N–MFP would result in a total aggregate annual collection of information burden of 85,257 hours [1102] and $4,798,160 in external costs.[1103]

4. Rule 30b1–8 and Form N–CR

a. Discussion of New Reporting Requirements

As outlined above, proposed new rule 30b1–8 would require money market funds to file new Form N–CR with the Commission when certain events occur. Similar to Form 8–K under the Exchange Act,[1104] Form N–CR would require disclosure, by means of a current report filed with the Commission, of certain specific reportable events. Under the floating NAV alternative, the information reported on Form N–CR would include instances of portfolio security default, sponsor support of funds, and certain significant deviations in net asset value.[1105] This requirement is a collection of information under the PRA, and is designed to enhance the Commission's oversight of money market funds and its ability to respond to market events. This new collection of information would be mandatory for money market funds that rely on rule 2a–7, and to the extent that the Commission receives confidential information pursuant to these collections of information, such information would be kept confidential, subject to the provisions of applicable law.[1106]

b. Estimated Burden

The staff estimates that the Commission would receive, in the aggregate, an average of 20 reports [1107] per year filed in response to an event specified on Part B (''Default or Event of Insolvency of Portfolio Security Issuer''), an average of 40 reports [1108]

[1089] This estimate is based on staff review of reports on Form N–MFP filed with the Commission for the month ended February 28, 2013.

[1090] The staff estimated this 35% in the current burden. This estimate is based on the following calculation: 586 funds × 35% = 205 funds.

[1091] The staff estimated this 65% in the current burden. This estimate is based on the following calculation: 586 funds × 65% = 381 funds.

[1092] This estimate is based on the following calculations: [30 hours for the initial monthly filing at a total cost of $7,800 per fund (8 hours × $243 blended average hourly rate for a financial reporting manager ($294 per hour) and fund senior accountant ($192 per hour) = $1,944 per fund) + (4 hours × $155 per hour for an intermediate accountant = $620 per fund) + (6 hours × $314 per hour for a senior database administrator = $1,884 per fund) + (4 hours × $300 for a senior portfolio manager = $1,200 per fund) + (8 hours × $269 per hour for a compliance manager = $2,152 per fund)] + [55 hours (5 hours per fund × 11 monthly filings) at a total cost of $14,245 per fund ($259 average cost per fund per burden hour × 55 hours)]. The additional average annual burden per fund for the first year is 85 hours (30 hours (initial monthly filing) + 55 hours (remaining 11 monthly filings)) and the additional average cost burden per fund for the first year is $22,045 ($7,800 (initial monthly filing) + $14,245 (remaining 11 monthly filings = $22,045).

[1093] This estimate is based on the following calculations: (16 hours × $243 blended average hourly rate for a financial reporting manager ($294 per hour) and fund senior accountant ($192 per hour) = $3,888 per fund) + (9 hours × $155 per hour for an intermediate accountant = $1,395 per fund) + (13 hours × $314 per hour for a senior database administrator = $4,082 per fund) + (9 hours × $300 for a senior portfolio manager = $2,700 per fund) + (13 hours × $269 per hour for a compliance manager = $3,497 per fund) = 60 hours (16 + 9 + 13 + 9 + 13) at a total cost of $15,562 per fund ($3,888 + $1,395 + $4,082 + $2,700 + $3,497). Therefore, the additional average cost per fund per burden hour is approximately $259 ($15,562/60 burden hours).

[1094] Staff estimates that the annual licensing fee for 35% of money market funds is $3,360: A 5% to 10% increase = $168–$336 in increased costs; staff estimates that the annual licensing fee for 65% of money market funds is $8,000: A 5% to 10% increase = $400–$800 in increased costs.

[1095] This estimate is based on the following calculation: 586 funds × 85 hours = 49,810 burden hours in year 1.

[1096] This estimate is based on the following calculation: 586 funds × $22,045 annual cost per fund in the initial year = $12.9 million.

[1097] This estimate is based on the following calculation: (205 funds × $336 additional external costs) + (381 funds × $800 additional external costs) = $373,680.

[1098] This estimate is based on the following calculation: 586 funds × 60 hours per fund = 35,160 hours.

[1099] This estimate is based on the following calculation: 586 funds × $15,562 annual cost per fund in subsequent years = $9.1 million.

[1100] *See supra* note 1097.

[1101] This estimate is based on the following calculation: (49,810 hours (year 1) + 35,160 hours (year 2) + 35,160 hours (year 3)) ÷ 3 = 40,043 hours; ($12.9 million (year 1) + $9.1million (year 2) + $9.1 million (year 3)) ÷ 3 = $10.4 million in time costs; + ($373,680 (year 1) + $373,680 (year 2) + $373,680 (year 3)) ÷ 3 = $373,680 million in external costs.

[1102] This estimate is based on the following calculation: current approved burden of 45,214 hours + 40,043 in additional burden hours as a result of our proposed amendments = 85,257 hours.

[1103] This estimate is based on the following calculation: current approved burden of $4,424,480 in external costs + $373,680 in additional external costs as a result of our proposed amendments = $4,798,160.

[1104] 17 CFR 249.308.

[1105] *See* proposed (FNAV) Form N–CR Parts A–D; *see also* section III.G.1.

[1106] *See supra* note 994.

[1107] Commission staff estimates this figure based in part by reference to our current estimate of an average of 20 notifications to the Commission of an event of default or insolvency that money market funds currently file pursuant to rule 2a–7(c)(7)(iii) each year. *See Submission for OMB Review, Comment Request, Extension: Rule 2a–7, OMB Control No. 3235–0268,* Securities and Exchange Commission [77 FR 236 (Dec. 7, 2012)].

[1108] Commission staff estimates this figure based in part by reference to our current estimate of an average of 25 notifications to the Commission of certain security purchases that money market funds

Continued

per year filed in response to an event specified on Part C (''Provision of Financial Support to Fund''), and an average of 1 report filed every 6 years [1109] in response to an event specified on Part D (''Deviation Between Current Net Asset Value Per Share and Intended Stable Price Per Share'') of Form N–CR.

When filing a report on Form N–CR,[1110] staff estimates that a fund would spend on average approximately 4 hours [1111] of an in-house attorney's and one hour of in-house accountant's time to prepare, review and submit Form N–CR, at a total time cost of $1,708.[1112] Accordingly, in the aggregate, staff estimates that compliance with new rule 30b1–8 and Form N–CR would result in a total annual burden of approximately 301 burden hours and total annual time costs of approximately $102,765.[1113] Given an estimated 586 money market funds that would be required to comply with new rule 30b1–8 and Form N–CR,[1114] this would result in an annual burden of approximately 0.51 burden hours and annual time costs of approximately $175 on a per-fund basis. Staff estimates that there will be no external costs associated with this collection of information.

5. Rule 34b–1(a)

Rule 34b–1 under the Act is an antifraud provision governing sales material that accompanies or follows the delivery of a statutory prospectus. Among other things, rule 34b–1 deems to be materially misleading any advertising material by a money market fund required to be filed with the Commission by section 24(b) of the Act that includes performance data, unless such advertising also includes the rule 482(b)(4) risk disclosures already discussed in section IV.A.6 below. Because we are amending the wording of the rule 482(b)(4) risk disclosures, rule 34b–1(a) is indirectly affected by our proposed amendments. However, we are proposing no changes to rule 34b–1(a) itself.

We already account for the burdens associated with the wording changes to the risk disclosures in money market fund advertising when discussing our amendments to rule 482(b)(4).[1115] By complying with our amendments to rule 482(b)(4), money market funds would also automatically remain in compliance with respect to how our proposed changes would affect rule 34b–1(a). Therefore, any burdens associated with rule 34b–1(a) as a result of our proposed amendment to rule 482(b)(4) are already accounted for in section IV.A.6 below.

6. Rule 482

Rule 482 applies to advertisements or other sales materials with respect to securities of an investment company registered under the Investment Company Act that is selling or proposing to sell its securities pursuant to a registration statement that has been filed under the Investment Company Act.[1116] In particular, rule 482(b) describes the information that is required to be included in an advertisement, including a cautionary statement under rule 482(b)(4) disclosing the particular risks associated with investing in a money market fund.[1117] This new collection of information would be mandatory for money market funds that rely on rule 2a–7, and to the extent that the Commission receives confidential information pursuant to these collections of information, such information would be kept confidential, subject to the provisions of applicable law.[1118]

a. Discussion of the Proposed Amendments

If implemented, the floating NAV alternative would change the investment expectations and experience of money market fund investors, rendering the current rule 482(b)(4) risk disclosures in advertisements for money market funds out of date. Accordingly, we are proposing to amend the particular wording of the rule 482(b)(4) risk disclosures in money market funds' advertisements (including requiring that they be disclosed prominently on a fund's Web site).[1119]

b. Change in Burden

The current approved collection of information for rule 482 is 301,179 annual aggregate hours. Given that the proposed amendments are one-time updates to the wording of the risk disclosures already required under current rule 482(b)(4), staff estimates that, once funds have made these one-time changes, the amendments to rule 482(b)(4) would only require money market funds to incur the same costs and hour burdens on an ongoing basis as under current rule 482(b)(4).

For each money market fund, staff estimates that internal marketing staff and in-house counsel would spend, on a one-time basis,[1120] an average of 4 hours to update and review the wording of the rule 482(b)(4) risk disclosures for each fund's printed advertising and sales materials, resulting in one-time time costs of $1,162.[1121] In addition, for

currently file in reliance on rule 17a–9 each year. *See Submission for OMB Review, Comment Request, Extension: Rule 2a–7, OMB Control No. 3235–0268,* Securities and Exchange Commission [77 FR 236 (Dec. 7, 2012)]. Because money market funds would be required to file a report in response to an event specified on Part C of Form N–CR if the fund receives any form of financial support from the fund's sponsor or other affiliated person (which support includes, but is not limited to, a rule 17a–9 security purchase), the staff estimates that the Commission will receive a greater number of reports on Form N–CR Part C than the number of notifications of rule 17a–9 security purchases that it currently receives.

[1109] Staff currently estimates that on average, one money market fund would break the buck and liquidate every six years. *See supra* note 1082.

[1110] For purposes of this estimate the staff expects that it would take approximately the same amount of time to prepare and file a report on Form N–CR, regardless under which Part of Form N–CR it is filed.

[1111] This estimate is derived in part from our current PRA estimate for Form 8–K.

[1112] This estimate is based on the following calculations: (4 hours × $379/hour for an attorney = $1,516), plus (1 hour × $192/hour for a fund senior accountant = $192), for a combined total of 5 hours and total time costs of $1,708.

[1113] This estimate is based on the following calculations: (20 reports filed per year in respect of Part B) + (40 reports filed per year in respect of Part C) + (0.167 reports filed per year in respect of Part D) = 60.167 reports filed per year. 60.167 reports filed per year × 5 hours per report = approximately 301 total annual burden hours. 60.167 reports filed per year × $1,708 in costs per report = $102,765 total annual costs.

[1114] This estimate is based on a staff review of reports on Form N–MFP filed with the Commission for the month ended February 28, 2013. For purposes of this PRA, the staff assumes that the universe of money market funds affected by the amendments to rule 482(b)(4) would be the same as the current universe for Form N–MFP.

[1115] *See supra* section IV.A.6.

[1116] *See* rule 482(a).

[1117] *See* rule 482(b)(4).

[1118] *See supra* note 994.

[1119] With respect to non-government money market funds and non-retail money market funds, *see* proposed (FNAV) rule 482(b)(4)(i). With respect to government money market funds and retail money market funds, *see* proposed (FNAV) rule 482(b)(4)(ii).

[1120] Under the floating NAV alternative, the compliance period for updating rule 482(b)(4) risk disclosures would be 2 years. The staff understands that money market funds commonly update and issue new advertising materials on a relatively periodic and frequent basis. Accordingly, given the extended compliance period proposed, the staff expects that funds should be able to amend the wording of their rule 482(b)(4) risk disclosures as part of one of their general updates of their advertising materials. Similarly, the staff believes that funds could update the corresponding risk disclosures on their Web sites when performing other periodic Web site maintenance. The staff therefore accounts only for the incremental change in burden that amending the rule 482(b)(4) risk disclosures would cause in the context of a larger update to a fund's advertising materials or Web site.

[1121] This estimate is based on the following calculation: 3 hours spent by a marketing manager to update the wording of the risk disclosures for each fund's marketing materials + 1 hour spent by an attorney reviewing the amended rule 482(b)(4) risk disclosures. Accordingly, the estimated costs are based on the following: $261/hour for a

each money market fund, staff estimates that internal information technology staff and in-house counsel would spend, on a one-time basis, an average of 1.25 hours to post and review the wording of the rule 482(b)(4) risk disclosures on a fund's Web site, resulting in one-time time costs of approximately $302.[1122] In the aggregate, staff estimates that each money market fund would spend a total of 5.25 hours and incur total time costs of approximately $1,464 on a one-time basis to comply with the amendments to rule 482(b)(4). Staff estimates that there would be no external costs incurred in complying with the proposed amendment.

Using an estimate of 586 money market funds that would be required to comply with the amendments to rule 482(b)(4),[1123] staff estimates that in the aggregate, these proposed amendments would result in a total one-time burden of approximately 3,077 burden hours[1124] at a total one-time time cost of approximately $857,904.[1125] Amortized over a three-year period, this would result in an average annual burden of approximately 1,026 burden hours at a total annual time cost of approximately $285,968 for all funds.

7. Form N–1A

We are also proposing amendments to Form N–1A in connection with our alternative proposal for money market funds to move to a floating NAV. These new collections of information would be mandatory for money market funds that rely on rule 2a–7, and to the extent that the Commission receives confidential information pursuant to these collections of information, such information would be kept confidential, subject to the provisions of applicable law.[1126]

a. Discussion of Proposed Amendments

The move to a floating NAV would be designed to change fundamentally the investment expectations and experience of money market fund investors. Because of the significance of this change, we propose to require that each money market fund, other than a government or retail fund, include a new bulleted statement disclosing the particular risks associated with investing in a floating NAV money market fund in the summary section of the statutory prospectus (and, accordingly, in any summary prospectus, if used). We also propose to include wording designed to inform investors about the primary general risks of investing in money market funds in this bulleted disclosure statement.[1127] With respect to money market funds that are not government or retail funds, we propose to remove current requirements that money market funds state that they seek to preserve the value of shareholder investments at $1.00 per share. This disclosure, which was adopted to inform investors in money market funds that a stable net asset value does not indicate that the fund will be able to maintain a stable NAV, will not be relevant once funds are required to ''float'' their net asset value. We propose to require government and retail funds, which the floating NAV proposal would exempt from the floating NAV requirement, to include a new bulleted disclosure statement in the summary section of the fund's statutory prospectus (and, accordingly, in any summary prospectus, if used) that does not discuss the risks of a floating NAV, but that would be designed to inform investors about the risks of investing in money market funds generally.

The proposed requirement that money market funds transition to a floating NAV would entail certain additional tax- and operations-related disclosure, which disclosure requirements would not necessitate rule and form amendments. However, we expect that, pursuant to current disclosure requirements, floating NAV money market funds would include disclosure in their prospectuses about the tax consequences to shareholders of buying, holding, exchanging, and selling the shares of the floating NAV fund. In addition, we expect that a floating NAV money market fund would update its prospectus and SAI disclosure regarding the purchase, redemption, and pricing of fund shares, to reflect any procedural changes resulting from the fund's use of a floating NAV.

For the reasons discussed above in section III.F.1.a, we are also proposing amendments to Form N–1A that would require all money market funds to provide SAI disclosure regarding historical instances in which the fund has received financial support from a sponsor or fund affiliate. Specifically, the proposed amendments would require each money market fund to disclose any occasion during the last ten years on which an affiliated person, promoter, or principal underwriter of the fund, or an affiliated person of such person, provided any form of financial support to the fund.

b. Change in Burden

The current approved collection of information for Form N–1A is 1,578,689 annual aggregate hours and the total annual external cost burden is $122,730,472. The respondents to this collection of information are open-end management investment companies registered with the Commission. The entities that would be affected by the proposed amendments to Form N–1A discussed above include all money market funds. However, various aspects of these amendments would only affect floating NAV money market funds, or alternatively would only affect government and retail money market funds relying on the proposed government fund exemption and retail fund exemption from the floating NAV requirement. For purposes of the PRA, staff estimates that, of the estimated 586 total money market funds,[1128] 165 funds would rely on the proposed government fund exemption,[1129] and 100 funds would rely on the proposed retail fund exemption.[1130]

The burdens associated with the proposed amendments to Form N–1A include one-time burdens as well as ongoing burdens. Commission staff estimates that each floating NAV money market fund would incur a one-time burden of 5 hours,[1131] at a time cost of

marketing manager × 3 hours = $783, plus $379/hour for an attorney × 1 hour = $379, for a combined total of $1,162.

[1122] This estimate is based on the following calculation: 1 hour spent by a webmaster to update a fund's Web site's risk disclosures, plus 15 minutes spent by an attorney reviewing the amended risk disclosures. The estimated costs are based on the following calculations: $207/hour for a webmaster × 1 hour = $207, plus $378/hour for an attorney × 0.25 hours = approximately $95, for a combined total of approximately $302.

[1123] This estimate is based on a staff review of reports on Form N–MFP filed with the Commission for the month ended February 28, 2013. For purposes of this PRA, the staff assumes that the universe of money market funds affected by the amendments to rule 482(b)(4) would be the same as the current universe for Form N–MFP.

[1124] This estimate is based on the following calculation: 5.25 burden hours per fund × 586 funds = approximately 3,077 total burden hours.

[1125] This estimate is based on the following calculation: approximately $1,464 total costs per fund × 586 funds = approximately $857,904 total costs.

[1126] *See supra* note 994.

[1127] As discussed above in section III.A.8, while money market funds are currently required to include a similar disclosure statement on their advertisements and sales materials, we propose amending this disclosure statement to emphasize that money market fund sponsors are not obligated to provide financial support, and that money market funds may not be an appropriate investment option for investors who cannot tolerate losses.

[1128] This estimate is based on a staff review of reports on Form N–MFP filed with the Commission for the month ended February 28, 2013.

[1129] This estimate is based on the number of money market funds that self-reported as Government/Agency or Treasury funds on Form N–MFP as of February 28, 2013.

[1130] *See supra* note 995.

[1131] This estimate is based on the following calculation: 1 hour to update registration statement to include bulleted disclosure statement + 3 hours

Continued

$1,480,[1132] to draft and finalize the required disclosure and amend its registration statement. In aggregate, staff estimates that floating NAV money market funds would incur a one-time burden of 1,605 hours,[1133] at a time cost of $475,080,[1134] to comply with the proposed Form N–1A disclosure requirements. In addition, Commission staff estimates that each floating NAV money market fund would incur an ongoing burden of 0.5 hours, at a time cost of $148,[1135] each year to review and update the SAI disclosure regarding historical instances in which the fund has received financial support from a sponsor or fund affiliate. In aggregate, staff estimates that floating NAV money market funds would incur an annual burden of approximately 161 hours,[1136] at a time cost of $47,656,[1137] to comply with the proposed Form N–1A disclosure requirements.

Amortizing these one-time and ongoing hour and cost burdens over three years results in an average annual increased burden of approximately 2 hours per floating NAV fund,[1138] at a time cost of $592 per fund.[1139] In aggregate, staff estimates that floating NAV money market funds would incur an average annual increased burden of 642 hours,[1140] at a time cost of $190,032,[1141] to comply with the proposed Form N–1A disclosure requirements.

Commission staff estimates that each government or retail money market fund would incur a one-time burden of 2 hours,[1142] at a time cost of $592,[1143] to draft and finalize the required disclosure and amend its registration statement. In aggregate, staff estimates that government and retail money market funds would incur a one-time burden of 530 hours,[1144] at a time cost of $156,880,[1145] to comply with the proposed Form N–1A disclosure requirements. In addition, Commission staff estimates that each government or retail money market fund would incur an ongoing burden of 0.5 hours, at a time cost of $148,[1146] each year to review and update the SAI disclosure regarding historical instances in which the fund has received financial support from a sponsor or fund affiliate. In aggregate, staff estimates that government and retail money market funds would incur an annual burden of approximately 133 hours,[1147] at a time cost of $39,368,[1148] to comply with the proposed Form N–1A disclosure requirements.

Amortizing these one-time and ongoing hour and cost burdens over three years results in an average annual increased burden of 1 hour per government or retail fund,[1149] at a time cost of $296.[1150] In aggregate, staff estimates that government and retail fund money market funds would incur an average annual increased burden of 265 hours,[1151] at a time cost of $78,440,[1152] to comply with the proposed Form N–1A disclosure requirements.

In total, the staff estimates that all money market funds (floating NAV funds, as well as government and retail funds that rely on the proposed government and retail exemptions) would incur an annual increased burden of 907 hours,[1153] at a time cost of $268,472,[1154] to comply with the proposed Form N–1A disclosure requirements. Additionally, the staff estimates that there would be one-time aggregate external costs (in the form of printing costs) of $3,134,588 associated with the proposed Form N–1A disclosure requirements; amortizing these external costs over three years results in annual aggregate external costs of $1,044,863.[1155]

---

to update registration statement to include tax- and operations-related disclosure about floating NAV + 1 hour to update registration statement to include disclosure about financial support received by the fund = 5 hours.

[1132] This estimate is based on the following calculations: (1 hour (to update registration statement to include bulleted disclosure statement) × $296 (blended rate for a compliance attorney and a senior programmer) = $296) + (3 hours (to update registration statement to include tax- and operations-related disclosure about floating NAV) × $296 (blended rate for a compliance attorney and a senior programmer) = $888) + (1 hour (to update registration statement to include disclosure about financial support received by the fund) × $296 (blended rate for a compliance attorney and a senior programmer) = $296 = $1,480.

[1133] This estimate is based on the following calculations: 5 hours × 321 funds (586 total money market funds—165 funds that would rely on the proposed government fund exemption—100 funds that would rely on the proposed retail fund exemption) = 1,605 hours.

[1134] This estimate is based on the following calculation: 1,605 hours × $296 (blended rate for a compliance attorney and a senior programmer) = $475,080.

[1135] This estimate is based on the following calculation: 0.5 hours × $296 (blended rate for a compliance attorney and a senior programmer) = $148.

[1136] This estimate is based on the following calculation: 0.5 hours × 321 funds (586 total money market funds—165 funds that would rely on the proposed government fund exemption—100 funds that would rely on the proposed retail fund exemption) = approximately 161 hours.

[1137] This estimate is based on the following calculation: 161 hours × $296 (blended rate for a compliance attorney and a senior programmer) = $47,656.

[1138] This estimate is based on the following calculation: 5 burden hours (year 1) + 0.5 burden hours (year 2) + 0.5 burden hours (year 3) ÷ 3 = 2 hours.

[1139] This estimate is based on the following calculation: $1,480 (year 1 monetized burden hours) + $148 (year 2 monetized burden hours) + $148 (year 3 monetized burden hours) ÷ 3 = $592.

[1140] This estimate is based on the following calculation: 2 hours × 321 funds (586 total money market funds—165 funds that would rely on the proposed government fund exemption—100 funds that would rely on the proposed retail fund exemption) = 642 hours.

[1141] This estimate is based on the following calculation: 642 hours × $296 (blended rate for a compliance attorney and a senior programmer) = $190,032.

[1142] This estimate is based on the following calculation: 1 hour to update registration statement to include bulleted disclosure statement + 1 hour to update registration statement to include disclosure about financial support received by the fund = 2 hours.

[1143] This estimate is based on the following calculation: (1 hour (to update registration statement to include bulleted disclosure statement) × $296 (blended rate for a compliance attorney and a senior programmer) = $296) + (1 hour (to update registration statement to include disclosure about financial support received by the fund) × $296 (blended rate for a compliance attorney and a senior programmer) = $296) = $592.

[1144] This estimate is based on the following calculation: 2 hours × 265 funds (165 funds that would rely on the proposed government fund exemption + 100 funds that would rely on the proposed retail fund exemption) = 530 hours.

[1145] This estimate is based on the following calculation: 530 hours × $296 (blended rate for a compliance attorney and a senior programmer) = $156,880.

[1146] This estimate is based on the following calculation: 0.5 hours × $296 (blended rate for a compliance attorney and a senior programmer) = $148.

[1147] This estimate is based on the following calculation: 0.5 hours × 265 funds (165 funds that would rely on the proposed government fund exemption + 100 funds that would rely on the proposed retail fund exemption) = approximately 133 hours.

[1148] This estimate is based on the following calculation: 133 hours × $296 (blended rate for a compliance attorney and a senior programmer) = $39,368.

[1149] This estimate is based on the following calculation: 2 burden hours (year 1) + 0.5 burden hours (year 2) + 0.5 burden hours (year 3) ÷ 3 = 1 hour.

[1150] This estimate is based on the following calculation: $592 (year 1 monetized burden hours) + $148 (year 2 monetized burden hours) + $148 (year 3 monetized burden hours) ÷ 3 = $296.

[1151] This estimate is based on the following calculation: 1 hour × 265 funds (165 funds that would rely on the proposed government fund exemption + 100 funds that would rely on the proposed retail fund exemption) = 265 hours.

[1152] This estimate is based on the following calculation: 265 hours × $296 (blended rate for a compliance attorney and a senior programmer) = $78,440.

[1153] This estimate is based on the following calculation: 642 hours + 265 hours = 907 hours. *See supra* notes 1140 and 1151.

[1154] This estimate is based on the following calculation: $190,032 + $78,440 = $268,472. *See supra* notes 1141 and 1152.

[1155] We expect that a fund that must include disclosure regarding historical instances in which the fund has received financial support from a sponsor or fund affiliate would need to add 1–4 pages of new disclosure to its registration statement. Adding this new disclosure would therefore increase the number of pages in, and change the printing costs of, the fund's registration statement.

Commission staff calculates the external costs associated with the proposed Form N–1A disclosure requirements as follows: 2.5 pages (mid-

8. Advisers Act Rule 204(b)–1 and Form PF

Advisers Act rule 204(b)–1 requires SEC-registered private fund advisers that have at least $150 million in private fund assets under management to report certain information regarding the private funds they advise on Form PF. The rule implements sections 204 and 211 of the Advisers Act, as amended by the Dodd-Frank Act, which direct the Commission (and the CFTC) to supply FSOC with information for use in monitoring systemic risk by establishing reporting requirements for private fund advisers. Form PF divides respondents into groups based on their size and the types of private funds they manage, with some groups of advisers required to file more information than others or more frequently than others. Large liquidity fund advisers—the only group of advisers that would be affected by today's proposed amendments to Form PF—must provide information concerning their liquidity funds on Form PF each quarter. Form PF contains a collection of information under the PRA.[1156] This new collection of information would be mandatory for large liquidity fund advisers, and would be kept confidential to the extent discussed above in section III.I. Based on data filed on Form PF and Form ADV, Commission staff estimates that, as of February 28, 2013, there were 25 large liquidity fund advisers subject to this quarterly filing requirement that collectively advised 43 liquidity funds.

a. Discussion of Proposed Amendments

Under the proposed amendments to Form PF, for each liquidity fund it manages, a large liquidity fund adviser would be required to provide, quarterly and with respect to each portfolio security, the following additional information for each month of the reporting period:

- The name of the issuer;
- The title of the issue;
- The CUSIP number;
- The legal entity identifier, or LEI, if available;
- At least one of the following other identifiers, in addition to the CUSIP and LEI, if available: ISIN, CIK, or any other unique identifier;
- The category of investment (*e.g.,* Treasury debt, U.S. government agency debt, asset-backed commercial paper, certificate of deposit, repurchase agreement[1157]);
- If the rating assigned by a credit rating agency played a substantial role in the liquidity fund's (or its adviser's) evaluation of the quality, maturity or liquidity of the security, the name of each credit rating agency and the rating each credit rating agency assigned to the security;
- The maturity date used to calculate weighted average maturity;
- The maturity date used to calculate weighted average life;
- The final legal maturity date;
- Whether the instrument is subject to a demand feature, guarantee, or other enhancements, and information about any of these features and their providers;
- For each security, reported separately for each lot purchased, the total principal amount; the purchase date(s); the yield at purchase and as of the end of each month during the reporting period for floating or variable rate securities; and the purchase price as a percentage of par;
- The value of the fund's position in the security and, if the fund uses the amortized cost method of valuation, the amortized cost value, in both cases with and without any sponsor support;
- The percentage of the liquidity fund's assets invested in the security;
- Whether the security is categorized as a level 1, 2, or 3 asset or liability on Form PF;[1158]
- Whether the security is an illiquid security, a daily liquid asset, and/or a weekly liquid asset, as defined in rule 2a–7; and
- Any explanatory notes.[1159]

Our proposed amendments to Form PF are designed, as discussed in more detail in section III.I above, to assist FSOC in its monitoring and assessment of systemic risk; to provide information for FSOC's use in determining whether and how to deploy its regulatory tools; and to collect data for use in our own regulatory program. The additional information we are proposing to require large liquidity fund advisers to provide with respect to the liquidity funds they advise is virtually the same information that money market funds must file on Form N–MFP as we propose to amend it, and should be familiar to large liquidity fund advisers because, as of February 28, 2013, virtually all of the 25 large liquidity funds advisers already manage a money market fund or have a related person that manages a money market fund. Because advisers would be required to report this information about their portfolio holdings, the proposed amendments to Form PF also would remove current Questions 56 and 57 on Form PF, which generally require large liquidity fund advisers to provide information about their liquidity funds' portfolio holdings broken out by asset class (rather than security by security). We also proposing to require large liquidity fund advisers to provide information about any securities sold by their liquidity funds during the reporting period, including sale and purchase prices. Finally, the amendments would require large liquidity fund advisers to identify any money market fund advised by the adviser or its related persons that pursues substantially the same investment objective and strategy and invests side by side in substantially the same positions as a liquidity fund the adviser reports on Form PF.

b. Current Burden

The current approved collection of information for Form PF is 258,000 annual aggregate hours and $25,684,000 in aggregate external costs. In estimating these total approved burdens, Commission staff estimated that the amortized average annual burden of Form PF for large liquidity fund advisers in particular would be 290 hours per large liquidity fund adviser for each of the first three years, resulting in an aggregate amortized annual burden of 23,200 hours for large liquidity fund advisers for each of the first three years.[1160] Staff estimated that

point of 1 page and 4 pages) × $0.045 per page × 27,863,000 money market fund registration statements printed annually = $3,134,588 one-time aggregate external costs. Amortizing these external costs over three years results in aggregate annual external costs of $1,044,863. Our estimate of potential printing costs ($0.045 per page: $0.035 for ink + $0.010 for paper) is based on data provided by Lexecon Inc. in response to Investment Company Act Release No. 27182 (Dec. 8, 2005) [70 FR 74598 (Dec. 15, 2005)]. *See* Lexecon Inc. Letter (Feb. 13, 2006), *available at http://www.sec.gov/rules/proposed/s71005/dbgross9453.pdf.* For purposes of this analysis, our best estimate of the number of money market fund registration statements printed annually is based on 27,863,000 money market fund shareholder accounts in 2012. *See* Investment Company Institute, *2013 Investment Company Fact Book,* at 178, *available at http://www.ici.org/pdf/2013_factbook.pdf.*

[1156] For purposes of the PRA analysis, the current burden associated with the requirements of rule 204(b)–1 is included in the collection of information requirements of Form PF.

[1157] For repurchase agreements we are also proposing to require large liquidity fund advisers to provide additional information regarding the underlying collateral and whether the repurchase agreement is ''open'' (*i.e.,* whether the repurchase agreement has no specified end date and, by its terms, will be extended or ''rolled'' each business day (or at another specified period) unless the investor chooses to terminate it).

[1158] *See* Question 14 of Form PF. *See also infra* notes 758–761 and accompanying and following text.

[1159] We also propose to define the following terms in Form PF: conditional demand feature; credit rating agency; demand feature; guarantee; guarantor; and illiquid security. *See* proposed Form PF: Glossary of Terms.

[1160] *See* Form PF Adopting Release, *supra* note 799, at n.411 (''290 burden hours on average per

Continued

the external cost burden would range from $0 to $50,000 per large private fund adviser, which resulted in aggregate estimated external costs attributable to large liquidity fund advisers of $4,000,000. The external cost estimates also included estimates for filing fees, which were are $150 per annual filing and $150 per quarterly filing, resulting in annual filings costs for large liquidity fund advisers of $48,000.[1161]

c. Change in Burden

Our staff estimates that the paperwork burdens associated with Form N–MFP (as we propose to amend it) are representative of the burdens that large liquidity fund advisers could incur as a result of our proposed amendments to Form PF because advisers would be required to file on Form PF virtually the same information money market funds would file on Form N–MFP as we propose to amend it and because, as discussed above, virtually all of the 25 large liquidity funds advisers already manage a money market fund or have a related person that manages a money market fund. Therefore, we believe that large liquidity fund advisers—when required to compile and report for their liquidity funds generally the same information virtually all of them already report for their money market funds—likely will use the same (or comparable) staff and/or external service providers to provide portfolio holdings information on Form N–MFP and Form PF.

Our staff accordingly estimates that our proposed amendments to Form PF would result in paperwork burden hours and external costs determined as follows. First, as discussed in the PRA analysis for our amendments to Form N–MFP, our staff estimates that the average annual amortized burdens per money market fund imposed by Form N–MFP as we propose to amend it are 145 hours [1162] and $8,187 in external costs.[1163] Our staff estimates that large liquidity fund advisers would incur these burdens for each of their liquidity funds, for the reasons discussed above, and would incur a time cost of $36,730 associated with the 145 estimated burden hours.[1164] Because our staff estimates that there were 25 large liquidity fund advisers that collectively advised 43 liquidity funds as of February 28, 2013 as discussed above, this would result in increased annual burdens per large liquidity fund adviser of 290 burden hours, at a total time cost of $73,460, and $16,374 in external costs.[1165] This would result in increased aggregate burden hours across all large liquidity fund advisers of 7,250 burden hours,[1166] at a time cost of $1,836,500,[1167] and $409,350 in external costs.[1168] Finally, the aggregate paperwork burden for Form PF under our proposed amendments therefore would be 249,300 burden hours [1169] and $23,310,350 in external costs.[1170]

*B. Alternative 2: Standby Liquidity Fees and Gates*

As discussed above, we are proposing an alternative to our floating NAV proposal. Under this alternative, we propose to require that, in the event that a money market fund's weekly liquid assets fell below 15% of its total assets, the money market fund would be required to institute a liquidity fee and permitted to impose a redemption gate.

1. Rule 2a–7

a. Board Determinations

Under the proposed liquidity fees and gates proposal, if a money market fund's weekly liquid assets fall below 15% of total assets, the fund's board may be required to make and document a number of determinations, when in the best interest of the fund, regarding the imposition of liquidity fees and gates, including (i) whether to impose the liquidity fee, and if so, what the amount of the liquidity fee should be (not to exceed 2%); (ii) whether to impose a redemption gate; (iii) when to remove a liquidity fee put in place (subject to other rule requirements); and (iv) when

year × 80 large hedge fund advisers = 23,200 hours.'').

[1161] This estimate is based on the following calculation: ($150 quarterly filing fee × 4 quarters) × 80 large liquidity fund advisers) = $48,000.

[1162] As discussed in the PRA analysis for Form N–MFP, our staff estimates that Form N–MFP, as we propose to amend it, would result in an aggregate collection of information burden of 85,257 hours. *See supra* note 1102 and accompanying text. Based on the staff's estimated 586 money market fund respondents, this results in a per fund annual burden of approximately 145 hours.

[1163] As discussed in the PRA analysis for Form N–MFP, our staff estimates that Form N–MFP, as we propose to amend it, would result in an aggregate external cost burden of $4,798,160. *See supra* note 1103. Based on the staff's estimated 586 money market fund respondents, this results in a per fund annual external cost burden of approximately $8,187.

[1164] Our staff estimates, as discussed above, that large liquidity fund advisers are likely to use the same (or comparable) staff and/or external service providers to provide portfolio holdings information on Form N–MFP and Form PF. Accordingly, our staff estimates that large liquidity fund advisers would use the same professionals, and in comparable proportions (conservatively based on the professionals used for the Form N–MFP initial filings), for purposes of the staff's estimate of time costs associated with our proposed amendments to Form PF. *See supra* note 1092. This results in the following estimated time cost for the staff's estimated 145 per liquidity fund hour burdens: (85 hours × $243 blended average hourly rate for a financial reporting manager ($294 per hour) and fund senior accountant ($192 per hour) = $20,655 per fund) + (10 hours × $155 per hour for an intermediate accountant = $1,550 per fund) + (17 hours × $314 per hour for a senior database administrator = $5,338 per fund) + (10 hours × $300 for a senior portfolio manager = $3,000 per fund) + (23 hours × $269 per hour for a compliance manager = $6,187 per fund) = $36,730.

[1165] This estimate assumes for purposes of the PRA that each large liquidity fund adviser advises two large liquidity funds (43 total liquidity funds divided by 25 large liquidity fund advisers). Each large liquidity fund adviser therefore would incur the following burdens: 145 estimated burden hours per fund × 2 large liquidity funds = 290 burden hours per large liquidity fund adviser; $36,730 estimated time cost per fund × 2 large liquidity funds = $73,460 time cost per large liquidity fund adviser; and $8,187 estimated external costs per fund × 2 large liquidity funds = $16,374 external costs per large liquidity fund adviser.

[1166] This estimate is based on the following calculation: 290 estimated additional burden hours per large liquidity fund adviser × 25 large liquidity fund advisers = 7,250.

[1167] This estimate is based on the following calculation: $73,460 estimated time cost per large liquidity fund adviser × 25 large liquidity fund advisers = $1,836,500.

[1168] This estimate is based on the following calculation: $16,374 estimated external costs per large liquidity fund adviser × 25 large liquidity fund advisers = $409,350.

[1169] Form PF's current approved burden includes 23,200 aggregate burden hours associated with large liquidity fund advisers, based on 80 large liquidity fund advisers and an estimated 290 burden hours per large liquidity fund adviser. Our amendments to Form PF would increase the estimated 290 burden hours per large liquidity fund adviser by 290 hours, as discussed above, resulting in a total of 580 burden hours per large liquidity fund adviser. Multiplying 580 by the current estimated number of 25 large liquidity fund advisers results in 14,500 burden hours attributable to large liquidity fund advisers, a 8,700 reduction from the approved burden hours attributable to large liquidity fund advisers. This therefore results in 249,300 total burden hours for all of Form PF (current approved 258,000 burden hours—8,700 reduction = 249,300).

[1170] Form PF's current approved burden includes $25,684,000 in external costs, which includes $4,000,000 attributable to large liquidity fund advisers for certain costs ($50,000 per adviser), and $48,000 (or $600 per adviser) for filing fees, in both cases assuming 80 large liquidity fund adviser respondents. Form PF's approved burden therefore includes a total of $4,048,000 in external costs attributable to large liquidity fund advisers. Reducing these estimates to reflect our staff's current estimate of 25 large liquidity fund adviser respondents results in costs of $1,250,000 (25 large liquidity fund advisers × $50,000 per adviser) and $15,000 (25 large liquidity fund advisers × $600), respectively, for an aggregate cost of $1,265,000. These costs, plus the additional external costs associated with our proposed amendments to Form PF ($409,350 as estimated above), result in total external costs attributable to large liquidity fund advisers of $1,674,350, a reduction of $2,373,650 from the currently approved external costs attributable to large liquidity fund advisers. This therefore results in total external cost for all of Form PF of $23,310,350 (current approved external cost burden of $25,684,000 − $2,373,650 reduction = $23,310,350).

to lift a redemption gate put in place (subject to other rule requirements).[1171] This requirement is a collection of information under the PRA, and is designed to ensure that a fund that imposes a liquidity fee or gate does so only when, as determined by the fund's board, it is in the best interest of the fund to do so. This new collection of information would be mandatory for money market funds that rely on rule 2a–7, and to the extent that the Commission receives confidential information pursuant to these collections of information, such information would be kept confidential, subject to the provisions of applicable law.[1172]

As discussed above, staff analysis of Form N–MFP data shows that, between March 2011 and October 2012, four prime money market funds had weekly liquid assets below 15% of total assets, the trigger for board determinations regarding the imposition of liquidity fees and gates. Commission staff estimates that the four money market funds we estimate would satisfy the triggering event would spend, on an annual basis, (i) four hours of a fund attorney's time to prepare materials for the board's determinations, (ii) two hours for the board to review those materials and make the required determinations, and (iii) one hour of a fund attorney's time per year, on average, to prepare the written records of such determinations.[1173] Therefore, staff estimates that the average annual burden to prepare materials and written records for a board's required determinations would be approximately seven hours per fund [1174] at a time cost of approximately $9,895 per fund.[1175] Therefore, staff estimates the annual burden would be approximately 28 burden hours [1176] and $39,580 in total time costs for all money market funds.[1177] Amortized over a three-year period, this would result in an average annual burden of approximately 9 hours and a time cost of $13,193 for all funds.[1178] There would be no external costs associated with this collection of information.

b. Retail Exemption

As discussed above in section III.B.5, we are not proposing a retail money market fund exemption from our liquidity fees and gates proposal. Accordingly, there would be no collection of information burden related to the retail exemption.

c. Asset-Backed Securities

As outlined above, we are proposing certain amendments relating to ABS securities that would be adopted if the first alternative (requiring money market funds to float their NAV per share) is adopted.[1179] Under the proposal, the board of directors would be required to adopt written procedures requiring periodic evaluation of its determination that the fund is not relying on an ABS sponsor's financial strength or its ability or willingness to provide liquidity. We are also proposing that these amendments would be adopted if the liquidity fees and gates alternative is adopted. Therefore, staff estimates that, under the liquidity fees and gates alternative, the one-time burden to adopt written procedures regarding the periodic evaluation of determinations made by the fund as to ABS not subject to guarantees would be approximately 1,647 hours and $1.2 million in total time costs for all money market funds. Amortized over a three-year period, this would result in an average annual burden of approximately 549 hours and time costs of $400,000 for all funds. In addition, staff estimates the annual burden to prepare materials and written records for a board's required review of new and existing determinations would be approximately 732 burden hours and $940,071 in total time costs for all money market funds. Amortized over a three-year period, this would result in an average annual burden of approximately 244 hours and time costs of $313,357 for all funds. There would be no external costs associated with this collection of information.

d. Notice to Commission

As outlined above, we propose to eliminate the requirements that money market funds provide electronic notice of any event of default or insolvency of a portfolio security and any purchase by a fund of a portfolio security by an affiliate in reliance on rule 17a–9.[1180] We are also proposing that these amendments would be adopted if the second alternative requiring liquidity fees and gates is adopted. Therefore, staff estimates that the proposed amendment to eliminate electronic notice of any event of default or insolvency would reduce the current collection of information by approximately 10 hours annually, at a total time cost savings of $3,790. Staff further estimates that the proposed amendment to eliminate electronic notification of a purchase of a portfolio security in reliance on rule 17a–9 would reduce the current collection of information by approximately 25 hours annually, at a total time cost savings of $9,475.[1181] There would be no external cost savings associated with this collection of information.

e. Stress Testing

As outlined above, we are proposing amendments to the stress testing provision of rule 2a–7 to enhance the hypothetical events for which a fund (or its adviser) is required to test. The amendments and enhancements we are proposing to the stress testing requirements would largely be identical under either reform alternative we might adopt, except that for floating NAV money market funds we would remove the standard to test against preserving a stable share price if we were to adopt the floating NAV alternative, as discussed above in more detail. Therefore, staff estimates that the aggregate one-time burden for all money market funds to implement the proposed amendments to stress testing would be the same as under our floating NAV alternative (8,464 hours at a total time cost of $3.9 million). Amortized over a three-year period, this would result in an average annual burden of 2,821 burden hours and $1.3 million total time cost for all funds.[1182] There would be no external costs associated with this collection of information.

f. Web site Disclosure

We are proposing four amendments to the information money market funds are required to disclose on their Web sites. These amendments would promote transparency of money market funds' risks and risk management by:

• Harmonizing the specific portfolio holdings information that rule 2a–7

[1171] *See* Proposed (Fees and Gates) rule 2a–7(c)(2)(i), (ii).

[1172] *See supra* note 994.

[1173] This estimate includes preparing and evaluating materials relevant to the determinations required in imposing (and removing) either or both liquidity fees and redemption gates. *See supra* note 1171.

[1174] This estimate is based on the following calculation: 4 hours to adopt + 2 hours for board review + 1 hour for record preparation = 7 hours per year.

[1175] This estimate is based on the following calculation: [5 hours × $379 per hour for an attorney = $1,895] + [2 hours × $4,000 per hour for a board of 8 directors = $8,000] = $9,895.

[1176] This estimate is based on the following calculation: 7 burden hours per money market fund × 4 funds = 28 total burden hours.

[1177] This estimate is based on the following calculation: 4 money market funds × $9,895 in total costs per fund complex = $39,580.

[1178] This estimate is based on the following calculation: 28 burden hours ÷ 3 = 9 average annual burden hours; $39,580 burden costs ÷ 3 = $13,193 average annual burden cost.

[1179] *See* Section IV.A.1.b above.

[1180] *See supra* section IV.A.1.c.

[1181] *Id.*

[1182] *See supra* section IV.A.1.e note 1032 and accompanying text.

currently requires funds to disclose on the fund's Web site with the corresponding portfolio holdings information proposed to be reported on Form N–MFP; [1183]

- Requiring that a fund disclose on its Web site a schedule, chart, graph, or other depiction showing the percentage of the fund's total assets that are invested in daily and weekly liquid assets, as well as the fund's net inflows or outflows, as of the end of each business day during the preceding six months (which depiction must be updated each business day as of the end of the preceding business day); [1184]
- Requiring that a fund disclose on its Web site a schedule, chart, graph, or other depiction showing the fund's daily current NAV per share, as of the end of each business day during the preceding six months (which depiction must be updated each business day as of the end of the preceding business day); [1185] and
- Requiring a fund to disclose on its Web site substantially the same information that the fund is required to report to the Commission on Form N–CR regarding the provision of financial support to the fund, the imposition and removal of liquidity fees, and the suspension and resumption of fund redemptions.[1186]

This new collection of information would be mandatory for money market funds that rely on rule 2a–7, and to the extent that the Commission receives confidential information pursuant to these collections of information, such information would be kept confidential, subject to the provisions of applicable law.[1187]

i. Disclosure of Portfolio Holdings Information

As outlined above, we are proposing amendments to the portfolio holdings information that rule 2a–7 currently requires money market funds to disclose on the fund's Web site to harmonize this information with the corresponding portfolio holdings information proposed to be reported on Form N–MFP. We are proposing substantially similar amendments under both the floating NAV alternative and the liquidity fees and gates alternative. Therefore, the burdens associated with the proposed amendments would be the same as those discussed in section IV.A.1.f.i above (7,032 aggregate hours per year, at a total aggregate time cost of $1,455,624). There would be no external costs associated with this collection of information.

ii. Disclosure of Daily Liquid Assets and Weekly Liquid Assets

We are proposing to require money market funds to disclose on the fund's Web site a schedule, chart, graph, or other depiction showing the percentage of the fund's total assets that are invested in daily and weekly liquid assets, as well as the fund's net inflows or outflows, and to update this depiction each business day, as discussed above. We are proposing identical requirements under both the floating NAV alternative and the liquidity fees and gates alternative. Therefore, the burdens associated with the proposed requirements would be the same as those discussed in Section IV.A.1.f.ii above (26,175 aggregate hours per year, at a total aggregate time cost of $7,523,849). There would be no external costs associated with this collection of information.

iii. Disclosure of Daily Current NAV

We are proposing to require a money market fund to disclose on the fund's Web site a schedule, chart, graph, or other depiction showing the fund's daily current NAV as of the end of the previous business day, and to update this depiction each business day, as discussed above. We are proposing substantially similar requirements under both the floating NAV alternative and the liquidity fees and gates alternative. Therefore, the burdens associated with the proposed requirements would be the same as those discussed in Section IV.A.1.f.iii above (26,175 aggregate hours per year, at a total aggregate time cost of $7,523,849). There would be no external costs associated with this collection of information.

iv. Disclosure Regarding Financial Support Received by the Fund, the Imposition and Removal of Liquidity Fees, and the Suspension and Resumption of Fund Redemptions

As outlined above, we are proposing to require money market fund to disclose on the fund's Web site substantially the same information that the fund is required to report to the Commission on Form N–CR regarding the provision of financial support to the fund. We are proposing identical requirements under both the floating NAV alternative and the liquidity fees and gates alternative. Therefore, the burdens associated with these proposed requirements would be the same as those discussed in Section IV.A.1.f.iv above (40 aggregate hours per year, at a total aggregate time cost of $8,280). There would be no external costs associated with this collection of information.

In connection with the fees and gates alternative, we are also proposing to require money market funds to disclose on the fund's Web site substantially the same information that the fund is required to report to the Commission on Form N–CR regarding the imposition and removal of liquidity fees, and the suspension and resumption of fund redemptions. Commission staff estimates that the Commission would receive, in aggregate, an average of 8 reports per year filed in response to events specified on Part E (''Imposition of liquidity fee''), Part F (''Suspension of Fund redemptions''), and Part G (''Removal of liquidity fees and/or resumption of Fund redemptions'') of Form N–CR.[1188] Because the required Web site disclosure overlaps with the information that a fund must disclose on Form N–CR when the fund imposes or removes liquidity fees, or suspends and resumes fund redemptions, we anticipate that the burdens a fund would incur to draft and finalize the disclosure that would appear on its Web site would largely be incurred when the fund files Form N–CR.[1189] Commission staff estimates that a fund would incur an additional burden of 1 hour, at a time cost of $207,[1190] each time that it updates its Web site to include the new disclosure. Accordingly, Commission staff estimates that the requirement to disclose information about the imposition and removal of liquidity

[1183] Proposed (Fees & Gates) rule 2a–7(h)(10)(i).

[1184] Proposed (Fees & Gates) rule 2a–7(h)(10)(ii).

[1185] Proposed (Fees & Gates) rule 2a–7(h)(10)(iii).

[1186] Proposed (FNAV) rule 2a–7(h)(10)(iv).

[1187] *See supra* note 994.

[1188] This estimate is based on staff's analysis of Form N–MFP data that shows that, between March 2011 and October 2012, 4 prime money market funds had weekly liquid assets below 15% at the time of filing. We assume that the Commission would receive 4 reports on Form N–CR filed in response to events specified on Part E (which requires filing when the 15% threshold is crossed, regardless of whether the fund imposes the default liquidity fee) and Part F (which requires filing when the 15% threshold is crossed and the fund imposes a redemption gate). Assuming that each time a fund crosses the 15% threshold, it would impose a fee or gate, and that it would eventually remove this fee or gate, we assume that the Commission would additionally receive 4 reports on Form N–CR filed in response to events specified on Part G (which requires filing when a fund that has imposed a liquidity fee and/or suspended the fund's redemptions determines to remove such fee and/or resume fund redemptions).

However, this is a conservative estimate, because we expect that funds would be less likely to cross the 15% threshold if we adopt our proposal, since we expect that the funds would increase their risk management around their level of weekly liquid assets in response to the fee and gate requirements.

[1189] *See infra* section IV.B.4.

[1190] This estimate is based on the following calculation: 1 hour per Web site update × $207 per hour for a webmaster = $207.

fees, and the suspension and resumption of fund redemptions, on the fund's Web site would result in a total aggregate burden of 8 hours per year,[1191] at a total aggregate time cost of $1,656.[1192] There would be no external costs associated with this collection of information.

v. Change in Burden

The aggregate additional annual burden associated with the proposed Web site disclosure requirements discussed above is 59,430 hours [1193] at a time cost of $16,513,258.[1194] Amortized over a three-year period, this would result in an average annual burden of 19,810 burden hours and $5,504,419 total cost for all funds.[1195] There would be no external costs associated with this collection of information.

g. Total Burden for Rule 2a–7

The currently approved burden for rule 2a–7 is 517,228 hours. The net aggregate additional burden hours associated with the proposed amendments to rule 2a–7 would increase the burden estimate to 540,626 hours annually for all funds.[1196]

2. Rule 22e–3

As outlined above, rule 22e–3 under the Investment Company Act exempts money market funds from section 22(e) of the Act to permit them to suspend redemptions and postpone payment of redemption proceeds in order to facilitate an orderly liquidation of the fund, provided that certain conditions are met. To provide shareholders with protections comparable to those currently provided by the rule while also updating the rule to make it consistent with our proposed amendments to rule 2a–7, we are proposing to amend rule 22e–3 under our fees and gates proposal to permit a money market fund to invoke the exemption in rule 22e–3 if the fund, at the end of a business day, has invested less than 15% of its total assets in weekly liquid assets.[1197] As under the current rule, a money market fund would continue to be able to invoke the exemption in rule 22e–3 if it had broken the buck or was about to break the buck.[1198]

The proposed amendments to rule 22e–3 under our fees and gates proposal, like the amendments we propose to rule 22e–3 under our floating NAV proposal, are designed to permit a money market fund to suspend redemptions when the fund is under significant stress, as the funds may do today under rule 22e–2. As with our proposed amendments to rule 22e–3 under our floating NAV proposal, we do not expect that money market funds would invoke the exemption provided by rule 22e–3 more frequently under our fees and gates proposal than they do today. Although we propose to change the circumstances under which a money market fund may invoke the exemption provided by rule 22e–3, the rule as we propose to amend it still would permit a money market fund to invoke the exemption only when the fund is under significant stress, and our staff estimates that a money market fund is likely to experience that level of stress and choose to suspend redemptions in reliance on rule 22e–3 with the same frequency that funds today may do so. Therefore, we are not revising rule 22e–3's current approved annual aggregate collection of information, which would remain approximately 30 minutes. There would be no change in the external cost burden associated with this collection of information.

3. Rule 30b1–7 and Form N–MFP

As outlined above, we are also proposing that these amendments would be adopted if the second alternative, requiring money market funds whose liquidity levels fell below a specified threshold to consider imposing a liquidity fee and permit the funds to suspend redemptions temporarily, were adopted. Therefore, as discussed above under the floating NAV proposal, Commission staff estimates that, under our fees and gates proposal, our proposed amendments to Form N–MFP would result in all money market funds, incurring, in aggregate, 40,043 hours at a total time cost of $10.4 million plus $373,680 in external costs for all funds.[1199] Staff estimates that our proposed amendments to Form N–MFP would result in a total aggregate annual collection of information burden of 85,257 hours and $4,798,160 in external costs.[1200]

4. Rule 30b1–8 and Form N–CR

As discussed above, we are proposing to adopt new Form N–CR under the floating NAV alternative, which would require disclosure, by means of a current report filed with the Commission, of certain specific reportable events. Similarly, we are also proposing to adopt new Form N–CR if the liquidity fees and gates alternative is adopted. Albeit with some variations, under both alternatives the information reported on Form N–CR would include instances of portfolio security default, sponsor support of funds, and certain significant deviations in net asset value.[1201] In addition, under the liquidity fees and gates alternative, we would also require that money market funds file a report on Form N–CR in response to events specified on Part E (''Imposition of Liquidity Fee''), Part F (''Suspension of Fund Redemptions'') and Part G (''Removal of Liquidity Fees and/or Resumption of Fund Redemptions'').

Under the liquidity fees and gates alternative, the staff estimates that on average the Commission would receive the same number of reports filed per year in response to the events specified on Parts B, C, and D as under the floating NAV alternative. In addition, the staff estimates that on average the Commission would an additional 8 reports per year filed in response to events specified on Parts E, F, and G of Form N–CR.[1202]

[1191] This estimate is based on the following calculation: 1 hour per Web site update × 8 Web site updates made by money market funds = 8 hours.

[1192] This estimate is based on the following calculation: 8 hours per year × $207 per hour for a webmaster = $1,656.

[1193] This estimate is based on the following calculation: 7,032 hours (annual aggregate burden for disclosure of portfolio holdings information) + 26,175 (annual aggregate burden for disclosure of daily liquid assets and weekly liquid assets) + 26,175 (annual aggregate burden for disclosure of daily market-based NAV) + 40 hours (annual aggregate burden for disclosure of financial support provided to money market funds) + 8 hours (annual aggregate burden for disclosure of the imposition and removal of liquidity fees, and the suspension and resumption of fund redemptions) = 59,430 hours.

[1194] This estimate is based on the following calculation: $1,455,624 (annual aggregate costs associated with disclosure of portfolio holdings information) + $7,523,849 (annual aggregate costs associated with disclosure of daily liquid assets and weekly liquid assets) + $7,523,849 (annual aggregate costs associated with disclosure of daily market-based NAV) + $8,280 (annual aggregate costs associated with disclosure of financial support provided to money market funds) + $1,656 (annual aggregate costs associated with disclosure of the imposition and removal of liquidity fees, and the suspension and resumption of fund redemptions) = $16,513,258.

[1195] This estimate is based on the following calculation: 59,430 hours ÷ 3 = 19,810 burden hours; $16,513,258 ÷ 3 = $5,504,419 burden cost.

[1196] This estimate is based on the following calculation: 517,228 hours (currently approved burden) + 9 hours (board determinations) + (549 hours + 244 hours) (ABS determination & recordkeeping)—(10 hours + 25 hours) (notice to the Commission) + 2,821 hours (stress testing) + 19,810 hours (Web site disclosure) = 540,626 hours.

[1197] Proposed (Fees & Gates) rule 2a–7(a)(1)(ii).

[1198] Proposed (Fees & Gates) rule 2a–7(a)(1)(i).

[1199] *See supra* note 1101 and accompanying text.

[1200] *See supra* notes 1102 and 1103 and accompanying text.

[1201] *See* proposed (FNAV) Form N–CR Parts A–D; proposed (Fees & Gates) Form N–CR Part A–D; *see also* section III.G.1.

[1202] This estimate is based on staff's analysis of Form N–MFP data that shows that, between March

Continued

As discussed above, the staff estimates that a fund would spend on average approximately 5 hours [1203] of an in-house attorney's and an accountant's time to prepare, review and submit Form N–CR, at a total time cost of $1,708.[1204] In the aggregate, the staff estimates that compliance with new rule 30b1–8 and Form N–CR would result in a total annual burden of approximately 341 burden hours and total annual time costs of approximately $116,429.[1205] Given an estimated 586 money market funds that would be required to comply with new rule 30b1–8 and Form N–CR,[1206] this would result in an average annual burden of approximately 0.58 burden hours and average annual time costs of approximately $199 on a per-fund basis. The staff estimates that there will be no external costs associated with this collection of information.

5. Rule 34b–1(a)

As outlined above,[1207] because we are amending the wording of the rule 482(b)(4) risk disclosures in money market funds' advertisements, rule 34b–1(a) is indirectly affected by our proposed amendments because it references rule 482. However, we are proposing no changes to rule 34b–1(a) itself.

We already account for the burdens associated with the wording changes to the risk disclosures in money market fund advertising when discussing our amendments to rule 482(b)(4).[1208] By complying with our amendments to rule 482(b)(4), money market funds would also automatically remain in compliance with respect to how our proposed changes would affect rule 34b–1(a). Therefore, any burdens associated with rule 34b–1(a) as a result of our proposed amendment to rule 482(b)(4) are already accounted for in section IV.B.6 below.

6. Rule 482

As outlined above, we are proposing to amend the wording of the rule 482(b)(4) risk disclosures in money market funds' advertisements that would be adopted under the floating NAV alternative.[1209] Similarly, we are also proposing to amend the wording of the rule 482(b)(4) risk disclosures in money market funds' advertisements (including prominently on a fund's Web site) if the liquidity fees and gates alternative is adopted.[1210] For purposes of the estimated burden of the proposed amendments under the liquidity fees and gates alternative, however, Commission staff estimates the same burden as under the floating NAV alternative as discussed in Section IV.A.6 above.[1211] Therefore, using an estimate of 586 money market funds that would be required to comply with the amendments to rule 482(b)(4),[1212] the staff estimates that in the aggregate, the proposed amendments would result in a total one-time burden of approximately 3,077 burden hours [1213] at a total one-time time cost of approximately $857,904.[1214] Amortized over a three-year period, this would result in an average annual burden of approximately 1,026 burden hours at an annual time cost of approximately $285,968 for all funds. The staff estimates that there would be no external costs incurred in complying with the proposed amendment.

7. Form N–1A

We are proposing amendments to Form N–1A in connection with the liquidity fees and gates alternative proposal. This new collection of information would be mandatory for money market funds that rely on rule 2a–7, and to the extent that the Commission receives confidential information pursuant to these collections of information, such information would be kept confidential, subject to the provisions of applicable law.[1215]

a. Discussion of Proposed Amendments

The Commission's fees and gates alternative proposal would permit funds to charge liquidity fees and impose redemption restrictions on money market fund investors. To inform investors about these potential restrictions, we propose to require that each money market fund (other than government money market funds that have chosen to rely on the proposed rule 2a–7 exemption for government money market funds from the fee and gate requirements) include a bulleted statement, disclosing the particular risks associated with investing in a fund that may impose liquidity fees or redemption restrictions, in the summary section of the statutory prospectus (and, accordingly, in any summary prospectus, if used). We also propose to include wording designed to inform investors about the primary general risks of investing in money market funds in this bulleted disclosure statement.[1216]

2011 and October 2012, 4 prime money market funds had weekly liquid assets below 15% at the time of filing. The staff assumes that the Commission would receive 4 reports on Form N–CR filed in response to events specified on Part E (which requires filing when the 15% threshold is crossed, regardless of whether the fund imposes the default liquidity fee) and Part F (which requires filing when the 15% threshold is crossed and the fund imposes a redemption gate). Solely for purposes of this estimate, the staff counts the filings of the initial as well as amended report under Parts E and F as one report. *See* instructions to proposed (Fees & Gates) Form N–CR Parts E, F. Assuming that each time a fund crosses the 15% threshold, it would impose a fee or gate, and that it would eventually remove this fee or gate, the staff assumes that the Commission would additionally receive 4 reports on Form N–CR filed in response to events specified on Part G (which requires filing when a fund that has imposed a liquidity fee and/or suspended the fund's redemptions determines to remove such fee and/or resume fund redemptions).

However, this is a conservative estimate, because the staff expects that funds would be less likely to cross the 15% threshold if the Commission adopts our proposal, since the staff expects that the funds would increase their risk management around their level of weekly liquid assets in response to the fee and gate requirements.

[1203] This estimate is derived in part from our current PRA estimate for Form 8–K. In addition, the staff expects that it would take approximately the same amount of time to prepare and file a report on Form N–CR, regardless under which Part of Form N–CR it is filed.

[1204] This estimate is based on the following calculation: (4 hours × $379/hour for an attorney = $1,516), plus (1 hour × 192/hour for a fund senior accountant = $192), for a combined total of 5 hours (4 hours for an attorney + 1 hour for a fund senior accountant) and total time costs of $1,708.

[1205] This estimate is based on the following calculations: (20 reports filed per year in respect of Part B) + (40 reports filed per year in respect of Part C) + (0.167 reports filed per year in respect of Part D (1 report every 6 years divided by 6 years)) + (8 reports filed per year in respect of Parts E, F and G) = 68.167 reports filed per year. 68.167 reports filed per year × 5 hours per report = approximately 341 total annual burden hours. 68.167 reports filed per year × $1,708 in costs per report = approximately $116,429 total annual costs.

[1206] *See supra* note 1114.

[1207] *See supra* section IV.A.5.

[1208] *See infra* section IV.B.6.

[1209] *See supra* section IV.A.6.

[1210] *See* (Fees & Gates) rule 482(b)(4)(i); (Fees & Gates) rule 482(b)(4)(ii).

[1211] In *supra* note 1120, we discuss how the proposed compliance period of 2 years under the floating NAV alternative should allow funds sufficient time to amend the wording of their rule 482(b)(4) risk disclosures as part of a more general, periodic update of their advertising materials and Web site. While shorter than under the floating NAV alternative, the staff expects that making these changes as part of a more general update should still be possible with a compliance period of only 1 year as proposed under the liquidity fees and gates alternative.

[1212] This estimate is based on a staff review of reports on Form N–MFP filed with the Commission for the month ended February 28, 2013. For purposes of this PRA, the staff assumes that the universe of money market funds affected by the amendments to rule 482(b)(4) would be the same as the current universe for Form N–MFP.

[1213] This estimate is based on the following calculation: 5.25 burden hours per fund × 586 funds = approximately 3,077 total burden hours.

[1214] This estimate is based on the following calculation: approximately $1,464 total costs per fund × 586 funds = approximately $857,904 total costs.

[1215] *See supra* note 994.

[1216] As discussed above in section III.B.8, while money market funds are currently required to include a similar disclosure statement on their advertisements and sales materials, we propose

The liquidity fees and gates proposal would exempt government money market funds from any fee or gate requirement, but a government money market fund would be permitted to impose fees or gates if the ability to impose fees or gates were disclosed in the fund's prospectus. Accordingly, the proposed amendments to Form N–1A would require government money market funds that have chosen to rely on this exemption to include a bulleted disclosure statement in the summary section of the fund's statutory prospectus (and, accordingly, in any summary prospectus, if used) that does not include discussion of the risks of liquidity fees and gates, but that includes additional detail about the risks of investing in money market funds generally.

Currently, funds are required to disclose any restrictions on fund redemptions in their registration statements. We expect that, to comply with these requirements, money market funds (besides government money market funds that have chosen to rely on the proposed rule 2a–7 exemption from the fee and gate requirements) would disclose in the statutory prospectus, as well as in the SAI, as applicable, the effects that the potential imposition of fees and/or gates may have on a shareholder's ability to redeem shares of the fund. We also expect that, promptly after a money market fund imposes a redemption fee or gate, it would inform prospective investors of any fees or gates currently in place by means of a prospectus supplement.

For the reasons discussed above in section III.B.8.c, we are also proposing amendments to Form N–1A that would require all money market funds (except government money market funds that have chosen to rely on the proposed rule 2a–7 exemption from the fee and gate requirements) to provide SAI disclosure regarding the historical occasions in which the fund's weekly liquid assets have fallen below 15% or the fund has imposed liquidity fees or redemption gates.

Finally, for the reasons discussed above in section III.F.1.a, we are proposing amendments to Form N–1A that would require all money market funds to provide SAI disclosure regarding historical instances in which the fund has received financial support from a sponsor or fund affiliate. Specifically, the proposed amendments would require each money market fund to disclose any occasion during the last ten years on which an affiliated person, promoter, or principal underwriter of the fund, or an affiliated person of such person, provided any form of financial support to the fund.

b. Change in Burden

The current approved collection of information for Form N–1A is 1,578,689 annual aggregate hours, and the total annual external cost burden is $122,730,472. The respondents to this collection of information are open-end management investment companies registered with the Commission. The entities that would be affected by the proposed amendments to Form N–1A discussed above include all money market funds. However, various aspects of these amendments would only affect those money market funds that are not government funds that rely on the proposed rule 2a–7 exemption from the fee and gate requirements, while others would only affect government funds relying on the proposed exemption. For purposes of the PRA, staff estimates that, of the estimated 586 total money market funds,[1217] 165 funds would rely on the proposed government fund exemption.[1218]

The burdens associated with the proposed amendments to Form N–1A include one-time burdens as well as ongoing burdens. Commission staff estimates that each money market fund (except government money market funds that have chosen to rely on the proposed rule 2a–7 exemption from the fee and gate requirements) would incur a one-time burden of 5 hours,[1219] at a time cost of $1,480,[1220] to draft and finalize the required disclosure and amend its registration statement. In aggregate, staff estimates that these funds would incur a one-time burden of 2,105 hours,[1221] at a time cost of $623,080,[1222] to comply with the proposed Form N–1A disclosure requirements. In addition, Commission staff estimates that each money market fund (except government money market funds relying on the proposed government fund exemption) would incur an ongoing burden of 1 hour, at a time cost of $296,[1223] each year to: 1) review and update the SAI disclosure regarding historical occasions in which the fund's weekly liquid assets have fallen below 15% or the fund has imposed liquidity fees or redemption gates; 2) review and update the SAI disclosure regarding historical instances in which the fund has received financial support from a sponsor or fund affiliate; and 3) inform prospective investors of any fees or gates currently in place (as appropriate) by means of a prospectus supplement. In aggregate, staff estimates that these funds would incur an annual burden of 421 hours,[1224] at a time cost of $124,616,[1225] to comply with the proposed Form N–1A requirements.

Amortizing these one-time and ongoing hour and cost burdens over three years results in an average annual increased burden of approximately 2 hours per fund (except government money market funds that have chosen to rely on the proposed rule 2a–7

amending this disclosure statement to emphasize that money market fund sponsors are not obligated to provide financial support, and that money market funds may not be an appropriate investment option for investors who cannot tolerate losses.

[1217] *See supra* note 1040.

[1218] This estimate is based on the number of money market funds that self-reported as Government/Agency or Treasury funds on Form N–MFP as of February 28, 2013.

[1219] This estimate is based on the following calculation: 1 hour to update registration statement to include bulleted disclosure statement + 3 hours to update registration statement to include disclosure about effects that fees/gates may have on shareholder redemptions, and disclosure about historical occasions in which the fund's weekly liquid assets have fallen below 15% or the fund has imposed fees/gates + 1 hour to update registration statement to include disclosure about financial support received by the fund = 5 hours.

[1220] This estimate is based on the following calculation: (1 hour (to update registration statement to include bulleted disclosure statement) × $296 (blended rate for a compliance attorney and a senior programmer) = $296) + (3 hours (to update registration statement to include disclosure about effects that fees/gates may have on shareholder redemptions, and disclosure about historical occasions in which the fund's weekly liquid assets have fallen below 15% or the fund has imposed fees/gates) × $296 (blended rate for a compliance attorney and a senior programmer) = $888) + (1 hour (to update registration statement to include disclosure about financial support received by the fund) × $296 (blended rate for a compliance attorney and a senior programmer) = $296) = $1,480.

[1221] This estimate is based on the following calculation: 5 hours × 421 funds (586 total money market funds—165 funds that would rely on the proposed government fund exemption) = 2,105 hours.

[1222] This estimate is based on the following calculation: 2,105 hours × $296 (blended rate for a compliance attorney and a senior programmer) = $623,080.

[1223] This estimate is based on the following calculation: (0.5 hours (to review and update the SAI disclosure regarding historical occasions in which the fund's weekly liquid assets have fallen below 15% or the fund has imposed liquidity fees or redemption gates, and to inform prospective investors of any fees or gates currently in place (as appropriate) by means of a prospectus supplement) × $296 (blended rate for a compliance attorney and a senior programmer) = $148) + (0.5 hours (to review and update the SAI disclosure regarding historical instances in which the fund has received financial support from a sponsor or fund affiliate) × $296 (blended rate for a compliance attorney and a senior programmer) = $148) = $296.

[1224] This estimate is based on the following calculation: 1 hours × 421 funds (586 total money market funds—165 funds that would rely on the proposed government fund exemption) = 421 hours.

[1225] This estimate is based on the following calculation: 421 hours × $296 (blended rate for a compliance attorney and a senior programmer) = $124,616.

exemption from the fee and gate requirements),[1226] at a time cost of approximately $691 per fund.[1227] In aggregate, staff estimates that these funds would incur an average annual increased burden of 842 hours,[1228] at a time cost of $249,232,[1229] to comply with the proposed Form N–1A disclosure requirements.

Commission staff estimates that each government money market fund that has chosen to rely on the proposed rule 2a–7 exemption from the fee and gate requirements would incur a one-time burden of 2 hours,[1230] at a time cost of $592,[1231] to draft and finalize the required disclosure and amend its registration statement. In aggregate, staff estimates that these government funds would incur a one-time burden of 330 hours,[1232] at a time cost of $97,680,[1233] to comply with the proposed Form N–1A disclosure requirements. In addition, Commission staff estimates that each government fund relying on the proposed government fund exemption would incur an ongoing burden of 0.5 hours, at a time cost of $148,[1234] each year to review and update the SAI disclosure regarding historical instances in which the fund has received financial support from a sponsor or fund affiliate. In aggregate, staff estimates that government funds would incur an annual burden of approximately 83 hours,[1235] at a time cost of $24,568,[1236] to comply with the proposed Form N–1A disclosure requirements.

Amortizing these one-time and ongoing hour and cost burdens over three years results in an average annual increased burden of 1 hour per government fund that has chosen to rely on the proposed rule 2a–7 exemption,[1237] at a time cost of $296 per fund.[1238] In aggregate, staff estimates that these government funds would incur an average annual increased burden of 165 hours,[1239] at a time cost of $48,840,[1240] to comply with the proposed Form N–1A disclosure requirements.

In total, the staff estimates that all money market funds would incur an average annual increased burden of 1,007 hours,[1241] at a time cost of $298,072,[1242] to comply with the proposed Form N–1A disclosure requirements. Additionally, the staff estimates that there would be one-time aggregate external costs (in the form of printing costs) of $6,269,175 associated with the proposed Form N–1A disclosure requirements; amortizing these costs over three years results in annual aggregate external costs of $2,089,725.[1243]

8. Advisers Act Rule 204(b)–1 and Form PF

We are proposing the same amendments to Form PF under both the floating NAV and fees and gates proposals. Staff estimates that the estimated paperwork burdens associated with our amendments to Form PF as discussed above in connection with our floating NAV proposal apply equally to our fees and gates proposal. Therefore, as discussed above under our floating NAV proposal, our staff estimates that the proposed amendments to Form PF under our fees and gates proposal also would result in (1) increased annual burdens per large liquidity fund advisers of 290 burden hours, at a total time cost of $73,460, and $16,374 in external costs;[1244] (2) increased aggregate annual burden hours across all large liquidity fund advisers of 7,250 burden hours, at a total time cost of $1,836,500, and $409,350 in external costs;[1245] and (3) the aggregate paperwork burden for Form PF being revised to 249,300 burden hours and $23,310,350 in external costs.[1246]

*C. Request for Comments*

We request comment on whether our estimates for the change in burden hours and associated costs, as well as any external costs for the proposed amendments described above under our first alternative proposal—floating NAV—are reasonable. We also request comment on whether our estimates for the change in burden hours associated costs, as well as any external costs for the proposed amendments described above under our second alternative proposal—liquidity fees and gates—are reasonable. Pursuant to 44 U.S.C. 3506(c)(2)(B), the Commission solicits comments in order to: (i) Evaluate

[1226] This estimate is based on the following calculation: (5 burden hours (year 1) + 1 burden hour (year 2) + 1 burden hours (year 3)) ÷ 3 = approximately 2 hours.

[1227] This estimate is based on the following calculation: ($1,480 (year 1 monetized burden hours) + $296 (year 2 monetized burden hours) + $296 (year 3 monetized burden hours)) ÷ 3 = approximately $691.

[1228] This estimate is based on the following calculation: 2 hours × 421 funds (586 total money market funds—165 funds that would rely on the proposed government fund exemption) = 842 hours.

[1229] This estimate is based on the following calculation: 842 hours × $296 (blended rate for a compliance attorney and a senior programmer) = $249,232.

[1230] This estimate is based on the following calculation: 1 hour to update registration statement to include bulleted disclosure statement + 1 hour to update registration statement to include disclosure about financial support received by the fund = 2 hours.

[1231] This estimate is based on the following calculation: (1 hour (to update registration statement to include bulleted disclosure statement) × $296 (blended rate for a compliance attorney and a senior programmer) = $296) + (1 hour (to update registration statement to include disclosure about financial support received by the fund) × $296 (blended rate for a compliance attorney and a senior programmer) = $296) = $592.

[1232] This estimate is based on the following calculation: 2 hours × 165 funds that would rely on the proposed government fund exemption = 330 hours.

[1233] This estimate is based on the following calculation: 330 hours × $296 (blended rate for a compliance attorney and a senior programmer) = $97,680.

[1234] This estimate is based on the following calculation: 0.5 hours × $296 (blended rate for a compliance attorney and a senior programmer) = $148.

[1235] This estimate is based on the following calculation: 0.5 hours × 165 funds that would rely on the proposed government fund exemption = approximately 83 hours.

[1236] This estimate is based on the following calculation: 83 hours × $296 (blended rate for a compliance attorney and a senior programmer) = $24,568.

[1237] This estimate is based on the following calculation: 2 burden hours (year 1) + 0.5 burden hours (year 2) + 0.5 burden hours (year 3) ÷ 3 = 1 hour.

[1238] This estimate is based on the following calculation: $592 (year 1 monetized burden hours) + $148 (year 2 monetized burden hours) + $148 (year 3 monetized burden hours) ÷ 3 = $296.

[1239] This estimate is based on the following calculation: 1 hour × 165 funds that would rely on the proposed government fund exemption = 165 hours.

[1240] This estimate is based on the following calculation: 165 hours × $296 (blended rate for a compliance attorney and a senior programmer) = $48,840.

[1241] This estimate is based on the following calculation: 842 hours + 165 hours = 1,007 hours. *See supra* notes 1228 and 1239.

[1242] This estimate is based on the following calculation: $249,232 + $48,840 = $298,072.

[1243] We expect that a fund that must include disclosure about historical occasions in which the fund's weekly liquid assets have fallen below 15% or the fund has imposed fees/gates, or historical instances in which the fund has received financial support from a sponsor or fund affiliate, would need to add 2–8 pages of new disclosure to its registration statement. Adding this new disclosure would therefore increase the number of pages in, and change the printing costs of, the fund's registration statement. Commission staff calculates the external costs associated with the proposed Form N–1A disclosure requirements as follows: 5 pages (mid-point of 2 pages and 8 pages) × $0.045 per page × 27,863,000 money market fund registration statements printed annually = $6,269,175 one-time aggregate external costs. Amortizing these external costs over three years results in aggregate annual external costs of $2,089,725. Our estimate of potential printing ($0.045 per page: $0.035 for ink + $0.010 for paper) is based on data provided by Lexecon Inc. in response to Investment Company Act Release No. 27182 (Dec. 8, 2005) [70 FR 74598 (Dec. 15, 2005)]. *See* Lexecon Inc. Letter (Feb. 13, 2006), *available at http://www.sec.gov/rules/proposed/s71005/dbgross9453.pdf.* For purposes of this analysis, our best estimate of the number of money market fund registration statements printed annually is based on 27,863,000 money market fund shareholder accounts in 2012. *See* Investment Company Institute, *2013 Investment Company Fact Book,* at 178, *available at http://www.ici.org/pdf/2013_factbook.pdf.*

[1244] *See infra* note 1165.

[1245] *See infra* notes 1166–1168.

[1246] *See infra* notes 1169–1170.

whether the proposed collections of information are necessary for the proper performance of the functions of the Commission, including whether the information will have practical utility; (ii) evaluate the accuracy of the Commission's estimate of the burden of the proposed collections of information; (iii) determine whether there are ways to enhance the quality, utility, and clarity of the information to be collected; and (iv) determine whether there are ways to minimize the burden of the collections of information on those who are to respond, including through the use of automated collection techniques or other forms of information technology.

The agency has submitted the proposed collection of information to OMB for approval. Persons wishing to submit comments on the collection of information requirements of the proposed amendments should direct them to the Office of Management and Budget, Attention Desk Officer for the Securities and Exchange Commission, Office of Information and Regulatory Affairs, Washington, DC 20503, and should send a copy to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, 100 F Street NE., Washington, DC 20549–1090, with reference to File No. S7–03–13. OMB is required to make a decision concerning the collections of information between 30 and 60 days after publication of this Release; therefore, a comment to OMB is best assured of having its full effect if OMB receives it within 30 days after publication of this Release. Requests for materials submitted to OMB by the Commission with regard to these collections of information should be in writing, refer to File No. S7–03–13, and be submitted to the Securities and Exchange Commission, Office of Investor Education and Advocacy, 100 F Street NE., Washington, DC 20549–0213.

## V. Regulatory Flexibility Act Certification

Section 3(a) of the Regulatory Flexibility Act of 1980 [1247] (''RFA'') requires the Commission to undertake an initial regulatory flexibility analysis (''IRFA'') of the proposed rule amendments on small entities unless the Commission certifies that the rule, if adopted, would not have a significant economic impact on a substantial number of small entities.[1248] Pursuant to 5 U.S.C. section 605(b), the Commission hereby certifies that new rule 30b1–8 and Form N–CR under the Investment Company Act of 1940 and the proposed amendments to rules 2a–7, 12d3–1, 18f–3, 22e–3, 30b1–7, and 31a–1 and Forms N–MFP and N–1A under the Investment Company Act, Form PF under the Investment Advisers Act of 1940, and rules 482 and 419 under the Securities Act of 1933, would not, if adopted have a significant economic impact on a substantial number of small entities.

The proposal would amend rule 2a–7 under the Investment Company Act to:

- Require money market funds other than government and retail money market funds: (a) to ''float'' their net asset values; or (b) under an alternative proposal, to impose, under certain circumstances, a liquidity fee, and permit funds to impose a redemption gate.
- Require that money market funds disclose on the fund's Web site daily and weekly liquidity, the funds' daily market-based NAV per share (or current NAV per share under our floating NAV proposal), and certain information that the fund is required to report to the Commission on new Form N–CR regarding the imposition and subsequent removal of liquidity fees or gates (where applicable).
- Require money market funds to treat certain affiliates as single issuers when applying rule 2a–7's 5% issuer diversification requirement.
- Require money market funds to treat the sponsors of asset-backed securities as guarantors subject to rule 2a–7's diversification requirements unless the fund's board of directors determines the fund is not relying on the sponsor's support when determining the asset-backed security's credit quality or liquidity.
- Require money market funds to apply rule 2a–7's diversification restrictions applicable to demand features and guarantees (including guarantees deemed issued by sponsors of asset-backed securities) to all of the funds' total assets, rather than 75% of the funds' total assets as provided in current rule 2a–7.
- Amend the stress testing requirements to require funds to adopt procedures providing for periodic testing (and reporting of results to fund boards) of money market funds' ability to maintain 15% of its total assets in weekly liquid assets (and, under the floating NAV proposal, eliminate the current requirement to test a fund's ability to maintain a stable NAV per share), based on specified amended hypothetical events.
- Make clarifying amendments to: (a) Certain characteristics of instruments that qualify as daily or weekly liquid assets; (b) the definition of demand feature; (c) the method for determining weighted average life for short-term floating rate securities; and (d) the method for determining the 45-day remaining maturity when complying with rule 2a–7's limitation on the acquisition of second tier securities.

We also are proposing to amend rule 22e–3, which exempts money market funds from section 22(e) to permit them to suspend redemptions in order to facilitate an orderly liquidation of fund assets. Under both proposals, we propose to amend the rule to provide that money market funds be permitted to suspend redemptions, when, among other requirements, the fund, at the end of a business day, has less than 15% of its total assets in weekly liquid assets.

We are also proposing new rule 30b1–8 that would require money market funds to file reports with the Commission on new Form N–CR upon the occurrence of specific events, which reports would immediately be made public. New Form N–CR would require all money market funds to make prompt public disclosure of instances of portfolio security default and sponsor support. If we adopt our liquidity fees and gates proposal, money market funds would be required to disclose a decline in the fund's weekly liquid assets below 15% of total assets, imposition and removal of liquidity fees and/or gates, and a decline in the market-based price of the fund below $0.9975. If we adopt our floating NAV proposal, money market funds would be required to disclose a decline in the market-based price of the fund below $0.9975 (for a government or retail money market fund that retains a stable price per share).

We also are proposing to amend rule 30b1–7 by (i) requiring that money market funds file Form N–MFP with the Commission, current as of the last business day or any subsequent calendar day of the preceding month; and (ii) making information filed on Form N–MFP publicly available immediately upon filing, rather than 60 days after the end of the month to which the information pertains. We also are proposing to amend Form N–MFP to reflect the proposed amendments to rule 2a–7 discussed above, request certain additional information that would be useful for our oversight of money market funds, and make technical and clarifying changes based on our experience with filings submitted during the past year and a half.

We are also proposing to amend Form PF to require registered investment advisers to certain ''qualifying'' liquidity funds to provide certain information with respect to those funds'

[1247] 5 U.S.C. 603(a).

[1248] 5 U.S.C. 605(b).

portfolio holdings, similar to the information we require money market funds to disclose on Form N–MFP.

We are also proposing to amend rule 482 under the Securities Act of 1933 to require that money market funds amend any ''advertisements'' to notify investors that the fund may impose a liquidity fee and/or gate under certain circumstances and include specific language informing investors about the potential risks of investing in money market funds (under our proposed liquidity fees and gates proposal). Similarly, if we adopt our alternative floating NAV proposal, we would amend rule 482 to provide enhanced disclosure to investors about the potential for fluctuation in the value of the fund shares and the possibility for losses.

We also are proposing under either alternative proposal to amend Form N–1A to require that money market funds include the revised risk disclosures (discussed above in proposing to amend rule 482) pursuant to Item 4 and also disclose historic instances of sponsor support. In addition, if we adopt our liquidity fees and gates proposal, we propose to amend Item 3 of Form N–1A to make clear that ''redemption fees'' would not include any liquidity fee imposed.

Finally, we are proposing to amend rules 12d3–1, 18f–3, 31a–1, and 419, in each case simply to update cross references in those rules to reflect our proposed amendments to rule 2a–7.

Based on information in filings submitted to the Commission, we believe that there are no money market funds that are small entities.[1249] For this reason, the Commission believes the new rule 30b1–8 and the proposed amendments to rules 2a–7, 12d3–1, 18f–3, 22e–3, 30b1–7, 31a–1, 419 and 482, and Forms N–CR, N–MFP, PF and N–1A, would not, if adopted, have a significant economic impact on a substantial number of small entities.

We encourage written comments regarding this certification. We solicit comment as to whether new rule 30b1–8 and the proposed amendments to rules 2a–7, 12d3–1, 18f–3, 22e–3, 30b1–7, 31a–1, 419 and 482, and Forms N–CR, N–MFP, PF and N–1A could have an effect on small entities that has not been considered. We request that commenters describe the nature of any impact on small entities and provide empirical data to support the extent of such impact.

[1249] Under the Investment Company Act, an investment company is considered a small business or small organization if it, together with other investment companies in the same group of related investment companies, has net assets of $50 million or less as of the end of its most recent fiscal year. *See* 17 CFR 270.0–10.

## VI. Statutory Authority

The Commission is proposing amendments to rule 419 under the rulemaking authority set forth in sections 3, 4, 5, 7, and 19 of the Securities Act [15 U.S.C. 77c, 77d, 77e, 77g, and 77s]. The Commission is proposing amendments to rule 482 pursuant to authority set forth in sections 5, 10(b), 19(a), and 28 of the Securities Act [15 U.S.C. 77e, 77j(b), 77s(a), and 77z–3] and sections 24(g) and 38(a) of the Investment Company Act [15 U.S.C. 80a–24(g) and 80a–37(a)]. The Commission is proposing amendments to rule 2a–7 under the exemptive and rulemaking authority set forth in sections 6(c), 8(b), 22(c), 35(d), and 38(a) of the Investment Company Act of 1940 [15 U.S.C. 80a–6(c), 80a–8(b), 80a–22(c), 80a–35(d), and 80a–37(a)]. The Commission is proposing amendments to rule 12d3–1 pursuant to the authority set forth in sections 6(c) and 38(a)] of the Investment Company Act [15 U.S.C. 80a–6(c) and 80a–37(a)]. The Commission is proposing amendments to rule 18f–3 pursuant to the authority set forth in sections 6(c) and 38(a) of the Investment Company Act [15 U.S.C. 80a–6(c) and 80a–37(a)]. The Commission is proposing amendments to rule 22e–3 pursuant to the authority set forth in sections 6(c), 22(e) and 38(a) of the Investment Company Act [15 U.S.C. 80a–6(c), 80a–22(e), and 80a–37(a)]. The Commission is proposing amendments to rule 30b1–7 and Form N–MFP pursuant to authority set forth in Sections 8(b), 30(b), 31(a), and 38(a) of the Investment Company Act [15 U.S.C. 80a–8(b), 80a–29(b), 80a–30(a), and 80a–37(a)]. The Commission is proposing new rule 30b1–8 and Form N–CR pursuant to authority set forth in Sections 8(b), 30(b), 31(a), and 38(a) of the Investment Company Act [15 U.S.C. 80a–8(b), 80a–29(b), 80a–30(a), and 80a–37(a)]. The Commission is proposing amendments to rule 31a–1 pursuant to authority set forth in sections 6(c) and 38(a)] of the Investment Company Act [15 U.S.C. 80a–6(c) and 80a–37(a)]. The Commission is proposing amendments to Form N–1A pursuant to authority set forth in Sections 5, 6, 7, 10, and 19(a) of the Securities Act [15 U.S.C. 77e, 77f, 77g, 77j and 77s(a)] and Sections 8, 24(a), 24(g), 30, and 38 of the Investment Company Act [15 U.S.C. 80a–8, 80a–24(a), 80a–24(g), 80a–29, and 80a–37]. The Commission is proposing amendments to Form PF pursuant to authority set forth in Sections 204(b) and 211(e) of the Advisers Act [15 U.S.C. 80b–4 and 15 U.S.C. 80b–11].

### List of Subjects in 17 CFR Parts 230, 239, 270, 274, and 279

Investment companies, Reporting and recordkeeping requirements, Securities.

### Text of Proposed Rules and Forms

For reasons set out in the preamble, Title 17, Chapter II of the Code of Federal Regulations is proposed to be amended as follows:

## PART 230—GENERAL RULES AND REGULATIONS, SECURITIES ACT OF 1933

■ 1. The general authority citation for Part 230 continues to read, in part, as follows:

**Authority:** 15 U.S.C. 77b, 77b note, 77c, 77d, 77f, 77g, 77h, 77j, 77r, 77s, 77z–3, 77sss, 78c, 78d, 78j, 78*l*, 78m, 78n, 78o, 78o–7 note, 78t, 78w, 78*ll*(d), 78mm, 80a–8, 80a–24, 80a–28, 80a–29, 80a–30, and 80a–37, unless otherwise noted.

* * * * *

■ 2. Section 230.419(b)(2)(iv)(B) is amended by removing the phrase ''paragraphs (c)(2), (c)(3), and (c)(4)'' and adding in its place ''paragraph (d)''.

■ 3. Section 230.482(b)(3)(i) is amended under Alternative 1 by adding after ''An advertisement for a money market fund'' the phrase ''that is subject to the exemption provisions of § 270.2a–7(c)(2) of this chapter or § 270.2a–7(c)(3) of this chapter''.

■ 4. Section 230.482(b)(4) is revised to read as follows:

### Alternative 1

**§ 230.482 Advertising by an investment company as satisfying requirements of section 10.**

* * * * *

(b) * * *

(4) Money market funds.

(i) An advertisement for an investment company that holds itself out to be a money market fund, and that is not subject to the exemption provisions of § 270.2a–7(c)(2) of this chapter or § 270.2a–7(c)(3) of this chapter, must include the following statement, presented as prescribed in Item 4(b) of Form N–1A (§ 274.11A of this chapter):

You could lose money by investing in the Fund.

You should not invest in the Fund if you require your investment to maintain a stable value.

The value of shares of the Fund will increase and decrease as a result of changes in the value of the securities in which the Fund invests. The value of the securities in which the Fund invests may in turn be affected by many factors, including interest

rate changes and defaults or changes in the credit quality of a security's issuer.

An investment in the Fund is not insured or guaranteed by the Federal Deposit Insurance Corporation or any other government agency.

The Fund's sponsor has no legal obligation to provide financial support to the Fund, and you should not expect that the sponsor will provide financial support to the Fund at any time.

(ii) An advertisement for an investment company that holds itself out to be a money market fund, and that is subject to the exemption provisions of § 270.2a–7(c)(2) of this chapter or § 270.2a–7(c)(3) of this chapter, must include the following statement, presented as prescribed in Item 4(b) of Form N–1A (§ 274.11A of this chapter):

You could lose money by investing in the Fund.

The Fund seeks to preserve the value of your investment at $1.00 per share, but cannot guarantee such stability.

An investment in the Fund is not insured or guaranteed by the Federal Deposit Insurance Corporation or any other government agency.

The Fund's sponsor has no legal obligation to provide financial support to the Fund, and you should not expect that the sponsor will provide financial support to the Fund at any time.

**Note to paragraph (b)(4).** If an affiliated person, promoter, or principal underwriter of the Fund, or an affiliated person of such a person, has entered into an agreement to provide financial support to the Fund, the statement may omit the last sentence (''The Fund's sponsor has no legal obligation to provide financial support to the Fund, and you should not expect that the sponsor will provide financial support to the Fund at any time.'') for the term of the agreement. For purposes of this Note, the term ''financial support'' includes, for example, any capital contribution, purchase of a security from the Fund in reliance on § 270.17a–9, purchase of any defaulted or devalued security at par, purchase of Fund shares, execution of letter of credit or letter of indemnity, capital support agreement (whether or not the Fund ultimately received support), or performance guarantee, or any other similar action to increase the value of the fund's portfolio or otherwise support the fund during times of stress.

## Alternative 2

### § 230.482 Advertising by an investment company as satisfying requirements of section 10.

* * * * *

(b) * * *

(4) Money market funds.

(i) An advertisement for an investment company that holds itself out to be a money market fund (including any money market fund that is subject to the exemption provisions of § 270.2a–7(c)(2)(iii) of this chapter, but that has chosen not to rely on the exemption provided by rule § 270.2a–7(c)(2)(iii) of this chapter) must include the following statement, presented as prescribed in Item 4(b) of Form N–1A (§ 274.11A of this chapter):

You could lose money by investing in the Fund.

The Fund seeks to preserve the value of your investment at $1.00 per share, but cannot guarantee such stability.

The Fund may impose a fee upon sale of your shares when the Fund is under considerable stress.

The Fund may temporarily suspend your ability to sell shares of the Fund when the Fund is under considerable stress.

An investment in the Fund is not insured or guaranteed by the Federal Deposit Insurance Corporation or any other government agency.

The Fund's sponsor has no legal obligation to provide financial support to the Fund, and you should not expect that the sponsor will provide financial support to the Fund at any time.

(ii) An advertisement for an investment company that holds itself out to be a money market fund, and that is subject to the exemption provisions of § 270.2a–7(c)(2)(iii) of this chapter and has chosen to rely on the exemption provided by § 270.2a–7(c)(2)(iii) of this chapter, must include the following statement, presented as prescribed in Item 4(b) of Form N–1A (§ 274.11A of this chapter):

You could lose money by investing in the Fund.

The Fund seeks to preserve the value of your investment at $1.00 per share, but cannot guarantee such stability.

An investment in the Fund is not insured or guaranteed by the Federal Deposit Insurance Corporation or any other government agency.

The Fund's sponsor has no legal obligation to provide financial support to the Fund, and you should not expect that the sponsor will provide financial support to the Fund at any time.

**Note to paragraph (b)(4).** If an affiliated person, promoter, or principal underwriter of the Fund, or an affiliated person of such a person, has entered into an agreement to provide financial support to the Fund, the statement may omit the last sentence (''The Fund's sponsor has no legal obligation to provide financial support to the Fund, and you should not expect that the sponsor will provide financial support to the Fund at any time.'') for the term of the agreement. For purposes of this Note, the term ''financial support'' includes, for example, any capital contribution, purchase of a security from the Fund in reliance on § 270.17a–9, purchase of any defaulted or devalued security at par, purchase of Fund shares, execution of letter of credit or letter of indemnity, capital support agreement (whether or not the Fund ultimately received support), or performance guarantee, or any other similar action to increase the value of the Fund's portfolio or otherwise support the Fund during times of stress.

## PART 270—RULES AND REGULATIONS, INVESTMENT COMPANY ACT OF 1940

■ 5. The authority citation for Part 270 continues to read, in part, as follows:

**Authority:** 15 U.S.C. 80a–1 *et seq.,* 80a–34(d), 80a–37, and 80a–39, unless otherwise noted.

* * * * *

■ 6. Section 270.2a–7 is revised to read as follows:

## Alternative 1

### § 270.2a–7 Money market funds.

(a) *Definitions.*

(1) *Acquisition* (or *acquire*) means any purchase or subsequent rollover (but does not include the failure to exercise a Demand Feature).

(2) *Amortized cost* means the value of a security at the fund's acquisition cost as adjusted for amortization of premium or accretion of discount rather than at the security's value based on current market factors.

(3) *Asset-backed security* means a fixed income security (other than a government security) issued by a special purpose entity (as defined in this paragraph (a)(3)), substantially all of the assets of which consist of qualifying assets (as defined in this paragraph (a)(3)). *Special purpose entity* means a trust, corporation, partnership or other entity organized for the sole purpose of issuing securities that entitle their holders to receive payments that depend primarily on the cash flow from qualifying assets, but does not include a registered investment company. *Qualifying assets* means financial assets, either fixed or revolving, that by their terms convert into cash within a finite time period, plus any rights or other assets designed to assure the servicing or timely distribution of proceeds to security holders.

(4) *Business day* means any day, other than Saturday, Sunday, or any customary business holiday.

(5) *Collateralized fully* has the same meaning as defined in § 270.5b–3(c)(1) except that § 270.5b–3(c)(1)(iv)(C) and (D) shall not apply.

(6) *Conditional demand feature* means a demand feature that is not an unconditional demand feature. A conditional demand feature is not a guarantee.

(7) *Conduit security* means a security issued by a municipal issuer (as defined in this paragraph (a)(7)) involving an arrangement or agreement entered into,

directly or indirectly, with a person other than a municipal issuer, which arrangement or agreement provides for or secures repayment of the security. *Municipal issuer* means a state or territory of the United States (including the District of Columbia), or any political subdivision or public instrumentality of a state or territory of the United States. A conduit security does not include a security that is:

(i) Fully and unconditionally guaranteed by a municipal issuer;

(ii) Payable from the general revenues of the municipal issuer or other municipal issuers (other than those revenues derived from an agreement or arrangement with a person who is not a municipal issuer that provides for or secures repayment of the security issued by the municipal issuer);

(iii) Related to a project owned and operated by a municipal issuer; or

(iv) Related to a facility leased to and under the control of an industrial or commercial enterprise that is part of a public project which, as a whole, is owned and under the control of a municipal issuer.

(8) *Daily liquid assets* means:

(i) Cash;

(ii) Direct obligations of the U.S. Government;

(iii) Securities that will mature, as determined without reference to the exceptions in paragraph (i) of this section regarding interest rate readjustments, or are subject to a demand feature that is exercisable and payable, within one business day; or

(iv) Amounts receivable and due unconditionally within one business day on pending sales of portfolio securities.

(9) *Demand feature* means a feature permitting the holder of a security to sell the security at an exercise price equal to the approximate amortized cost of the security plus accrued interest, if any, at the later of the time of exercise or the settlement of the transaction, paid within 397 calendar days of exercise.

(10) *Designated NRSRO* means any one of at least four nationally recognized statistical rating organizations, as that term is defined in section 3(a)(62) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)(62)), that:

(i) The money market fund's board of directors:

(A) Has designated as an NRSRO whose credit ratings with respect to any obligor or security or particular obligors or securities will be used by the fund to determine whether a security is an eligible security; and

(B) Determines at least once each calendar year issues credit ratings that are sufficiently reliable for such use;

(ii) Is not an ''affiliated person,'' as defined in section 2(a)(3)(C) of the Act (15 U.S.C. 80a–2(a)(3)(C)), of the issuer of, or any insurer or provider of credit support for, the security; and

(iii) The fund discloses in its statement of additional information is a designated NRSRO, including any limitations with respect to the fund's use of such designation.

(11) *Eligible security* means:

(i) A rated security with a remaining maturity of 397 calendar days or less that has received a rating from the requisite NRSROs in one of the two highest short-term rating categories (within which there may be sub-categories or gradations indicating relative standing); or

(ii) An unrated security that is of comparable quality to a security meeting the requirements for a rated security in paragraph (a)(11)(i) of this section, as determined by the money market fund's board of directors; provided, however, that: a security that at the time of issuance had a remaining maturity of more than 397 calendar days but that has a remaining maturity of 397 calendar days or less and that is an unrated security is not an eligible security if the security has received a long-term rating from any designated NRSRO that is not within the designated NRSRO's three highest long-term ratings categories (within which there may be sub-categories or gradations indicating relative standing), unless the security has received a long-term rating from the requisite NRSROs in one of the three highest rating categories.

(iii) In addition, in the case of a security that is subject to a demand feature or guarantee:

(A) The guarantee has received a rating from a designated NRSRO or the guarantee is issued by a guarantor that has received a rating from a designated NRSRO with respect to a class of debt obligations (or any debt obligation within that class) that is comparable in priority and security to the guarantee, unless:

(*1*) The guarantee is issued by a person that, directly or indirectly, controls, is controlled by or is under common control with the issuer of the security subject to the guarantee (other than a sponsor of a special purpose entity with respect to an asset-backed security);

(*2*) The security subject to the guarantee is a repurchase agreement that is collateralized fully; or

(*3*) The guarantee is itself a government security; and

(B) The issuer of the demand feature or guarantee, or another institution, has undertaken promptly to notify the holder of the security in the event the demand feature or guarantee is substituted with another demand feature or guarantee (if such substitution is permissible under the terms of the demand feature or guarantee).

(12) *Event of insolvency* has the same meaning as defined in § 270.5b–3(c)(2).

(13) *First tier security* means any eligible security that:

(i) Is a rated security that has received a short-term rating from the requisite NRSROs in the highest short-term rating category for debt obligations (within which there may be sub-categories or gradations indicating relative standing);

(ii) Is an unrated security that is of comparable quality to a security meeting the requirements for a rated security in paragraph (a)(13)(i) of this section, as determined by the fund's board of directors;

(iii) Is a security issued by a registered investment company that is a money market fund; or

(iv) Is a government security.

(14) *Floating rate security* means a security the terms of which provide for the adjustment of its interest rate whenever a specified interest rate changes and that, at any time until the final maturity of the instrument or the period remaining until the principal amount can be recovered through demand, can reasonably be expected to have a market value that approximates its amortized cost.

(15) *Government security* has the same meaning as defined in section 2(a)(16) of the Act (15 U.S.C. 80a–2(a)(16)).

(16) *Guarantee:*

(i) Means an unconditional obligation of a person other than the issuer of the security to undertake to pay, upon presentment by the holder of the guarantee (if required), the principal amount of the underlying security plus accrued interest when due or upon default, or, in the case of an unconditional demand feature, an obligation that entitles the holder to receive upon the later of exercise or the settlement of the transaction the approximate amortized cost of the underlying security or securities, plus accrued interest, if any. A guarantee includes a letter of credit, financial guaranty (bond) insurance, and an unconditional demand feature (other than an unconditional demand feature provided by the issuer of the security).

(ii) The sponsor of a special purpose entity with respect to an asset-backed security shall be deemed to have provided a guarantee with respect to the

entire principal amount of the asset-backed security for purposes of this section, except paragraphs (a)(11)(iii) (definition of eligible security), (d)(2)(iii) (credit substitution), (d)(3)(iv)(A) (fractional guarantees) and (e) (guarantees not relied on) of this section, unless the money market fund's board of directors has determined that the fund is not relying on the sponsor's financial strength or its ability or willingness to provide liquidity, credit or other support to determine the quality (pursuant to paragraph (d)(2) of this section) or liquidity (pursuant to paragraph (d)(4) of this section) of the asset-backed security, and maintains a record of this determination (pursuant to paragraphs (g)(6) and (h)(6) of this section).

(17) *Guarantee issued by a non-controlled person* means a guarantee issued by:

(i) A person that, directly or indirectly, does not control, and is not controlled by or under common control with the issuer of the security subject to the guarantee (*control* has the same meaning as defined in section 2(a)(9) of the Act) (15 U.S.C. 80a–2(a)(9)); or

(ii) A sponsor of a special purpose entity with respect to an asset-backed security if the money market fund's board of directors has made the findings described in paragraph (g)(6) of this section.

(18) *Illiquid security* means a security that cannot be sold or disposed of in the ordinary course of business within seven calendar days at approximately the value ascribed to it by the fund.

(19) *Penny-rounding method* of pricing means the method of computing an investment company's price per share for purposes of distribution, redemption and repurchase whereby the current net asset value per share is rounded to the nearest one percent.

(20) *Rated security* means a security that meets the requirements of paragraphs (a)(20)(i) or (ii) of this section, in each case subject to paragraph (a)(20)(iii) of this section:

(i) The security has received a short-term rating from a designated NRSRO, or has been issued by an issuer that has received a short-term rating from a designated NRSRO with respect to a class of debt obligations (or any debt obligation within that class) that is comparable in priority and security with the security; or

(ii) The security is subject to a guarantee that has received a short-term rating from a designated NRSRO, or a guarantee issued by a guarantor that has received a short-term rating from a designated NRSRO with respect to a class of debt obligations (or any debt obligation within that class) that is comparable in priority and security with the guarantee; but

(iii) A security is not a rated security if it is subject to an external credit support agreement (including an arrangement by which the security has become a refunded security) that was not in effect when the security was assigned its rating, unless the security has received a short-term rating reflecting the existence of the credit support agreement as provided in paragraph (a)(20)(i) of this section, or the credit support agreement with respect to the security has received a short-term rating as provided in paragraph (a)(20)(ii) of this section.

(21) *Refunded security* has the same meaning as defined in § 270.5b–3(c)(4).

(22) *Requisite NRSROs* means:

(i) Any two designated NRSROs that have issued a rating with respect to a security or class of debt obligations of an issuer; or

(ii) If only one designated NRSRO has issued a rating with respect to such security or class of debt obligations of an issuer at the time the fund acquires the security, that designated NRSRO.

(23) *Second tier security* means any eligible security that is not a first tier security.

(24) *Single state fund* means a tax exempt fund that holds itself out as seeking to maximize the amount of its distributed income that is exempt from the income taxes or other taxes on investments of a particular state and, where applicable, subdivisions thereof.

(25) *Tax exempt fund* means any money market fund that holds itself out as distributing income exempt from regular federal income tax.

(26) *Total assets* means the total value of the money market fund's assets, as defined in section 2(a)(41) of the Act (15 U.S.C. 80a–2(a)(41)) and the rules thereunder.

(27) *Unconditional demand feature* means a demand feature that by its terms would be readily exercisable in the event of a default in payment of principal or interest on the underlying security or securities.

(28) *United States dollar-denominated* means, with reference to a security, that all principal and interest payments on such security are payable to security holders in United States dollars under all circumstances and that the interest rate of, the principal amount to be repaid, and the timing of payments related to such security do not vary or float with the value of a foreign currency, the rate of interest payable on foreign currency borrowings, or with any other interest rate or index expressed in a currency other than United States dollars.

(29) *Unrated security* means a security that is not a rated security.

(30) *Variable rate security* means a security the terms of which provide for the adjustment of its interest rate on set dates (such as the last day of a month or calendar quarter) and that, upon each adjustment until the final maturity of the instrument or the period remaining until the principal amount can be recovered through demand, can reasonably be expected to have a market value that approximates its amortized cost.

(31) *Weekly liquid assets* means:

(i) Cash;

(ii) Direct obligations of the U.S. Government;

(iii) Government securities that are issued by a person controlled or supervised by and acting as an instrumentality of the government of the United States pursuant to authority granted by the Congress of the United States that:

(A) Are issued at a discount to the principal amount to be repaid at maturity without provision for the payment of interest; and

(B) Have a remaining maturity date of 60 days or less;

(iv) Securities that will mature, as determined without reference to the exceptions in paragraph (i) of this section regarding interest rate readjustments, or are subject to a demand feature that is exercisable and payable, within five business days; or

(v) Amounts receivable and due unconditionally within five business days on pending sales of portfolio securities.

(b) Holding out and use of names and titles.

(1) It shall be an untrue statement of material fact within the meaning of section 34(b) of the Act (15 U.S.C. 80a–33(b)) for a registered investment company, in any registration statement, application, report, account, record, or other document filed or transmitted pursuant to the Act, including any advertisement, pamphlet, circular, form letter, or other sales literature addressed to or intended for distribution to prospective investors that is required to be filed with the Commission by section 24(b) of the Act (15 U.S.C. 80a–24(b)), to hold itself out to investors as a money market fund or the equivalent of a money market fund, unless such registered investment company complies with this section.

(2) It shall constitute the use of a materially deceptive or misleading name or title within the meaning of section 35(d) of the Act (15 U.S.C. 80a–

34(d)) for a registered investment company to adopt the term ''money market'' as part of its name or title or the name or title of any redeemable securities of which it is the issuer, or to adopt a name that suggests that it is a money market fund or the equivalent of a money market fund, unless such registered investment company complies with this section.

(3) For purposes of paragraph (b)(2) of this section, a name that suggests that a registered investment company is a money market fund or the equivalent thereof includes one that uses such terms as ''cash,'' ''liquid,'' ''money,'' ''ready assets'' or similar terms.

(c) *Share price.*

(1) *Level of accuracy.* Except as provided in paragraphs (c)(2) and (c)(3) of this section, the money market fund must compute its price per share for purposes of distribution, redemption and repurchase by rounding the fund's current net asset value per share to the fourth decimal place in the case of a fund with a $1.0000 share price or an equivalent level of accuracy for money market funds with a different share price (*e.g.* $10.000 or $100.00 per share).

(2) *Exemption for funds investing primarily in government securities.* A money market fund may, notwithstanding section 2(a)(41) of the Act (15 U.S.C. 80a–2(a)(41)) and §§ 270.2a–4 and 270.22c–1, compute the current price per share of its redeemable securities for purposes of distribution, redemption and repurchase by use of the penny-rounding method if and so long as eighty percent or more of the money market fund's total assets are invested in cash, government securities, and/or repurchase agreements that are collateralized fully.

(3) *Exemption for retail money market funds.*

(i) *General.* A money market fund may, notwithstanding section 2(a)(41) of the Act (15 U.S.C. 80a–2(a)(41)) and §§ 270.2a–4 and 270.22c–1, compute the current price per share of its redeemable securities for purposes of distribution, redemption and repurchase by use of the penny-rounding method if, subject to paragraph (c)(3)(ii) of this section, the fund does not permit any shareholder of record to redeem more than $1,000,000 of redeemable securities on any one business day.

(ii) *Omnibus account holders.* A money market fund may permit a shareholder of record to redeem more than $1,000,000 of redeemable securities on any one business day if the shareholder of record is a broker, dealer, bank, or other person that holds securities issued by the fund in nominee name (''omnibus account holder'') and the money market fund has policies and procedures reasonably designed to allow the conclusion that the omnibus account holder does not permit any beneficial owner of the money market fund's shares, directly or indirectly, (or the omnibus account holder itself investing for its own account) to redeem more than $1,000,000 of redeemable securities on any one business day.

(iii) *Exemptions.*

(A) A money market fund is exempt from the requirements of sections 18(f)(1) and 22(e) of the Act (15 U.S.C. 80a–18(f)(1) and 80a–22(e)) to the extent necessary to permit the money market fund to limit redemptions in excess of $1,000,000 of redeemable securities on any one business day as provided in paragraphs (c)(3)(i) and (ii) of this section.

(B) A registered separate account funding variable insurance contracts and the sponsoring insurance company of such account are exempt from the requirements of section 27(i)(2)(A) of the Act (15 U.S.C. 80a–27(i)(2)(A)) to the extent necessary to permit the separate account or the sponsoring insurance company of such account to apply the limitations on redemptions as provided in paragraphs (c)(3)(i) and (ii) of this section to contract owners who allocate all or a portion of their contract value to a subaccount of the separate account that is either a money market fund or that invests all of its assets in shares of a money market fund.

(d) *Risk-limiting conditions.*

(1) *Portfolio maturity.* The money market fund must maintain a dollar-weighted average portfolio maturity appropriate to its investment objectives; provided, however, that the money market fund must not:

(i) Acquire any instrument with a remaining maturity of greater than 397 calendar days;

(ii) Maintain a dollar-weighted average portfolio maturity (''WAM'') that exceeds 60 calendar days; or

(iii) Maintain a dollar-weighted average portfolio maturity that exceeds 120 calendar days, determined without reference to the exceptions in paragraph (i) of this section regarding interest rate readjustments (''WAL'').

(2) *Portfolio quality.*

(i) *General.* The money market fund must limit its portfolio investments to those United States dollar-denominated securities that the fund's board of directors determines present minimal credit risks (which determination must be based on factors pertaining to credit quality in addition to any rating assigned to such securities by a designated NRSRO) and that are at the time of acquisition eligible securities.

(ii) *Second tier securities.* No money market fund may acquire a second tier security with a remaining maturity of greater than 45 calendar days, *determined without reference to the exceptions in paragraph (i) of this section* regarding interest rate readjustments. Immediately after the acquisition of any second tier security, a money market fund must not have invested more than three percent of its total assets in second tier securities.

(iii) *Securities subject to guarantees.* A security that is subject to a guarantee may be determined to be an eligible security or a first tier security based solely on whether the guarantee is an eligible security or first tier security, as the case may be.

(iv) *Securities subject to conditional demand features.* A security that is subject to a conditional demand feature (''underlying security'') may be determined to be an eligible security or a first tier security only if:

(A) The conditional demand feature is an eligible security or first tier security, as the case may be;

(B) At the time of the acquisition of the underlying security, the money market fund's board of directors has determined that there is minimal risk that the circumstances that would result in the conditional demand feature not being exercisable will occur; and

*(1)* The conditions limiting exercise either can be monitored readily by the fund or relate to the taxability, under federal, state or local law, of the interest payments on the security; or

*(2)* The terms of the conditional demand feature require that the fund will receive notice of the occurrence of the condition and the opportunity to exercise the demand feature in accordance with its terms; and

(C) The underlying security or any guarantee of such security (or the debt securities of the issuer of the underlying security or guarantee that are comparable in priority and security with the underlying security or guarantee) has received either a short-term rating or a long-term rating, as the case may be, from the requisite NRSROs within the NRSROs' two highest short-term or long-term rating categories (within which there may be sub-categories or gradations indicating relative standing) or, if unrated, is determined to be of comparable quality by the money market fund's board of directors to a security that has received a rating from the requisite NRSROs within the NRSROs' two highest short-term or long-term rating categories, as the case may be.

(3) *Portfolio diversification.*

(i) *Issuer diversification.* The money market fund must be diversified with respect to issuers of securities acquired by the fund as provided in paragraphs (d)(3)(i) and (d)(3)(ii) of this section, other than with respect to government securities and securities subject to a guarantee issued by a non-controlled person.

(A) *Taxable and national funds.* Immediately after the acquisition of any security, a money market fund other than a single state fund must not have invested more than:

*(1)* Five percent of its total assets in securities issued by the issuer of the security, provided, however, that such a fund may invest up to twenty-five percent of its total assets in the first tier securities of a single issuer for a period of up to three business days after the acquisition thereof; provided, further, that the fund may not invest in the securities of more than one issuer in accordance with the foregoing proviso in this paragraph at any time; and

*(2)* Ten percent of its total assets in securities issued by or subject to demand features or guarantees from the institution that issued the demand feature or guarantee.

(B) *Single state funds.* Immediately after the acquisition of any security, a single state fund must not have invested:

*(1)* With respect to seventy-five percent of its total assets, more than five percent of its total assets in securities issued by the issuer of the security; and

*(2)* With respect to all of its total assets, more than ten percent of its total assets in securities issued by or subject to demand features or guarantees from the institution that issued the demand feature or guarantee.

(C) *Second tier securities.* Immediately after the acquisition of any second tier security, a money market fund must not have invested more than one half of one percent of its total assets in the second tier securities of any single issuer, and must not have invested more than 2.5 percent of its total assets in second tier securities issued by or subject to demand features or guarantees from the institution that issued the demand feature or guarantee.

(ii) *Issuer diversification calculations.* For purposes of making calculations under paragraph (d)(3)(i) of this section:

(A) *Repurchase agreements.* The acquisition of a repurchase agreement may be deemed to be an acquisition of the underlying securities, provided the obligation of the seller to repurchase the securities from the money market fund is collateralized fully *and the fund's board of directors has evaluated the seller's creditworthiness.*

(B) *Refunded securities.* The acquisition of a refunded security shall be deemed to be an acquisition of the escrowed government securities.

(C) *Conduit securities.* A conduit security shall be deemed to be issued by the person (other than the municipal issuer) ultimately responsible for payments of interest and principal on the security.

(D) *Asset-backed securities.*

*(1) General.* An asset-backed security acquired by a fund (''primary ABS'') shall be deemed to be issued by the special purpose entity that issued the asset-backed security, provided, however:

(*i*) *Holdings of primary ABS.* Any person whose obligations constitute ten percent or more of the principal amount of the qualifying assets of the primary ABS (''ten percent obligor'') shall be deemed to be an issuer of the portion of the primary ABS such obligations represent; and

(*ii*) *Holdings of secondary ABS.* If a ten percent obligor of a primary ABS is itself a special purpose entity issuing asset-backed securities (''secondary ABS''), any ten percent obligor of such secondary ABS also shall be deemed to be an issuer of the portion of the primary ABS that such ten percent obligor represents.

*(2) Restricted special purpose entities.* A ten percent obligor with respect to a primary or secondary ABS shall not be deemed to have issued any portion of the assets of a primary ABS as provided in paragraph (d)(3)(ii)(D)*(1)* of this section if that ten percent obligor is itself a special purpose entity issuing asset-backed securities (''restricted special purpose entity''), and the securities that it issues (other than securities issued to a company that controls, or is controlled by or under common control with, the restricted special purpose entity and which is not itself a special purpose entity issuing asset-backed securities) are held by only one other special purpose entity.

*(3) Demand features and guarantees.* In the case of a ten percent obligor deemed to be an issuer, the fund must satisfy the diversification requirements of paragraphs (d)(3)(iii) of this section with respect to any demand feature or guarantee to which the ten percent obligor's obligations are subject.

(E) *Shares of other money market funds.* A money market fund that acquires shares issued by another money market fund in an amount that would otherwise be prohibited by paragraph (d)(3)(i) of this section shall nonetheless be deemed in compliance with this section if the board of directors of the acquiring money market fund reasonably believes that the fund in which it has invested is in compliance with this section.

(F) *Treatment of certain affiliated entities.* The money market fund, when calculating the amount of its total assets invested in securities issued by any particular issuer for purposes of paragraph (d)(3)(i) of this section, must treat as a single issuer two or more issuers of securities owned by the money market fund if one issuer controls the other, is controlled by the other issuer, or is under common control with the other issuer, provided that ''control'' for this purpose means ownership of more than 50 percent of the issuer's voting securities.

(iii) *Diversification rules for demand features and guarantees.* The money market fund must be diversified with respect to demand features and guarantees acquired by the fund as provided in paragraphs (d)(3)(iii) and (d)(3)(iv) of this section, other than with respect to a demand feature issued by the same institution that issued the underlying security, or with respect to a guarantee or demand feature that is itself a government security.

(A) *General.* Immediately after the acquisition of any demand feature or guarantee, any security subject to a demand feature or guarantee, or a security directly issued by the issuer of a demand feature or guarantee, a money market fund must not have invested more than ten percent of its total assets in securities issued by or subject to demand features or guarantees from the institution that issued the demand feature or guarantee.

(B) *Second tier demand features or guarantees.* Immediately after the acquisition of any demand feature or guarantee, any security subject to a demand feature or guarantee, a security directly issued by the issuer of a demand feature or guarantee, or a security after giving effect to the demand feature or guarantee, in all cases that is a second tier security, a money market fund must not have invested more than 2.5 percent of its total assets in securities issued by or subject to demand features or guarantees from the institution that issued the demand feature or guarantee.

(iv) *Demand feature and guarantee diversification calculations.*

(A) *Fractional demand features or guarantees.* In the case of a security subject to a demand feature or guarantee from an institution by which the institution guarantees a specified portion of the value of the security, the institution shall be deemed to guarantee the specified portion thereof.

(B) *Layered demand features or guarantees.* In the case of a security subject to demand features or guarantees from multiple institutions that have not limited the extent of their obligations as described in paragraph (d)(3)(iv)(A) of this section, each institution shall be deemed to have provided the demand feature or guarantee with respect to the entire principal amount of the security.

(v) *Diversification safe harbor.* A money market fund that satisfies the applicable diversification requirements of paragraphs (d)(3) and (e) of this section shall be deemed to have satisfied the diversification requirements of section 5(b)(1) of the Act (15 U.S.C. 80a–5(b)(1)) and the rules adopted thereunder.

(4) *Portfolio liquidity.* The money market fund must hold securities that are sufficiently liquid to meet reasonably foreseeable shareholder redemptions in light of the fund's obligations under section 22(e) of the Act (15 U.S.C. 80a–22(e)) and any commitments the fund has made to shareholders; provided, however, that:

(i) *Illiquid securities.* The money market fund may not acquire any illiquid security if, immediately after the acquisition, the money market fund would have invested more than five percent of its total assets in illiquid securities.

(ii) *Minimum daily liquidity requirement.* The money market fund may not acquire any security other than a daily liquid asset if, immediately after the acquisition, the fund would have invested less than ten percent of its total assets in daily liquid assets. This provision does not apply to tax exempt funds.

(iii) *Minimum weekly liquidity requirement.* The money market fund may not acquire any security other than a weekly liquid asset if, immediately after the acquisition, the fund would have invested less than thirty percent of its total assets in weekly liquid assets.

(e) *Demand features and guarantees not relied upon.* If the fund's board of directors has determined that the fund is not relying on a demand feature or guarantee to determine the quality (pursuant to paragraph (d)(2) of this section), or maturity (pursuant to paragraph (i) of this section), or liquidity of a portfolio security (pursuant to paragraph (d)(4) of this section), and maintains a record of this determination (pursuant to paragraphs (g)(3) and (h)(7) of this section), then the fund may disregard such demand feature or guarantee for all purposes of this section.

(f) *Downgrades, defaults and other events.*

(1) *Downgrades.*

(i) *General.* Upon the occurrence of either of the events specified in paragraphs (f)(1)(i)(A) and (B) of this section with respect to a portfolio security, the board of directors of the money market fund shall reassess promptly whether such security continues to present minimal credit risks and shall cause the fund to take such action as the board of directors determines is in the best interests of the money market fund:

(A) A portfolio security of a money market fund ceases to be a first tier security (either because it no longer has the highest rating from the requisite NRSROs or, in the case of an unrated security, the board of directors of the money market fund determines that it is no longer of comparable quality to a first tier security); and

(B) The money market fund's investment adviser (or any person to whom the fund's board of directors has delegated portfolio management responsibilities) becomes aware that any unrated security or second tier security held by the money market fund has, since the security was acquired by the fund, been given a rating by a designated NRSRO below the designated NRSRO's second highest short-term rating category.

(ii) *Securities to be disposed of.* The reassessments required by paragraph (f)(1)(i) of this section shall not be required if the fund disposes of the security (or it matures) within five business days of the specified event and, in the case of events specified in paragraph (f)(1)(i)(B) of this section, the board is subsequently notified of the adviser's actions.

(iii) *Special rule for certain securities subject to demand features.* In the event that after giving effect to a rating downgrade, more than 2.5 percent of the fund's total assets are invested in securities issued by or subject to demand features from a single institution that are second tier securities, the fund shall reduce its investment in securities issued by or subject to demand features from that institution to no more than 2.5 percent of its total assets by exercising the demand features at the next succeeding exercise date(s), absent a finding by the board of directors that disposal of the portfolio security would not be in the best interests of the money market fund.

(2) *Defaults and other events.* Upon the occurrence of any of the events specified in paragraphs (f)(2)(i) through (iv) of this section with respect to a portfolio security, the money market fund shall dispose of such security as soon as practicable consistent with achieving an orderly disposition of the security, by sale, exercise of any demand feature or otherwise, absent a finding by the board of directors that disposal of the portfolio security would not be in the best interests of the money market fund (which determination may take into account, among other factors, market conditions that could affect the orderly disposition of the portfolio security):

(i) The default with respect to a portfolio security (other than an immaterial default unrelated to the financial condition of the issuer);

(ii) A portfolio security ceases to be an eligible security;

(iii) A portfolio security has been determined to no longer present minimal credit risks; or

(iv) An event of insolvency occurs with respect to the issuer of a portfolio security or the provider of any demand feature or guarantee.

(3) *Notice to the Commission.* The money market fund must notify the Commission of the occurrence of certain material events, as specified in Form N–CR (§ 274.222 of this chapter).

(4) *Defaults for purposes of paragraphs (f)(2) and (3) of this section.* For purposes of paragraphs (f)(2) and (3) of this section, an instrument subject to a demand feature or guarantee shall not be deemed to be in default (and an event of insolvency with respect to the security shall not be deemed to have occurred) if:

(i) In the case of an instrument subject to a demand feature, the demand feature has been exercised and the fund has recovered either the principal amount or the amortized cost of the instrument, plus accrued interest;

(ii) The provider of the guarantee is continuing, without protest, to make payments as due on the instrument; or

(iii) The provider of a guarantee with respect to an asset-backed security pursuant to paragraph (a)(16)(ii) of this section is continuing, without protest, to provide credit, liquidity or other support as necessary to permit the asset-backed security to make payments as due.

(g) *Required procedures.* The money market fund's board of directors must adopt written procedures including the following:

(1) *General.* In supervising the money market fund's operations and delegating special responsibilities involving portfolio management to the money market fund's investment adviser, the money market fund's board of directors, as a particular responsibility within the overall duty of care owed to its shareholders, must establish written procedures reasonably designed, taking

into account current market conditions, to achieve the fund's investment objectives of earning short-term yields, consistent with the preservation of capital and, for a money market that relies on the exemptions provided by paragraph (c)(2) or (c)(3) of this section, to assure to the extent reasonably practicable that the money market fund's price per share, as computed for the purpose of distribution, redemption and repurchase, rounded to the nearest one percent, will not deviate from the stable price established by the board of directors.

(2) *Securities for which maturity is determined by reference to demand features.* In the case of a security for which maturity is determined by reference to a demand feature, written procedures shall require ongoing review of the security's continued minimal credit risks, and that review must be based on, among other things, financial data for the most recent fiscal year of the issuer of the demand feature and, in the case of a security subject to a conditional demand feature, the issuer of the security whose financial condition must be monitored under paragraph (d)(2)(iv) of this section, whether such data is publicly available or provided under the terms of the security's governing documentation.

(3) *Securities subject to demand features or guarantees.* In the case of a security subject to one or more demand features or guarantees that the fund's board of directors has determined that the fund is not relying on to determine the quality (pursuant to paragraph (d)(2) of this section), maturity (pursuant to paragraph (i) of this section) or liquidity (pursuant to paragraph (d)(4) of this section) of the security subject to the demand feature or guarantee, written procedures must require periodic evaluation of such determination.

(4) *Adjustable rate securities without demand features.* In the case of a variable rate or floating rate security that is not subject to a demand feature and for which maturity is determined pursuant to paragraph (i)(1), (i)(2) or (i)(4) of this section, written procedures shall require periodic review of whether the interest rate formula, upon readjustment of its interest rate, can reasonably be expected to cause the security to have a market value that approximates its amortized cost value.

(5) *Ten percent obligors of asset-backed securities.* In the case of an asset-backed security, written procedures must require the fund to periodically determine the number of ten percent obligors (as that term is used in paragraph (d)(3)(ii)(D) of this section) deemed to be the issuers of all or a portion of the asset-backed security for purposes of paragraph (d)(3)(ii)(D) of this section; provided, however, written procedures need not require periodic determinations with respect to any asset-backed security that a fund's board of directors has determined, at the time of acquisition, will not have, or is unlikely to have, ten percent obligors that are deemed to be issuers of all or a portion of that asset-backed security for purposes of paragraph (d)(3)(ii)(D) of this section, and maintains a record of this determination.

(6) *Asset-backed securities not subject to guarantees.* In the case of an asset-backed security for which the fund's board of directors has determined that the fund is not relying on the sponsor's financial strength or its ability or willingness to provide liquidity, credit or other support in connection with the asset-backed security to determine the quality (pursuant to paragraph (d)(2) of this section) or liquidity (pursuant to paragraph (d)(4) of this section) of the asset-backed security, written procedures must require periodic evaluation of such determination.

(7) *Stress Testing.* Written procedures must provide for:

*(i)* The periodic testing, at such intervals as the board of directors determines appropriate and reasonable in light of current market conditions, of the money market fund's ability to have invested at least fifteen percent of its total assets in weekly liquid assets and, in the case of a money market fund relying on the exemptions provided by paragraph (c)(2) or (3) of this section, the fund's ability to maintain the stable price per share established by the board of directors for the purpose of distribution, redemption, and repurchase, based upon specified hypothetical events that include, but are not limited to:

(A) Increases in the general level of short-term interest rates;

(B) An increase in shareholder redemptions, together with an assessment of how the fund would meet the redemptions, taking into consideration assumptions regarding the relative liquidity of the fund's portfolio securities, the prices for which portfolio securities could be sold, the fund's historical experience meeting redemption requests, and any other relevant factors;

(C) A downgrade or default of portfolio securities, and the effects these events could have on other securities held by the fund;

(D) The widening or narrowing of spreads among the indexes to which interest rates of portfolio securities are tied;

(E) Other movements in interest rates that may affect the fund's portfolio securities, such as parallel and non-parallel shifts in the yield curve; and

(F) Combinations of these and any other events the adviser deems relevant, assuming a positive correlation of risk factors (*e.g.,* assuming that a security default likely will be followed by increased redemptions) and taking into consideration the extent to which the fund's portfolio securities are correlated such that adverse events affecting a given security are likely to also affect one or more other securities (*e.g.,* a consideration of whether issuers in the same or related industries or geographic regions would be affected by adverse events affecting issuers in the same industry or geographic region).

(ii) A report on the results of such testing to be provided to the board of directors at its next regularly scheduled meeting (or sooner, if appropriate in light of the results), which report must include:

(A) The date(s) on which the testing was performed and the magnitude of each hypothetical event that would cause the money market fund to have invested less than fifteen percent of its total assets in weekly liquid assets and, in the case of a money market fund relying on the exemptions provided by paragraph (c)(2) or (3) of this section, that would cause the fund's price per share for purposes of distribution, redemption and repurchase to deviate from the stable price per share established by the board of directors; and

(B) An assessment by the fund's adviser of the fund's ability to withstand the events (and concurrent occurrences of those events) that are reasonably likely to occur within the following year, including such information as may reasonably be necessary for the board of directors to evaluate the stress testing conducted by the adviser and the results of the testing.

(h) *Recordkeeping and reporting.*

(1) *Written procedures.* For a period of not less than six years following the replacement of such procedures with new procedures (the first two years in an easily accessible place), a written copy of the procedures (and any modifications thereto) described in paragraphs (g) and (j) of this section must be maintained and preserved.

(2) *Board considerations and actions.* For a period of not less than six years (the first two years in an easily accessible place) a written record must be maintained and preserved of the board of directors' considerations and actions taken in connection with the discharge of its responsibilities, as set

forth in this section, to be included in the minutes of the board of directors' meetings.

(3) *Credit risk analysis.* For a period of not less than three years from the date that the credit risks of a portfolio security were most recently reviewed, a written record of the determination that a portfolio security presents minimal credit risks and the designated NRSRO ratings (if any) used to determine the status of the security as an eligible security, first tier security or second tier security shall be maintained and preserved in an easily accessible place.

(4) *Determinations with respect to adjustable rate securities.* For a period of not less than three years from the date when the assessment was most recently made, a written record must be preserved and maintained, in an easily accessible place, of the determination required by paragraph (g)(4) of this section (that a variable rate or floating rate security that is not subject to a demand feature and for which maturity is determined pursuant to paragraph (i)(1), (i)(2) or (i)(4) of this section can reasonably be expected, upon readjustment of its interest rate at all times during the life of the instrument, to have a market value that approximates its amortized cost).

(5) *Determinations with respect to asset-backed securities.* For a period of not less than three years from the date when the determination was most recently made, a written record must be preserved and maintained, in an easily accessible place, of the determinations required by paragraph (g)(5) of this section (the number of ten percent obligors (as that term is used in paragraph (d)(3)(ii)(D) of this section) deemed to be the issuers of all or a portion of the asset-backed security for purposes of paragraph (d)(3)(ii)(D) of this section). The written record must include:

(i) The identities of the ten percent obligors (as that term is used in paragraph (d)(3)(ii)(D) of this section), the percentage of the qualifying assets constituted by the securities of each ten percent obligor and the percentage of the fund's total assets that are invested in securities of each ten percent obligor; and

(ii) Any determination that an asset-backed security will not have, or is unlikely to have, ten percent obligors deemed to be issuers of all or a portion of that asset-backed security for purposes of paragraph (d)(3)(ii)(D) of this section.

(6) *Evaluations with respect to asset-backed securities not subject to guarantees.* For a period of not less than three years from the date when the evaluation was most recently made, a written record must be preserved and maintained, in an easily accessible place, of the evaluation required by paragraph (g)(6) of this section (regarding asset-backed securities not subject to guarantees).

(7) *Evaluations with respect to securities subject to demand features or guarantees.* For a period of not less than three years from the date when the evaluation was most recently made, a written record must be preserved and maintained, in an easily accessible place, of the evaluation required by paragraph (g)(3) of this section (regarding securities subject to one or more demand features or guarantees).

(8) *Reports with respect to stress testing.* For a period of not less than six years (the first two years in an easily accessible place), a written copy of the report required under paragraph (g)(7)(ii) of this section must be maintained and preserved.

(9) *Inspection of records.* The documents preserved pursuant to paragraph (h) of this section are subject to inspection by the Commission in accordance with section 31(b) of the Act (15 U.S.C. 80a–30(b)) as if such documents were records required to be maintained pursuant to rules adopted under section 31(a) of the Act (15 U.S.C. 80a–30(a)).

(10) *Web site disclosure of portfolio holdings and other fund information.* The money market fund must post prominently on its Web site the following information:

(i) For a period of not less than six months, beginning no later than the fifth business day of the month, a schedule of its investments, as of the last business day or subsequent calendar day of the preceding month, that includes the following information:

(A) With respect to the money market fund and each class of redeemable shares thereof:

*(1)* The WAM; and

*(2)* The WAL.

(B) With respect to each security held by the money market fund:

*(1)* Name of the issuer;

*(2)* Category of investment (indicate the category that most closely identifies the instrument from among the following: U.S. Treasury Debt; U.S. Government Agency Debt; Non U.S. Sovereign Debt; Non U.S. Sub-Sovereign Debt; Variable Rate Demand Note; Other Municipal Debt; Financial Company Commercial Paper; Asset-Backed Commercial Paper; Other Asset-Backed Security; Non-Financial Company Commercial Paper; Collateralized Commercial Paper; Certificate of Deposit (including Time Deposits and Euro Time Deposits); Structured Investment Vehicle Note; Other Note; U.S. Treasury Repurchase Agreement; Government Agency Repurchase Agreement; Other Repurchase Agreement; Insurance Company Funding Agreement; Investment Company; Other Instrument);

*(3)* CUSIP number (if any);

*(4)* Principal amount;

*(5)* The maturity date determined by taking into account the maturity shortening provisions in paragraph (i) of this section (*i.e.,* the maturity date used to calculate WAM under paragraph (d)(1)(ii) of this section);

*(6)* The maturity date determined without reference to the exceptions in paragraph (i) of this section regarding interest rate readjustments (*i.e.,* the maturity used to calculate WAL under paragraph (d)(1)(iii) of this section);

*(7)* Coupon or yield; and

*(8)* Value.

(ii) A schedule, chart, graph, or other depiction, which must be updated each business day as of the end of the preceding business day, showing, as of the end of each business day during the preceding six months:

(A) The percentage of the money market fund's total assets invested in daily liquid assets;

(B) The percentage of the money market fund's total assets invested in weekly liquid assets; and

(C) The money market fund's net inflows or outflows.

(iii) A schedule, chart, graph, or other depiction showing the money market fund's net asset value per share (which each fund relying on the exemption provided by paragraph (c)(2) or (c)(3) of this section must calculate based on current market factors before applying the penny rounding method), rounded to the fourth decimal place in the case of funds with a $1.0000 share price or an equivalent level of accuracy for funds with a different share price (*e.g.,* $10.000 or $100.00 per share), as of the end of each business day during the preceding six months, which must be updated each business day as of the end of the preceding business day.

(iv) A link to a Web site of the Securities and Exchange Commission where a user may obtain the most recent 12 months of publicly available information filed by the money market fund pursuant to § 270.30b1–7.

(v) For a period of not less than one year, beginning no later than the first business day following the occurrence of any event specified in Part C of Form N–CR (§ 274.222 of this chapter), the same information that the money market fund is required to report to the

Commission on Part C of Form N–CR concerning such event.

(i) *Maturity of portfolio securities.* For purposes of this section, the maturity of a portfolio security shall be deemed to be the period remaining (calculated from the trade date or such other date on which the fund's interest in the security is subject to market action) until the date on which, in accordance with the terms of the security, the principal amount must unconditionally be paid, or in the case of a security called for redemption, the date on which the redemption payment must be made, except as provided in paragraphs (i)(1) through (i)(8) of this section:

(1) *Adjustable rate government securities.* A government security that is a variable rate security where the variable rate of interest is readjusted no less frequently than every 397 calendar days shall be deemed to have a maturity equal to the period remaining until the next readjustment of the interest rate. A government security that is a floating rate security shall be deemed to have a remaining maturity of one day.

(2) *Short-term variable rate securities.* A variable rate security, the principal amount of which, in accordance with the terms of the security, must unconditionally be paid in 397 calendar days or less shall be deemed to have a maturity equal to the earlier of the period remaining until the next readjustment of the interest rate or the period remaining until the principal amount can be recovered through demand.

(3) *Long-term variable rate securities.* A variable rate security, the principal amount of which is scheduled to be paid in more than 397 calendar days, that is subject to a demand feature, shall be deemed to have a maturity equal to the longer of the period remaining until the next readjustment of the interest rate or the period remaining until the principal amount can be recovered through demand.

(4) *Short-term floating rate securities.* A floating rate security, the principal amount of which, in accordance with the terms of the security, must unconditionally be paid in 397 calendar days or less shall be deemed to have a maturity of one day, except for purposes of determining WAL under paragraph (d)(1)(iii) of this section, in which case it shall be deemed to have a maturity equal to the period remaining until the principal amount can be recovered through demand.

(5) *Long-term floating rate securities.* A floating rate security, the principal amount of which is scheduled to be paid in more than 397 calendar days, that is subject to a demand feature, shall be deemed to have a maturity equal to the period remaining until the principal amount can be recovered through demand.

(6) *Repurchase agreements.* A repurchase agreement shall be deemed to have a maturity equal to the period remaining until the date on which the repurchase of the underlying securities is scheduled to occur, or, where the agreement is subject to demand, the notice period applicable to a demand for the repurchase of the securities.

(7) *Portfolio lending agreements.* A portfolio lending agreement shall be treated as having a maturity equal to the period remaining until the date on which the loaned securities are scheduled to be returned, or where the agreement is subject to demand, the notice period applicable to a demand for the return of the loaned securities.

(8) *Money market fund securities.* An investment in a money market fund shall be treated as having a maturity equal to the period of time within which the acquired money market fund is required to make payment upon redemption, unless the acquired money market fund has agreed in writing to provide redemption proceeds to the investing money market fund within a shorter time period, in which case the maturity of such investment shall be deemed to be the shorter period.

(j) *Delegation.* The money market fund's board of directors may delegate to the fund's investment adviser or officers the responsibility to make any determination required to be made by the board of directors under this section other than the determinations required by paragraphs (a)(10)(i) (designation of NRSROs), (f)(2) (defaults and other events), (g)(1) (general required procedures), and (g)(7) (stress testing procedures) of this section.

(1) *Written guidelines.* The board of directors must establish and periodically review written guidelines (including guidelines for determining whether securities present minimal credit risks as required in paragraph (d)(2) of this section) and procedures under which the delegate makes such determinations.

(2) *Oversight.* The board of directors must take any measures reasonably necessary (through periodic reviews of fund investments and the delegate's procedures in connection with investment decisions and prompt review of the adviser's actions in the event of the default of a security or event of insolvency with respect to the issuer of the security or any guarantee or demand feature to which it is subject that requires notification of the Commission under paragraph (f)(3) of this section by reference to Form N–CR (§ 274.222 of this chapter)) to assure that the guidelines and procedures are being followed.

**Alternative 2**

**§ 270.2a–7 Money market funds.**

(a) *Definitions.*

(1) *Acquisition* (or *Acquire*) means any purchase or subsequent rollover (but does not include the failure to exercise a demand feature).

(2) *Amortized cost* means the value of a security at the fund's acquisition cost as adjusted for amortization of premium or accretion of discount rather than at the security's value based on current market factors.

(3) *Asset-backed security* means a fixed income security (other than a government security) issued by a special purpose entity (as defined in this paragraph (a)(3)), substantially all of the assets of which consist of qualifying assets (as defined in this paragraph (a)(3)). *Special purpose entity* means a trust, corporation, partnership or other entity organized for the sole purpose of issuing securities that entitle their holders to receive payments that depend primarily on the cash flow from qualifying assets, but does not include a registered investment company. *Qualifying assets* means financial assets, either fixed or revolving, that by their terms convert into cash within a finite time period, plus any rights or other assets designed to assure the servicing or timely distribution of proceeds to security holders.

(4) *Business day* means any day, other than Saturday, Sunday, or any customary business holiday.

(5) *Collateralized fully* has the same meaning as defined in § 270.5b–3(c)(1) except that § 270.5b–3(c)(1)(iv)(C) and (D) shall not apply.

(6) *Conditional demand feature* means a demand feature that is not an unconditional demand feature. A conditional demand feature is not a guarantee.

(7) *Conduit security* means a security issued by a municipal issuer (as defined in this paragraph (a)(7)) involving an arrangement or agreement entered into, directly or indirectly, with a person other than a municipal issuer, which arrangement or agreement provides for or secures repayment of the security. *Municipal issuer* means a state or territory of the United States (including the District of Columbia), or any political subdivision or public instrumentality of a state or territory of the United States. A conduit security does not include a security that is:

(i) Fully and unconditionally guaranteed by a municipal issuer;

(ii) Payable from the general revenues of the municipal issuer or other municipal issuers (other than those revenues derived from an agreement or arrangement with a person who is not a municipal issuer that provides for or secures repayment of the security issued by the municipal issuer);

(iii) Related to a project owned and operated by a municipal issuer; or

(iv) Related to a facility leased to and under the control of an industrial or commercial enterprise that is part of a public project which, as a whole, is owned and under the control of a municipal issuer.

(8) *Daily liquid assets* means:

(i) Cash;

(ii) Direct obligations of the U.S. Government;

(iii) Securities that will mature, as determined without reference to the exceptions in paragraph (i) of this section regarding interest rate readjustments, or are subject to a demand feature that is exercisable and payable, within one business day; or

(iv) Amounts receivable and due unconditionally within one business day on pending sales of portfolio securities.

(9) *Demand feature* means a feature permitting the holder of a security to sell the security at an exercise price equal to the approximate amortized cost of the security plus accrued interest, if any, at the later of the time of exercise or the settlement of the transaction, paid within 397 calendar days of exercise.

(10) *Designated NRSRO* means any one of at least four nationally recognized statistical rating organizations, as that term is defined in section 3(a)(62) of the Securities Exchange Act of 1934 (15 U.S.C. 78c(a)(62)), that:

(i) The money market fund's board of directors:

(A) Has designated as an NRSRO whose credit ratings with respect to any obligor or security or particular obligors or securities will be used by the fund to determine whether a security is an eligible security; and

(B) Determines at least once each calendar year issues credit ratings that are sufficiently reliable for such use;

(ii) Is not an ''affiliated person,'' as defined in section 2(a)(3)(C) of the Act (15 U.S.C. 80a–2(a)(3)(C)), of the issuer of, or any insurer or provider of credit support for, the security; and

(iii) The fund discloses in its statement of additional information is a designated NRSRO, including any limitations with respect to the fund's use of such designation.

(11) *Eligible security* means:

(i) A rated security with a remaining maturity of 397 calendar days or less that has received a rating from the requisite NRSROs in one of the two highest short-term rating categories (within which there may be sub-categories or gradations indicating relative standing); or

(ii) An unrated security that is of comparable quality to a security meeting the requirements for a rated security in paragraph (a)(11)(i) of this section, as determined by the money market fund's board of directors; provided, however, that: a security that at the time of issuance had a remaining maturity of more than 397 calendar days but that has a remaining maturity of 397 calendar days or less and that is an unrated security is not an eligible security if the security has received a long-term rating from any designated NRSRO that is not within the designated NRSRO's three highest long-term ratings categories (within which there may be sub-categories or gradations indicating relative standing), unless the security has received a long-term rating from the requisite NRSROs in one of the three highest rating categories.

(iii) In addition, in the case of a security that is subject to a demand feature or guarantee:

(A) The guarantee has received a rating from a designated NRSRO or the guarantee is issued by a guarantor that has received a rating from a designated NRSRO with respect to a class of debt obligations (or any debt obligation within that class) that is comparable in priority and security to the guarantee, unless:

(*1*) The guarantee is issued by a person that, directly or indirectly, controls, is controlled by or is under common control with the issuer of the security subject to the guarantee (other than a sponsor of a special purpose entity with respect to an asset-backed security);

(*2*) The security subject to the guarantee is a repurchase agreement that is collateralized fully; or

(*3*) The guarantee is itself a government security; and

(B) The issuer of the demand feature or guarantee, or another institution, has undertaken promptly to notify the holder of the security in the event the demand feature or guarantee is substituted with another demand feature or guarantee (if such substitution is permissible under the terms of the demand feature or guarantee).

(12) *Event of insolvency* has the same meaning as defined in § 270.5b–3(c)(2).

(13) *First tier security* means any eligible security that:

(i) Is a rated security that has received a short-term rating from the requisite NRSROs in the highest short-term rating category for debt obligations (within which there may be sub-categories or gradations indicating relative standing);

(ii) Is an unrated security that is of comparable quality to a security meeting the requirements for a rated security in paragraph (a)(13)(i) of this section, as determined by the fund's board of directors;

(iii) Is a security issued by a registered investment company that is a money market fund; or

(iv) Is a government security.

(14) *Floating rate security* means a security the terms of which provide for the adjustment of its interest rate whenever a specified interest rate changes and that, at any time until the final maturity of the instrument or the period remaining until the principal amount can be recovered through demand, can reasonably be expected to have a market value that approximates its amortized cost.

(15) *Government security* has the same meaning as defined in section 2(a)(16) of the Act (15 U.S.C. 80a–2(a)(16)).

(16) *Guarantee:*

(i) Means an unconditional obligation of a person other than the issuer of the security to undertake to pay, upon presentment by the holder of the guarantee (if required), the principal amount of the underlying security plus accrued interest when due or upon default, or, in the case of an unconditional demand feature, an obligation that entitles the holder to receive upon the later of exercise or the settlement of the transaction the approximate amortized cost of the underlying security or securities, plus accrued interest, if any. A guarantee includes a letter of credit, financial guaranty (bond) insurance, and an unconditional demand feature (other than an unconditional demand feature provided by the issuer of the security).

(ii) The sponsor of a special purpose entity with respect to an asset-backed security shall be deemed to have provided a guarantee with respect to the entire principal amount of the asset-backed security for purposes of this section, except paragraphs (a)(11)(iii) (definition of eligible security), (d)(2)(iii) (credit substitution), (d)(3)(iv)(A) (fractional guarantees) and (e) (guarantees not relied on) of this section, unless the money market fund's board of directors has determined that the fund is not relying on the sponsor's financial strength or its ability or willingness to provide liquidity, credit or other support to determine the quality (pursuant to paragraph (d)(2) of this section) or liquidity (pursuant to paragraph (d)(4) of this section) of the

asset-backed security, and maintains a record of this determination (pursuant to paragraphs (g)(6) and (h)(6) of this section).

(17) *Guarantee issued by a non-controlled person* means a guarantee issued by:

(i) A person that, directly or indirectly, does not control, and is not controlled by or under common control with the issuer of the security subject to the guarantee (*control* has the same meaning as defined in section 2(a)(9) of the Act) (15 U.S.C. 80a–2(a)(9)); or

(ii) A sponsor of a special purpose entity with respect to an asset-backed security if the money market fund's board of directors has made the findings described in paragraph (g)(6) of this section.

(18) *Illiquid security* means a security that cannot be sold or disposed of in the ordinary course of business within seven calendar days at approximately the value ascribed to it by the fund.

(19) *Penny-rounding method* of pricing means the method of computing an investment company's price per share for purposes of distribution, redemption and repurchase whereby the current net asset value per share is rounded to the nearest one percent.

(20) *Rated security* means a security that meets the requirements of paragraphs (a)(20)(i) or (ii) of this section, in each case subject to paragraph (a)(20)(iii) of this section:

(i) The security has received a short-term rating from a designated NRSRO, or has been issued by an issuer that has received a short-term rating from a designated NRSRO with respect to a class of debt obligations (or any debt obligation within that class) that is comparable in priority and security with the security; or

(ii) The security is subject to a guarantee that has received a short-term rating from a designated NRSRO, or a guarantee issued by a guarantor that has received a short-term rating from a designated NRSRO with respect to a class of debt obligations (or any debt obligation within that class) that is comparable in priority and security with the guarantee; but

(iii) A security is not a rated security if it is subject to an external credit support agreement (including an arrangement by which the security has become a refunded security) that was not in effect when the security was assigned its rating, unless the security has received a short-term rating reflecting the existence of the credit support agreement as provided in paragraph (a)(20)(i) of this section, or the credit support agreement with respect to the security has received a short-term rating as provided in paragraph (a)(20)(ii) of this section.

(21) *Refunded security* has the same meaning as defined in § 270.5b–3(c)(4).

(22) *Requisite NRSROs* means:

(i) Any two designated NRSROs that have issued a rating with respect to a security or class of debt obligations of an issuer; or

(ii) If only one designated NRSRO has issued a rating with respect to such security or class of debt obligations of an issuer at the time the fund acquires the security, that designated NRSRO.

(23) *Second tier security* means any eligible security that is not a first tier security.

(24) *Single state fund* means a tax exempt fund that holds itself out as seeking to maximize the amount of its distributed income that is exempt from the income taxes or other taxes on investments of a particular state and, where applicable, subdivisions thereof.

(25) *Tax exempt fund* means any money market fund that holds itself out as distributing income exempt from regular federal income tax.

(26) *Total assets* means the total value of the money market fund's assets, as defined in section 2(a)(41) of the Act (15 U.S.C. 80a–2(a)(41)) and the rules thereunder.

(27) *Unconditional demand feature* means a demand feature that by its terms would be readily exercisable in the event of a default in payment of principal or interest on the underlying security or securities.

(28) *United States dollar-denominated* means, with reference to a security, that all principal and interest payments on such security are payable to security holders in United States dollars under all circumstances and that the interest rate of, the principal amount to be repaid, and the timing of payments related to such security do not vary or float with the value of a foreign currency, the rate of interest payable on foreign currency borrowings, or with any other interest rate or index expressed in a currency other than United States dollars.

(29) *Unrated security* means a security that is not a rated security.

(30) *Variable rate security* means a security the terms of which provide for the adjustment of its interest rate on set dates (such as the last day of a month or calendar quarter) and that, upon each adjustment until the final maturity of the instrument or the period remaining until the principal amount can be recovered through demand, can reasonably be expected to have a market value that approximates its amortized cost.

(31) *Weekly liquid assets* means:

(i) Cash;

(ii) Direct obligations of the U.S. Government;

(iii) Government securities that are issued by a person controlled or supervised by and acting as an instrumentality of the government of the United States pursuant to authority granted by the Congress of the United States that:

(A) Are issued at a discount to the principal amount to be repaid at maturity without provision for the payment of interest; and

(B) Have a remaining maturity date of 60 days or less;

(iv) Securities that will mature, as determined without reference to the exceptions in paragraph (i) of this section regarding interest rate readjustments, or are subject to a demand feature that is exercisable and payable, within five business days; or

(v) Amounts receivable and due unconditionally within five business days on pending sales of portfolio securities.

(b) Holding out and use of names and titles.

(1) It shall be an untrue statement of material fact within the meaning of section 34(b) of the Act (15 U.S.C. 80a–33(b)) for a registered investment company, in any registration statement, application, report, account, record, or other document filed or transmitted pursuant to the Act, including any advertisement, pamphlet, circular, form letter, or other sales literature addressed to or intended for distribution to prospective investors that is required to be filed with the Commission by section 24(b) of the Act (15 U.S.C. 80a–24(b)), to hold itself out to investors as a money market fund or the equivalent of a money market fund, unless such registered investment company complies with this section.

(2) It shall constitute the use of a materially deceptive or misleading name or title within the meaning of section 35(d) of the Act (15 U.S.C. 80a–34(d)) for a registered investment company to adopt the term ''money market'' as part of its name or title or the name or title of any redeemable securities of which it is the issuer, or to adopt a name that suggests that it is a money market fund or the equivalent of a money market fund, unless such registered investment company complies with this section.

(3) For purposes of paragraph (b)(2) of this section, a name that suggests that a registered investment company is a money market fund or the equivalent thereof includes one that uses such terms as ''cash,'' ''liquid,'' ''money,'' ''ready assets'' or similar terms.

(c) *Share price calculations.* The current price per share, for purposes of distribution, redemption and repurchase, of any redeemable security issued by any registered investment company (''money market fund'' or ''fund''), notwithstanding the requirements of section 2(a)(41) of the Act (15 U.S.C. 80a–2(a)(41)) and of §§ 270.2a–4 and 270.22c–1, may be computed by use of the penny-rounding method; provided, however, that:

(1) *Board findings.* The board of directors of the money market fund must determine, in good faith, that it is in the best interests of the money market fund to maintain a stable price per share by virtue of the penny-rounding method.

(2) *Liquidity fees and temporary suspensions of redemptions.* Except as provided in paragraph (c)(2)(iii) of this section, and notwithstanding sections 22(e) and 27(i) of the Act (15 U.S.C. 80a–22(e) and 80a–27(i)) and § 270.22c–1:

(i) *Liquidity fees.* If, at the end of a business day, the money market fund has invested less than fifteen percent of its total assets in weekly liquid assets, the fund must institute a liquidity fee, effective as of the beginning of the next business day, as described in paragraphs (c)(2)(i)(A) and (B) of this section, unless the fund's board of directors, including a majority of the directors who are not interested persons of the fund, determines that imposing the fee is not in the best interest of the fund.

(A) *Amount of liquidity fee.* The liquidity fee shall be two percent of the value of shares redeemed unless the money market fund's board of directors, including a majority of the directors who are not interested persons of the fund, determines that a lower fee level is in the best interest of the fund. If a liquidity fee remains in effect for more than one business day, the board of directors, including a majority of the directors who are not interested persons of the fund, may vary the level of the liquidity fee (provided that the liquidity fee may not exceed two percent of the value of shares redeemed) if it determines that the new fee level is in the best interest of the fund, with the new fee level taking effect as of the beginning of the next business day.

(B) *Duration and application of liquidity fee.* Once imposed, a liquidity fee, which must be applied to all shares redeemed, shall remain in effect until the money market fund's board of directors, including a majority of the directors who are not interested persons of the fund, determines that imposing the liquidity fee is not in the best interest of the fund, provided that if, at the end of a business day, the money market fund has invested thirty percent or more of its total assets in weekly liquid assets, the fund must cease charging the liquidity fee, effective as of the beginning of the next business day.

(ii) *Temporary suspension of redemptions.* If, at the end of a business day, the money market fund has invested less than fifteen percent of its total assets in weekly liquid assets, the fund's board of directors, including a majority of the directors who are not interested persons of the fund, may determine to suspend the right of redemption temporarily, effective at the beginning of the next business day, if the board determines that doing so is in the best interest of the fund. The temporary suspension of redemptions may remain in effect until the fund's board of directors, including a majority of the directors who are not interested persons of the fund, determines to restore the right of redemption, provided that the fund must restore the right of redemption within thirty calendar days of suspending redemptions (or the next business day following such day) or on such earlier business day if, at the end of the preceding business day, the money market fund has invested thirty percent or more of its total assets in weekly liquid assets. The money market fund may not suspend the right of redemption pursuant to this paragraph for more than thirty days in any ninety-day period.

(iii) *Exemption for government money market funds.* A money market fund is not required to comply with paragraphs (c)(2)(i) and (ii) of this section if and so long as eighty percent or more of the money market fund's total assets are invested in cash, government securities, and/or repurchase agreements that are collateralized fully, but such a fund may choose not to rely on the exemption provided by this paragraph, and may impose liquidity fees and suspend redemptions temporarily, provided that the fund must then comply with paragraphs (c)(2)(i) and (ii) of this section and any other requirements that apply to liquidity fees and temporary suspensions of redemptions (*e.g.,* Item 4(b)(1)(ii) of Form N–1A (§ 274.11A of this chapter)).

(iv) *Variable contracts.* A variable insurance contract sold by a registered separate account funding variable insurance contracts or the sponsoring insurance company of such separate account may apply a liquidity fee or temporary suspension of redemptions pursuant to paragraph (c)(2) of this section to contract owners who allocate all or a portion of their contract value to a subaccount of the separate account that is either a money market fund or that invests all of its assets in shares of a money market fund.

(d) *Risk-limiting conditions.*

(1) *Portfolio maturity.* The money market fund must maintain a dollar-weighted average portfolio maturity appropriate to its objective of maintaining a stable price per share; provided, however, that the money market fund must not:

(i) Acquire any instrument with a remaining maturity of greater than 397 calendar days;

(ii) Maintain a dollar-weighted average portfolio maturity (''WAM'') that exceeds 60 calendar days; or

(iii) Maintain a dollar-weighted average portfolio maturity that exceeds 120 calendar days, determined without reference to the exceptions in paragraph (i) of this section regarding interest rate readjustments (''WAL'').

(2) *Portfolio quality.*

(i) *General.* The money market fund must limit its portfolio investments to those United States dollar-denominated securities that the fund's board of directors determines present minimal credit risks (which determination must be based on factors pertaining to credit quality in addition to any rating assigned to such securities by a designated NRSRO) and that are at the time of acquisition eligible securities.

(ii) *Second tier securities.* No money market fund may acquire a second tier security with a remaining maturity of greater than 45 calendar days, determined without reference to the exceptions in paragraph (i) of this section regarding interest rate readjustments. Immediately after the acquisition of any second tier security, a money market fund must not have invested more than three percent of its total assets in second tier securities.

(iii) *Securities subject to guarantees.* A security that is subject to a guarantee may be determined to be an eligible security or a first tier security based solely on whether the guarantee is an eligible security or first tier security, as the case may be.

(iv) *Securities subject to conditional demand features.* A security that is subject to a conditional demand feature (''underlying security'') may be determined to be an eligible security or a first tier security only if:

(A) The conditional demand feature is an eligible security or first tier security, as the case may be;

(B) At the time of the acquisition of the underlying security, the money market fund's board of directors has determined that there is minimal risk that the circumstances that would result

in the conditional demand feature not being exercisable will occur; and

*(1)* The conditions limiting exercise either can be monitored readily by the fund or relate to the taxability, under federal, state or local law, of the interest payments on the security; or

*(2)* The terms of the conditional demand feature require that the fund will receive notice of the occurrence of the condition and the opportunity to exercise the demand feature in accordance with its terms; and

(C) The underlying security or any guarantee of such security (or the debt securities of the issuer of the underlying security or guarantee that are comparable in priority and security with the underlying security or guarantee) has received either a short-term rating or a long-term rating, as the case may be, from the requisite NRSROs within the NRSROs' two highest short-term or long-term rating categories (within which there may be sub-categories or gradations indicating relative standing) or, if unrated, is determined to be of comparable quality by the money market fund's board of directors to a security that has received a rating from the requisite NRSROs within the NRSROs' two highest short-term or long-term rating categories, as the case may be.

(3) *Portfolio diversification.*

(i) *Issuer diversification.* The money market fund must be diversified with respect to issuers of securities acquired by the fund as provided in paragraphs (d)(3)(i) and (d)(3)(ii) of this section, other than with respect to government securities and securities subject to a guarantee issued by a non-controlled person.

(A) *Taxable and national funds.* Immediately after the acquisition of any security, a money market fund other than a single state fund must not have invested more than:

*(1)* Five percent of its total assets in securities issued by the issuer of the security, provided, however, that such a fund may invest up to twenty-five percent of its total assets in the first tier securities of a single issuer for a period of up to three business days after the acquisition thereof; provided, further, that the fund may not invest in the securities of more than one issuer in accordance with the foregoing proviso in this paragraph at any time; and

*(2)* Ten percent of its total assets in securities issued by or subject to demand features or guarantees from the institution that issued the demand feature or guarantee.

(B) *Single state funds.* Immediately after the acquisition of any security, a single state fund must not have invested:

*(1)* With respect to seventy-five percent of its total assets, more than five percent of its total assets in securities issued by the issuer of the security; and

*(2)* With respect to all of its total assets, more than ten percent of its total assets in securities issued by or subject to demand features or guarantees from the institution that issued the demand feature or guarantee.

(C) *Second tier securities.* Immediately after the acquisition of any second tier security, a money market fund must not have invested more than one half of one percent of its total assets in the second tier securities of any single issuer, and must not have invested more than 2.5 percent of its total assets in second tier securities issued by or subject to demand features or guarantees from the institution that issued the demand feature or guarantee.

(ii) *Issuer diversification calculations.* For purposes of making calculations under paragraph (d)(3)(i) of this section:

(A) *Repurchase agreements.* The acquisition of a repurchase agreement may be deemed to be an acquisition of the underlying securities, provided the obligation of the seller to repurchase the securities from the money market fund is collateralized fully and the fund's board of directors has evaluated the seller's creditworthiness.

(B) *Refunded securities.* The acquisition of a refunded security shall be deemed to be an acquisition of the escrowed government securities.

(C) *Conduit securities.* A conduit security shall be deemed to be issued by the person (other than the municipal issuer) ultimately responsible for payments of interest and principal on the security.

(D) *Asset-backed securities.*

*(1) General.* An asset-backed security acquired by a fund (''primary ABS'') shall be deemed to be issued by the special purpose entity that issued the asset-backed security, provided, however:

(*i*) *Holdings of primary ABS.* Any person whose obligations constitute ten percent or more of the principal amount of the qualifying assets of the primary ABS (''ten percent obligor'') shall be deemed to be an issuer of the portion of the primary ABS such obligations represent; and

(*ii*) *Holdings of secondary ABS.* If a ten percent obligor of a primary ABS is itself a special purpose entity issuing asset-backed securities (''secondary ABS''), any ten percent obligor of such secondary ABS also shall be deemed to be an issuer of the portion of the primary ABS that such ten percent obligor represents.

*(2) Restricted special purpose entities.* A ten percent obligor with respect to a primary or secondary ABS shall not be deemed to have issued any portion of the assets of a primary ABS as provided in paragraph (d)(3)(ii)(D)*(1)* of this section if that ten percent obligor is itself a special purpose entity issuing asset-backed securities (''restricted special purpose entity''), and the securities that it issues (other than securities issued to a company that controls, or is controlled by or under common control with, the restricted special purpose entity and which is not itself a special purpose entity issuing asset-backed securities) are held by only one other special purpose entity.

*(3) Demand features and guarantees.* In the case of a ten percent obligor deemed to be an issuer, the fund must satisfy the diversification requirements of paragraphs (d)(3)(iii) of this section with respect to any demand feature or guarantee to which the ten percent obligor's obligations are subject.

(E) *Shares of other money market funds.* A money market fund that acquires shares issued by another money market fund in an amount that would otherwise be prohibited by paragraph (d)(3)(i) of this section shall nonetheless be deemed in compliance with this section if the board of directors of the acquiring money market fund reasonably believes that the fund in which it has invested is in compliance with this section.

(F) *Treatment of certain affiliated entities.* The money market fund, when calculating the amount of its total assets invested in securities issued by any particular issuer for purposes of paragraph (d)(3)(i) of this section, must treat as a single issuer two or more issuers of securities owned by the money market fund if one issuer controls the other, is controlled by the other issuer, or is under common control with the other issuer, provided that ''control'' for this purpose means ownership of more than 50 percent of the issuer's voting securities.

(iii) *Diversification rules for demand features and guarantees.* The money market fund must be diversified with respect to demand features and guarantees acquired by the fund as provided in paragraphs (d)(3)(iii) and (d)(3)(iv) of this section, other than with respect to a demand feature issued by the same institution that issued the underlying security, or with respect to a guarantee or demand feature that is itself a government security.

(A) *General.* Immediately after the acquisition of any demand feature or

guarantee, any security subject to a demand feature or guarantee, or a security directly issued by the issuer of a demand feature or guarantee, a money market fund must not have invested more than ten percent of its total assets in securities issued by or subject to demand features or guarantees from the institution that issued the demand feature or guarantee.

(B) *Second tier demand features or guarantees.* Immediately after the acquisition of any demand feature or guarantee, any security subject to a demand feature or guarantee, a security directly issued by the issuer of a demand feature or guarantee, or a security after giving effect to the demand feature or guarantee, in all cases that is a second tier security, a money market fund must not have invested more than 2.5 percent of its total assets in securities issued by or subject to demand features or guarantees from the institution that issued the demand feature or guarantee.

(iv) *Demand feature and guarantee diversification calculations.*

(A) *Fractional demand features or guarantees.* In the case of a security subject to a demand feature or guarantee from an institution by which the institution guarantees a specified portion of the value of the security, the institution shall be deemed to guarantee the specified portion thereof.

(B) *Layered demand features or guarantees.* In the case of a security subject to demand features or guarantees from multiple institutions that have not limited the extent of their obligations as described in paragraph (d)(3)(iv)(A) of this section, each institution shall be deemed to have provided the demand feature or guarantee with respect to the entire principal amount of the security.

(v) *Diversification safe harbor.* A money market fund that satisfies the applicable diversification requirements of paragraphs (d)(3) and (e) of this section shall be deemed to have satisfied the diversification requirements of section 5(b)(1) of the Act (15 U.S.C. 80a–5(b)(1)) and the rules adopted thereunder.

(4) *Portfolio liquidity.* The money market fund must hold securities that are sufficiently liquid to meet reasonably foreseeable shareholder redemptions in light of the fund's obligations under section 22(e) of the Act (15 U.S.C. 80a–22(e)) and any commitments the fund has made to shareholders; provided, however, that:

(i) *Illiquid securities.* The money market fund may not acquire any illiquid security if, immediately after the acquisition, the money market fund would have invested more than five percent of its total assets in illiquid securities.

(ii) *Minimum daily liquidity requirement.* The money market fund may not acquire any security other than a daily liquid asset if, immediately after the acquisition, the fund would have invested less than ten percent of its total assets in daily liquid assets. This provision does not apply to tax exempt funds.

(iii) *Minimum weekly liquidity requirement.* The money market fund may not acquire any security other than a weekly liquid asset if, immediately after the acquisition, the fund would have invested less than thirty percent of its total assets in weekly liquid assets.

(e) *Demand features and guarantees not relied upon.* If the fund's board of directors has determined that the fund is not relying on a demand feature or guarantee to determine the quality (pursuant to paragraph (d)(2) of this section), or maturity (pursuant to paragraph (i) of this section), or liquidity of a portfolio security (pursuant to paragraph (d)(4) of this section), and maintains a record of this determination (pursuant to paragraphs (g)(3) and (h)(7) of this section), then the fund may disregard such demand feature or guarantee for all purposes of this section.

(f) *Downgrades, defaults and other events.*

(1) *Downgrades.*

(i) *General.* Upon the occurrence of either of the events specified in paragraphs (f)(1)(i)(A) and (B) of this section with respect to a portfolio security, the board of directors of the money market fund shall reassess promptly whether such security continues to present minimal credit risks and shall cause the fund to take such action as the board of directors determines is in the best interests of the money market fund:

(A) A portfolio security of a money market fund ceases to be a first tier security (either because it no longer has the highest rating from the requisite NRSROs or, in the case of an unrated security, the board of directors of the money market fund determines that it is no longer of comparable quality to a first tier security); and

(B) The money market fund's investment adviser (or any person to whom the fund's board of directors has delegated portfolio management responsibilities) becomes aware that any unrated security or second tier security held by the money market fund has, since the security was acquired by the fund, been given a rating by a designated NRSRO below the designated NRSRO's second highest short-term rating category.

(ii) *Securities to be disposed of.* The reassessments required by paragraph (f)(1)(i) of this section shall not be required if the fund disposes of the security (or it matures) within five business days of the specified event and, in the case of events specified in paragraph (f)(1)(i)(B) of this section, the board is subsequently notified of the adviser's actions.

(iii) *Special rule for certain securities subject to demand features.* In the event that after giving effect to a rating downgrade, more than 2.5 percent of the fund's total assets are invested in securities issued by or subject to demand features from a single institution that are second tier securities, the fund shall reduce its investment in securities issued by or subject to demand features from that institution to no more than 2.5 percent of its total assets by exercising the demand features at the next succeeding exercise date(s), absent a finding by the board of directors that disposal of the portfolio security would not be in the best interests of the money market fund.

(2) *Defaults and other events.* Upon the occurrence of any of the events specified in paragraphs (f)(2)(i) through (iv) of this section with respect to a portfolio security, the money market fund shall dispose of such security as soon as practicable consistent with achieving an orderly disposition of the security, by sale, exercise of any demand feature or otherwise, absent a finding by the board of directors that disposal of the portfolio security would not be in the best interests of the money market fund (which determination may take into account, among other factors, market conditions that could affect the orderly disposition of the portfolio security):

(i) The default with respect to a portfolio security (other than an immaterial default unrelated to the financial condition of the issuer);

(ii) A portfolio security ceases to be an eligible security;

(iii) A portfolio security has been determined to no longer present minimal credit risks; or

(iv) An event of insolvency occurs with respect to the issuer of a portfolio security or the provider of any demand feature or guarantee.

(3) *Notice to the Commission.* The money market fund must notify the Commission of the occurrence of certain material events, as specified in Form N–CR (§ 274.222 of this chapter).

(4) *Defaults for purposes of Paragraphs (f)(2) and (3) of this section.* For purposes of paragraphs (f)(2) and (3)

of this section, an instrument subject to a demand feature or guarantee shall not be deemed to be in default (and an event of insolvency with respect to the security shall not be deemed to have occurred) if:

(i) In the case of an instrument subject to a demand feature, the demand feature has been exercised and the fund has recovered either the principal amount or the amortized cost of the instrument, plus accrued interest;

(ii) The provider of the guarantee is continuing, without protest, to make payments as due on the instrument; or

(iii) The provider of a guarantee with respect to an asset-backed security pursuant to paragraph (a)(16)(ii) of this section is continuing, without protest, to provide credit, liquidity or other support as necessary to permit the asset-backed security to make payments as due.

(g) *Required procedures.* The money market fund's board of directors must adopt written procedures including the following:

(1) *General.* In supervising the money market fund's operations and delegating special responsibilities involving portfolio management to the money market fund's investment adviser, the money market fund's board of directors, as a particular responsibility within the overall duty of care owed to its shareholders, must establish written procedures reasonably designed, taking into account current market conditions and the money market fund's investment objectives, to assure to the extent reasonably practicable that the money market fund's price per share, as computed for the purpose of distribution, redemption and repurchase, rounded to the nearest one percent, will not deviate from the stable price established by the board of directors.

(2) *Securities for which maturity is determined by reference to demand features.* In the case of a security for which maturity is determined by reference to a demand feature, written procedures shall require ongoing review of the security's continued minimal credit risks, and that review must be based on, among other things, financial data for the most recent fiscal year of the issuer of the demand feature and, in the case of a security subject to a conditional demand feature, the issuer of the security whose financial condition must be monitored under paragraph (d)(2)(iv) of this section, whether such data is publicly available or provided under the terms of the security's governing documentation.

(3) *Securities subject to demand features or guarantees.* In the case of a security subject to one or more demand features or guarantees that the fund's board of directors has determined that the fund is not relying on to determine the quality (pursuant to paragraph (d)(2) of this section), maturity (pursuant to paragraph (i) of this section) or liquidity (pursuant to paragraph (d)(4) of this section) of the security subject to the demand feature or guarantee, written procedures must require periodic evaluation of such determination.

(4) *Adjustable rate securities without demand features.* In the case of a variable rate or floating rate security that is not subject to a demand feature and for which maturity is determined pursuant to paragraph (i)(1), (i)(2) or (i)(4) of this section, written procedures shall require periodic review of whether the interest rate formula, upon readjustment of its interest rate, can reasonably be expected to cause the security to have a market value that approximates its amortized cost value.

(5) *Ten percent obligors of asset-backed securities.* In the case of an asset-backed security, written procedures must require the fund to periodically determine the number of ten percent obligors (as that term is used in paragraph (d)(3)(ii)(D) of this section) deemed to be the issuers of all or a portion of the asset-backed security for purposes of paragraph (d)(3)(ii)(D) of this section; provided, however, written procedures need not require periodic determinations with respect to any asset-backed security that a fund's board of directors has determined, at the time of acquisition, will not have, or is unlikely to have, ten percent obligors that are deemed to be issuers of all or a portion of that asset-backed security for purposes of paragraph (d)(3)(ii)(D) of this section, and maintains a record of this determination.

(6) *Asset-backed securities not subject to guarantees.* In the case of an asset backed-security for which the fund's board of directors has determined that the fund is not relying on the sponsor's financial strength or its ability or willingness to provide liquidity, credit or other support in connection with the asset-backed security to determine the quality (pursuant to paragraph (d)(2) of this section) or liquidity (pursuant to paragraph (d)(4) of this section) of the asset-backed security, written procedures must require periodic evaluation of such determination.

(7) *Stress testing.* Written procedures must provide for:

(i) The periodic testing, at such intervals as the board of directors determines appropriate and reasonable in light of current market conditions, of the money market fund's ability to maintain the stable price per share established by the board of directors for the purpose of distribution, redemption, and repurchase, and to have invested at least fifteen percent of its assets in weekly liquid assets, based upon specified hypothetical events that include, but are not limited to:

(A) Increases in the general level of short-term interest rates;

(B) An increase in shareholder redemptions, together with an assessment of how the fund would meet the redemptions, taking into consideration assumptions regarding the relative liquidity of the fund's portfolio securities, the prices for which portfolio securities could be sold, the fund's historical experience meeting redemption requests, and any other relevant factors;

(C) A downgrade or default of portfolio securities, and the effects these events could have on other securities held by the fund;

(D) The widening or narrowing of spreads among the indexes to which interest rates of portfolio securities are tied;

(E) Other movements in interest rates that may affect the fund's portfolio securities, such as parallel and non-parallel shifts in the yield curve; and

(F) Combinations of these and any other events the adviser deems relevant, assuming a positive correlation of risk factors (*e.g.,* assuming that a security default likely will be followed by increased redemptions) and taking into consideration the extent to which the fund's portfolio securities are correlated such that adverse events affecting a given security are likely to also affect one or more other securities (*e.g.,* a consideration of whether issuers in the same or related industries or geographic regions would be affected by adverse events affecting issuers in the same industry or geographic region).

(ii) A report on the results of such testing to be provided to the board of directors at its next regularly scheduled meeting (or sooner, if appropriate in light of the results), which report must include:

(A) The date(s) on which the testing was performed and the magnitude of each hypothetical event that would cause the fund's price per share for purposes of distribution, redemption and repurchase to deviate from the stable price per share established by the board of directors, or cause the fund to have invested less than fifteen percent of its assets in weekly liquid assets; and

(B) An assessment by the fund's adviser of the fund's ability to withstand the events (and concurrent occurrences of those events) that are reasonably

likely to occur within the following year, including such information as may reasonably be necessary for the board of directors to evaluate the stress testing conducted by the adviser and the results of the testing.

(h) *Record keeping and reporting.*

(1) *Written procedures.* For a period of not less than six years following the replacement of such procedures with new procedures (the first two years in an easily accessible place), a written copy of the procedures (and any modifications thereto) described in paragraphs (g) and (j) of this section must be maintained and preserved.

(2) *Board considerations and actions.* For a period of not less than six years (the first two years in an easily accessible place) a written record must be maintained and preserved of the board of directors' considerations and actions taken in connection with the discharge of its responsibilities, as set forth in this section, to be included in the minutes of the board of directors' meetings.

(3) *Credit risk analysis.* For a period of not less than three years from the date that the credit risks of a portfolio security were most recently reviewed, a written record of the determination that a portfolio security presents minimal credit risks and the designated NRSRO ratings (if any) used to determine the status of the security as an eligible security, first tier security or second tier security shall be maintained and preserved in an easily accessible place.

(4) *Determinations with respect to adjustable rate securities.* For a period of not less than three years from the date when the assessment was most recently made, a written record must be preserved and maintained, in an easily accessible place, of the determination required by paragraph (g)(4) of this section (that a variable rate or floating rate security that is not subject to a demand feature and for which maturity is determined pursuant to paragraph (i)(1), (i)(2) or (i)(4) of this section can reasonably be expected, upon readjustment of its interest rate at all times during the life of the instrument, to have a market value that approximates its amortized cost).

(5) *Determinations with respect to asset-backed securities.* For a period of not less than three years from the date when the determination was most recently made, a written record must be preserved and maintained, in an easily accessible place, of the determinations required by paragraph (g)(5) of this section (the number of ten percent obligors (as that term is used in paragraph (d)(3)(ii)(D) of this section) deemed to be the issuers of all or a portion of the asset-backed security for purposes of paragraph (d)(3)(ii)(D) of this section). The written record must include:

(i) The identities of the ten percent obligors (as that term is used in paragraph (d)(3)(ii)(D) of this section), the percentage of the qualifying assets constituted by the securities of each ten percent obligor and the percentage of the fund's total assets that are invested in securities of each ten percent obligor; and

(ii) Any determination that an asset-backed security will not have, or is unlikely to have, ten percent obligors deemed to be issuers of all or a portion of that asset-backed security for purposes of paragraph (d)(3)(ii)(D) of this section.

(6) *Evaluations with respect to asset-backed securities not subject to guarantees.* For a period of not less than three years from the date when the evaluation was most recently made, a written record must be preserved and maintained, in an easily accessible place, of the evaluation required by paragraph (g)(6) of this section (regarding asset-backed securities not subject to guarantees).

(7) *Evaluations with respect to securities subject to demand features or guarantees.* For a period of not less than three years from the date when the evaluation was most recently made, a written record must be preserved and maintained, in an easily accessible place, of the evaluation required by paragraph (g)(3) of this section (regarding securities subject to one or more demand features or guarantees).

(8) *Reports with respect to stress testing.* For a period of not less than six years (the first two years in an easily accessible place), a written copy of the report required under paragraph (g)(7)(ii) of this section must be maintained and preserved.

(9) *Inspection of records.* The documents preserved pursuant to paragraph (h) of this section are subject to inspection by the Commission in accordance with section 31(b) of the Act (15 U.S.C. 80a–30(b)) as if such documents were records required to be maintained pursuant to rules adopted under section 31(a) of the Act (15 U.S.C. 80a–30(a)).

(10) *Web site disclosure of portfolio holdings and other fund information.* The money market fund must post prominently on its Web site the following information:

(i) For a period of not less than six months, beginning no later than the fifth business day of the month, a schedule of its investments, as of the last business day or subsequent calendar day of the preceding month, that includes the following information:

(A) With respect to the money market fund and each class of redeemable shares thereof:

*(1)* The WAM; and

*(2)* The WAL.

(B) With respect to each security held by the money market fund:

*(1)* Name of the issuer;

*(2) Category of investment (indicate the category that most closely identifies the instrument from among the following:* U.S. Treasury Debt; U.S. Government Agency Debt; Non U.S. Sovereign Debt; Non U.S. Sub-Sovereign Debt; Variable Rate Demand Note; Other Municipal Debt; Financial Company Commercial Paper; Asset-Backed Commercial Paper; Other Asset-Backed Security; Non-Financial Company Commercial Paper; Collateralized Commercial Paper; Certificate of Deposit (including Time Deposits and Euro Time Deposits); Structured Investment Vehicle Note; Other Note; U.S. Treasury Repurchase Agreement; Government Agency Repurchase Agreement; Other Repurchase Agreement; Insurance Company Funding Agreement; Investment Company; Other Instrument);

*(3)* CUSIP number (if any);

*(4)* Principal amount;

*(5)* The maturity date determined by taking into account the maturity shortening provisions in paragraph (i) of this section (*i.e.,* the maturity date used to calculate WAM under paragraph (d)(1)(ii) of this section)*;*

*(6)* The maturity date determined without reference to the exceptions in paragraph (i) of this section regarding interest rate readjustments (*i.e.,* the maturity used to calculate WAL under paragraph (d)(1)(iii) of this section)*;*

*(7)* Coupon or yield; and

*(8)* Value.

(ii) A schedule, chart, graph, or other depiction, which must be updated each business day as of the end of the preceding business day, showing, as of the end of each business day during the preceding six months:

(A) The percentage of the money market fund's total assets invested in daily liquid assets;

(B) The percentage of the money market fund's total assets invested in weekly liquid assets; and

(C) The money market fund's net inflows or outflows.

(iii) A schedule, chart, graph, or other depiction showing the money market fund's net asset value per share (which the fund must calculate based on current market factors before applying the penny-rounding method), rounded to the fourth decimal place in the case

of funds with a $1.0000 share price or an equivalent level of accuracy for funds with a different share price (*e.g.,* $10.000 or $100.00 per share), as of the end of each business day during the preceding six months, which must be updated each business day as of the end of the preceding business day.

(iv) A link to a Web site of the Securities and Exchange Commission where a user may obtain the most recent 12 months of publicly available information filed by the money market fund pursuant to § 270.30b1–7.

(v) For a period of not less than one year, beginning no later than the first business day following the occurrence of any event specified in Parts C, E, F, or G of Form N–CR (§ 274.222 of this chapter), the same information that the money market fund is required to report to the Commission on Part C, Part E (Items E.1 and E.2), Part F (Items F.1 and F.2), or Part G of Form N–CR concerning such event.

(11) *Processing of transactions.* The money market fund (or its transfer agent) must have the capacity to redeem and sell securities issued by the fund at a price based on the current net asset value per share pursuant to § 270.22c–1. Such capacity must include the ability to redeem and sell securities at prices that do not correspond to a stable price per share.

(i) *Maturity of portfolio securities.* For purposes of this section, the maturity of a portfolio security shall be deemed to be the period remaining (calculated from the trade date or such other date on which the fund's interest in the security is subject to market action) until the date on which, in accordance with the terms of the security, the principal amount must unconditionally be paid, or in the case of a security called for redemption, the date on which the redemption payment must be made, except as provided in paragraphs (i)(1) through (i)(8) of this section:

(1) *Adjustable rate government securities.* A government security that is a variable rate security where the variable rate of interest is readjusted no less frequently than every 397 calendar days shall be deemed to have a maturity equal to the period remaining until the next readjustment of the interest rate. A government security that is a floating rate security shall be deemed to have a remaining maturity of one day.

(2) *Short-term variable rate securities.* A variable rate security, the principal amount of which, in accordance with the terms of the security, must unconditionally be paid in 397 calendar days or less shall be deemed to have a maturity equal to the earlier of the period remaining until the next readjustment of the interest rate or the period remaining until the principal amount can be recovered through demand.

(3) *Long-term variable rate securities.* A variable rate security, the principal amount of which is scheduled to be paid in more than 397 calendar days, that is subject to a demand feature, shall be deemed to have a maturity equal to the longer of the period remaining until the next readjustment of the interest rate or the period remaining until the principal amount can be recovered through demand.

(4) *Short-term floating rate securities.* A floating rate security, the principal amount of which, in accordance with the terms of the security, must unconditionally be paid in 397 calendar days or less shall be deemed to have a maturity of one day, except for purposes of determining WAL under paragraph (d)(1)(iii) of this section, in which case it shall be deemed to have a maturity equal to the period remaining until the principal amount can be recovered through demand.

(5) *Long-term floating rate securities.* A floating rate security, the principal amount of which is scheduled to be paid in more than 397 calendar days, that is subject to a demand feature, shall be deemed to have a maturity equal to the period remaining until the principal amount can be recovered through demand.

(6) *Repurchase agreements.* A repurchase agreement shall be deemed to have a maturity equal to the period remaining until the date on which the repurchase of the underlying securities is scheduled to occur, or, where the agreement is subject to demand, the notice period applicable to a demand for the repurchase of the securities.

(7) *Portfolio lending agreements.* A portfolio lending agreement shall be treated as having a maturity equal to the period remaining until the date on which the loaned securities are scheduled to be returned, or where the agreement is subject to demand, the notice period applicable to a demand for the return of the loaned securities.

(8) *Money market fund securities.* An investment in a money market fund shall be treated as having a maturity equal to the period of time within which the acquired money market fund is required to make payment upon redemption, unless the acquired money market fund has agreed in writing to provide redemption proceeds to the investing money market fund within a shorter time period, in which case the maturity of such investment shall be deemed to be the shorter period.

(j) *Delegation.* The money market fund's board of directors may delegate to the fund's investment adviser or officers the responsibility to make any determination required to be made by the board of directors under this section other than the determinations required by paragraphs (a)(10)(i) (designation of NRSROs), (c)(1) (board findings), (c)(2)(i) and (ii) (determinations related to liquidity fees and temporary suspensions), (f)(2) (defaults and other events), (g)(1) (general required procedures), and (g)(7) (stress testing procedures) of this section.

(1) *Written Guidelines.* The board of directors must establish and periodically review written guidelines (including guidelines for determining whether securities present minimal credit risks as required in paragraph (d)(2) of this section) and procedures under which the delegate makes such determinations.

(2) *Oversight.* The board of directors must take any measures reasonably necessary (through periodic reviews of fund investments and the delegate's procedures in connection with investment decisions and prompt review of the adviser's actions in the event of the default of a security or event of insolvency with respect to the issuer of the security or any guarantee or demand feature to which it is subject that requires notification of the Commission under paragraph (f)(3) of this section by reference to Form N–CR (§ 274.222 of this chapter)) to assure that the guidelines and procedures are being followed.

■ 7. Section 270.12d3–1(d)(7)(v) is amended by removing ''§ 270.2a–7(a)(8) and § 270.2a–7(a)(15)'' and adding in its place ''§ 270.2a–7(a)(9) and § 270.2a–7(a)(16)''.

■ 8. Section 270.18f–3(c)(2)(i) is amended by removing the phrase ''that determines net asset value using the amortized cost method permitted by § 270.2a–7'' and adding in its place ''that operates in compliance with § 270.2a–7''.

■ 9. Section § 270.22e–3 is amended by revising paragraph (a)(1) and adding paragraph (d).

The revisions and additions read as follows.

**Alternative 1**

**§ 270.22e–3 Exemption for liquidation of money market funds.**

(a) * * *

(1) The fund, at the end of a business day, has invested less than fifteen percent of its total assets in weekly liquid assets or, in the case of a fund relying on the exemptions provided by

§ 270.2a–7(c)(2) or (3), the fund's price per share as computed for the purpose of distribution, redemption and repurchase, rounded to the nearest one percent, has deviated from the stable price established by the board of directors or the fund's board of directors, including a majority of directors who are not interested persons of the fund, determines that such a deviation is likely to occur;

* * * * *

(d) *Definitions.* Each of the terms business day, total assets, and weekly liquid assets has the same meaning as defined in § 270.2a–7.

**Alternative 2**

**§ 270.22e–3 Exemption for liquidation of money market funds.**

(a) * * *

(1) The fund, at the end of a business day, has invested less than fifteen percent of its total assets in weekly liquid assets, or the fund's price per share as computed for the purpose of distribution, redemption and repurchase, rounded to the nearest one percent, has deviated from the stable price established by the board of directors or the fund's board of directors, including a majority of directors who are not interested persons of the fund, determines that such a deviation is likely to occur;

* * * * *

(d) *Definitions.* Each of the terms business day, total assets, and weekly liquid assets has the same meaning as defined in § 270.2a–7.

■ 10. Section 270.30b1–7 is revised to read as follows:

**§ 270.30b1–7 Monthly report for money market funds.**

Every registered open-end management investment company, or series thereof, that is regulated as a money market fund under § 270.2a–7 must file with the Commission a monthly report of portfolio holdings on Form N–MFP (§ 274.201 of this chapter), current as of the last business day or any subsequent calendar day of the preceding month, no later than the fifth business day of each month.

■ 11. Section 270.30b1–8 is added to read as follows:

**§ 270.30b1–8. Current report for money market funds.**

Every registered open-end management investment company, or series thereof, that is regulated as a money market fund under § 270.2a–7, that experiences any of the events specified on Form N–CR (17 CFR 274.222 of this chapter), must file with the Commission a current report on Form N–CR within the period specified in that form.

■ 12. Section 270.31a–1(b)(1) is amended by removing ''§ 270.2a–7(a)(8) or § 270.2a–7(a)(15)'' and adding in its place ''§ 270.2a–7(a)(9) or § 270.2a–7(a)(16)''.

## PART 239—FORMS PRESCRIBED UNDER THE SECURITIES ACT OF 1933

■ 13. The authority citation for Part 239 continues to read in part as follows:

**Authority:** 15 U.S.C. 77f, 77g, 77h, 77j, 77s, 77z–2, 77z–3, 77sss, 78c, 78*l,* 78m, 78n, 78*o*(d), 78o–7 note, 78u–5, 78w(a), 78ll, 78mm, 80a–2(a), 80a–3, 80a–8, 80a–9, 80a–10, 80a–13, 80a–24, 80a–26, 80a–29, 80a–30, and 80a–37, unless otherwise noted.

* * * * *

## PART 274—FORMS PRESCRIBED UNDER THE INVESTMENT COMPANY ACT OF 1940

■ 14. The authority citation for Part 274 continues to read in part as follows:

**Authority:** 15 U.S.C. 77f, 77g, 77h, 77j, 77s, 78c(b), 78*l,* 78m, 78n, 78o(d), 80a–8, 80a–24, 80a–26, and 80a–29, unless otherwise noted.

* * * * *

■ 15. Form N–1A (referenced in §§ 239.15A and 274.11A) is amended by:

■ a. Revising paragraph (b)(1)(ii) of Item 4; and

■ b. Adding a paragraph (g) to Item 16; or

■ c. Revising paragraph 2(b) of the instructions to Item 3;

■ d. Revising paragraph (b)(1)(ii) of Item 4; and

■ e. Adding a paragraph (g) to Item 16.

The additions and revisions read as follows:

**Note:** The text of Form N–1A does not, and this amendment will not, appear in the Code of Federal Regulations.

**Alternative 1**

**Form N–1A**

* * * * *

**Item 4. Risk/Return Summary: Investments, Risks, and Performance**

* * * * *

(b) * * *

*(1)* * * *

(ii)(A) If the Fund is a Money Market Fund that is not subject to the exemption provisions of § 270.2a–7(c)(2) or § 270.2a–7(c)(3), include the following bulleted statement:

- You could lose money by investing in the Fund.
- You should not invest in the Fund if you require your investment to maintain a stable value.
- The value of shares of the Fund will increase and decrease as a result of changes in the value of the securities in which the Fund invests. The value of the securities in which the Fund invests may in turn be affected by many factors, including interest rate changes and defaults or changes in the credit quality of a security's issuer.
- An investment in the Fund is not insured or guaranteed by the Federal Deposit Insurance Corporation or any other government agency.
- The Fund's sponsor has no legal obligation to provide financial support to the Fund, and you should not expect that the sponsor will provide financial support to the Fund at any time.

(B) If the Fund is a Money Market Fund that is subject to the exemption provisions of § 270.2a–7(c)(2) or § 270.2a–7(c)(3), include the following bulleted statement:

- You could lose money by investing in the Fund.
- The Fund seeks to preserve the value of your investment at $1.00 per share, but cannot guarantee such stability.
- An investment in the Fund is not insured or guaranteed by the Federal Deposit Insurance Corporation or any other government agency.
- The Fund's sponsor has no legal obligation to provide financial support to the Fund, and you should not expect that the sponsor will provide financial support to the Fund at any time.

*Instruction.* If an affiliated person, promoter, or principal underwriter of the Fund, or an affiliated person of such a person, has entered into an agreement to provide financial support to the Fund, and the term of the agreement will extend for at least one year following the effective date of the Fund's registration statement, the bulleted statement specified in Item 4(b)(1)(ii)(A) or Item 4(b)(1)(ii)(B) may omit the last bulleted sentence (''The Fund's sponsor has no legal obligation to provide financial support to the Fund, and you should not expect that the sponsor will provide financial support to the Fund at any time.''). For purposes of this Instruction, the term ''financial support'' includes, for example, any capital contribution, purchase of a security from the Fund in reliance on § 270.17a–9, purchase of any defaulted or devalued security at par, purchase of Fund shares, execution of letter of credit or letter of indemnity, capital support agreement (whether or not the Fund ultimately received support), or performance guarantee, or any other similar action to increase the value of the fund's portfolio or otherwise support the fund during times of stress.

* * * * *

**Item 16. Description of the Fund and Its Investments and Risks**

* * * * *

(g) *Financial Support Provided to Money Market Funds.* If the Fund is a Money Market Fund, disclose any occasion during the last 10 years on which an affiliated person, promoter, or principal underwriter of the Fund, or an affiliated person of such a person, provided any form of financial support to the Fund, including a description of the nature of support, person providing support, brief description of the relationship between the person providing support and the Fund, brief description of the reason for support, date support provided, amount of support, security supported (if applicable), value of security supported on date support was initiated (if applicable), term of support, and a brief description of any contractual restrictions relating to support.

*Instructions*

1. The term ''financial support'' includes, for example, any capital contribution, purchase of a security from the Fund in reliance on § 270.17a–9, purchase of any defaulted or devalued security at par, purchase of Fund shares, execution of letter of credit or letter of indemnity, capital support agreement (whether or not the Fund ultimately received support), or performance guarantee, or any other similar action to increase the value of the Fund's portfolio or otherwise support the Fund during times of stress.

2. If during the last 10 years, the Fund has participated in one or more mergers with another investment company (a ''merging investment company''), provide the information required by Item 16(g) with respect to any merging investment company as well as with respect to the Fund; for purposes of this instruction, the term ''merger'' means a merger, consolidation, or purchase or sale of substantially all of the assets between the Fund and a merging investment company.

**Alternative 2**

**Form N–1A**

* * * * *

**Item 3. Risk/Return Summary: Fee Table**

* * * * *

*Instructions*

* * * * *

*2. Shareholder Fees.*

* * * * *

(b) ''Redemption Fee'' includes a fee charged for any redemption of the Fund's shares, but does not include a deferred sales charge (load) imposed upon redemption, and, if the Fund is a Money Market Fund, does not include a liquidity fee imposed upon the sale of Fund shares in accordance with rule 2a–7(c)(2).

* * * * *

**Item 4. Risk/Return Summary: Investments, Risks, and Performance**

* * * * *

(b) * * *

*(1)* * * *

* * * * *

(ii)(A) If the Fund is a Money Market Fund (including any Money Market Fund that is subject to the exemption provisions of rule 2a–7(c)(2)(iii), but that has chosen not to rely on the rule 2a–7(c)(2)(iii) exemption provisions), include the following bulleted statement:

- You could lose money by investing in the Fund.
- The Fund seeks to preserve the value of your investment at $1.00 per share, but cannot guarantee such stability.
- The Fund may impose a fee upon sale of your shares when the Fund is under considerable stress.
- The Fund may temporarily suspend your ability to sell shares of the Fund when the Fund is under considerable stress.
- An investment in the Fund is not insured or guaranteed by the Federal Deposit Insurance Corporation or any other government agency.
- The Fund's sponsor has no legal obligation to provide financial support to the Fund, and you should not expect that the sponsor will provide financial support to the Fund at any time.

(B) If the Fund is a Money Market Fund that is subject to the exemption provisions of rule 2a–7(c)(2)(iii) and that has chosen to rely on the rule 2a–7(c)(2)(iii) exemption provisions, include the following bulleted statement:

- You could lose money by investing in the Fund.
- The Fund seeks to preserve the value of your investment at $1.00 per share, but cannot guarantee such stability.
- An investment in the Fund is not insured or guaranteed by the Federal Deposit Insurance Corporation or any other government agency.
- The Fund's sponsor has no legal obligation to provide financial support to the Fund, and you should not expect that the sponsor will provide financial support to the Fund at any time.

*Instruction.* If an affiliated person, promoter, or principal underwriter of the Fund, or an affiliated person of such a person, has entered into an agreement to provide financial support to the Fund, and the term of the agreement will extend for at least one year following the effective date of the Fund's registration statement, the bulleted statement specified in Item 4(b)(1)(ii)(A) or Item 4(b)(1)(ii)(B) may omit the last bulleted sentence (''The Fund's sponsor has no legal obligation to provide financial support to the Fund, and you should not expect that the sponsor will provide financial support to the Fund at any time.''). For purposes of this Instruction, the term ''financial support'' includes, for example, any capital contribution, purchase of a security from the Fund in reliance on § 270.17a–9, purchase of any defaulted or devalued security at par, purchase of Fund shares, execution of letter of credit or letter of indemnity, capital support agreement (whether or not the Fund ultimately received support), or performance guarantee, or any other similar action to increase the value of the Fund's portfolio or otherwise support the Fund during times of stress.

* * * * *

**Item 16. Description of the Fund and Its Investments and Risks**

* * * * *

(g) *Money Market Fund Material Events.* If the Fund is a Money Market Fund (except any Money Market Fund that is subject to the exemption provisions of rule 2a–7(c)(2)(iii) and has chosen to rely on the rule 2a–7(c)(2)(iii) exemption provisions) disclose, if applicable, the following events:

(1) During the last 10 years, any occasion on which the Fund has invested less than fifteen percent of its total assets in weekly liquid assets (as provided in rule 2a–7(c)(2)), and with respect to each such occasion, whether the Fund's board of directors determined to impose a liquidity fee pursuant to rule 2a–7(c)(2)(i) and/or temporarily suspend the Fund's redemptions pursuant to rule 2a–7(c)(2)(ii).

*Instructions.* With respect to each such occasion, disclose: the dates and length of time for which the Fund invested less than fifteen percent of its total assets in weekly liquid assets; a brief description of the facts and circumstances leading to the Fund's investing less than fifteen percent of its total assets in weekly liquid assets; the dates and length of time for which the Fund's board of directors determined to impose a liquidity fee pursuant to rule

2a–7(c)(2)(i) and/or temporarily suspend the Fund's redemptions pursuant to rule 2a–7(c)(2)(ii); and a short discussion of the board's analysis supporting its decision to impose a liquidity fee (or not to impose a liquidity fee) and/or temporarily suspend the Fund's redemptions.

(2) During the last 10 years, any occasion on which an affiliated person, promoter, or principal underwriter of the Fund, or an affiliated person of such a person, provided any form of financial support to the Fund, including a description of the nature of support, person providing support, brief description of the relationship between the person providing support and the Fund, brief description of the reason for support, date support provided, amount of support, security supported (if applicable), value (calculated using available market quotations or an appropriate substitute that reflects current market conditions) of security supported on date support was initiated (if applicable), term of support, and a brief description of any contractual restrictions relating to support.

*Instructions*

1. The term ''financial support'' includes, for example, any capital contribution, purchase of a security from the Fund in reliance on § 270.17a–9, purchase of any defaulted or devalued security at par, purchase of Fund shares, execution of letter of credit or letter of indemnity, capital support agreement (whether or not the Fund ultimately received support), or performance guarantee, or any other similar action to increase the value of the Fund's portfolio or otherwise support the Fund during times of stress.

2. If during the last 10 years, the Fund has participated in one or more mergers with another investment company (a ''merging investment company''), provide the information required by Item 16(g)(2) with respect to any merging investment company as well as with respect to the Fund; for purposes of this instruction, the term ''merger'' means a merger, consolidation, or purchase or sale of substantially all of the assets between the Fund and a merging investment company.

■ 16. Form N–MFP (referenced in § 274.201) is revised to read as follows:

**Note:** The text of Form N–MFP does not, and this amendment will not, appear in the Code of Federal Regulations.

**Form N–MFP**

**Monthly Schedule of Portfolio Holdings of Money Market Funds**

Form N–MFP is to be used by registered open-end management investment companies, or series thereof, that are regulated as money market funds pursuant to rule 2a–7 under the Investment Company Act of 1940 (''Act'') (17 CFR 270.2a–7) (''money market funds''), to file reports with the Commission pursuant to rule 30b1–7 under the Act (17 CFR 270.30b1–7). The Commission may use the information provided on Form N–MFP in its regulatory, disclosure review, inspection, and policymaking roles.

**General Instructions**

*A. Rule as to Use of Form N–MFP*

Form N–MFP is the public reporting form that is to be used for monthly reports of money market funds required by section 30(b) of the Act and rule 30b1–7 under the Act (17 CFR 270.30b1–7). A money market fund must report information about the fund and its portfolio holdings as of the last business day or any subsequent calendar day of the preceding month. The Form N–MFP must be filed with the Commission no later than the fifth business day of each month, but may be filed any time beginning on the first business day of the month. Each money market fund, or series of a money market fund, is required to file a separate form. If the money market fund does not have any classes, the fund must provide the information required by Part B for the series.

A money market fund may file an amendment to a previously filed Form N–MFP at any time, including an amendment to correct a mistake or error in a previously filed form. A fund that files an amendment to a previously filed form must provide information in response to all items of Form N–MFP, regardless of why the amendment is filed.

*B. Application of General Rules and Regulations*

The General Rules and Regulations under the Act contain certain general requirements that are applicable to reporting on any form under the Act. These general requirements should be carefully read and observed in the preparation and filing of reports on this form, except that any provision in the form or in these instructions shall be controlling.

*C. Filing of Form N–MFP*

A money market fund must file Form N–MFP in accordance with rule 232.13 of Regulation S–T. Form N–MFP must be filed electronically using the Commission's EDGAR system.

*D. Paperwork Reduction Act Information*

A registrant is not required to respond to the collection of information contained in Form N–MFP unless the Form displays a currently valid Office of Management and Budget (''OMB'') control number. Please direct comments concerning the accuracy of the information collection burden estimate and any suggestions for reducing the burden to the Secretary, Securities and Exchange Commission, 100 F Street NE., Washington, DC 20549–1090. The OMB has reviewed this collection of information under the clearance requirements of 44 U.S.C. 3507.

*E. Definitions*

References to sections and rules in this Form N–MFP are to the Investment Company Act of 1940 [15 U.S.C. 80a] (the ''Investment Company Act''), unless otherwise indicated. Terms used in this Form N–MFP have the same meaning as in the Investment Company Act or related rules, unless otherwise indicated.

As used in this Form N–MFP, the terms set out below have the following meanings:

''Cash'' means demand deposits in depository institutions and cash holdings in custodial accounts.

''Class'' means a class of shares issued by a Multiple Class Fund that represents interests in the same portfolio of securities under rule 18f–3 [17 CFR 270.18f–3] or under an order exempting the Multiple Class Fund from sections 18(f), 18(g), and 18(i) [15 U.S.C. 80a–18(f), 18(g), and 18(i)].

''Fund'' means the Registrant or a separate Series of the Registrant. When an item of Form N–MFP specifically applies to a Registrant or a Series, those terms will be used.

''LEI'' means, with respect to any company, the ''legal entity identifier'' assigned by or on behalf of an internationally recognized standards setting body and required for reporting purposes by the U.S. Department of the Treasury's Office of Financial Research or a financial regulator. In the case of a financial institution, if a ''legal entity identifier'' has not been assigned, then LEI means the RSSD ID assigned by the National Information Center of the Board of Governors of the Federal Reserve System, if any.

''Master-Feeder Fund'' means a two-tiered arrangement in which one or more Funds (or registered or unregistered pooled investment

vehicles) (each a ''Feeder Fund''), holds shares of a single Fund (the ''Master Fund'') in accordance with section 12(d)(1)(E) [15 U.S.C. 80a–12(d)(1)(E)].

''Money Market Fund'' means a Fund that holds itself out as a money market fund and meets the requirements of rule 2a–7 [17 CFR 270.2a–7].

''Securities Act'' means the Securities Act of 1933 [15 U.S.C. 77a–aa].

''Series'' means shares offered by a Registrant that represent undivided interests in a portfolio of investments and that are preferred over all other series of shares for assets specifically allocated to that series in accordance with rule 18f–2(a) [17 CFR 270.18f–2(a)].

''Value'' has the meaning defined in section 2(a)(41) of the Act (15 U.S.C. 80a–2(a)(41)).

**United States Securities And Exchange Commission, Washington, DC 20549**

**Form N–MFP, Monthly Schedule Of Portfolio Holdings Of Money Market Funds**

**General Information**

Item 1. Report for [mm/dd/yyyy].
Item 2. CIK Number of Registrant.
Item 3. LEI of Registrant (if available) (See General Instructions E.)
Item 4. EDGAR Series Identifier.
Item 5. Total number of share classes in the series.
Item 6. Do you anticipate that this will be the fund's final filing on Form N–MFP? [Y/N] If Yes, answer Items 6.a–6.c.
a. Is the fund liquidating? [Y/N]
b. Is the fund merging with, or being acquired by, another fund? [Y/N]
c. If applicable, identify the successor fund by CIK, Securities Act file number, and EDGAR series identifier.
Item 7. Has the fund acquired or merged with another fund since the last filing? [Y/N] If Yes, answer Item 7.a.
a. Identify the acquired or merged fund by CIK, Securities Act file number, and EDGAR series identifier.
Item 8. Provide the name, email address, and telephone number of the person authorized to receive information and respond to questions about this Form N–MFP.

**Part A: Series-Level Information About the Fund**

Item A.1 Securities Act File Number.
Item A.2 Investment Adviser.
a. SEC file number of investment adviser.
Item A.3 Sub-Adviser. If a fund has one or more sub-advisers, disclose the name of each sub-adviser.
a. SEC file number of each sub-adviser.
Item A.4 Independent Public Accountant.
a. City and state of independent public accountant.
Item A.5 Administrator. If a fund has one or more administrators, disclose the name of each administrator.
Item A.6 Transfer Agent.
a. CIK Number.
b. SEC file number of transfer agent.
Item A.7 Master-Feeder Funds. Is this a Feeder Fund? [Y/N] If Yes, answer Items A.7.a–7.c.
a. Identify the Master Fund by CIK or, if the fund does not have a CIK, by name.
b. Securities Act file number of the Master Fund.
c. EDGAR series identifier of the Master Fund.
Item A.8 Master-Feeder Funds. Is this a Master Fund? [Y/N] If Yes, answer Items A.8.a–8.c.
a. Identify all Feeder Funds by CIK or, if the fund does not have a CIK, by name.
b. Securities Act file number of each Feeder Fund.
c. EDGAR series identifier of each Feeder Fund.
Item A.9 Is this series primarily used to fund insurance company separate accounts? [Y/N]
Item A.10 Category. Indicate the category that most closely identifies the money market fund from among the following: Treasury, Government/Agency, Exempt Government, Prime, Single State, or Other Tax Exempt.
Item A.11 Dollar-weighted average portfolio maturity (''WAM'' as defined in rule 2a–7(d)(1)(ii)).
Item A.12 Dollar-weighted average life maturity (''WAL'' as defined in rule 2a–7(d)(1)(iii)). Calculate WAL without reference to the exceptions in rule 2a–7(d) regarding interest rate readjustments.
Item A.13 Liquidity. Provide the following, to the nearest cent, as of the close of business on each Friday during the month reported (if the reporting date falls on a holiday or other day on which the fund does not calculate the daily or weekly liquidity, provide the value as of the close of business on the date in that week last calculated):
a. Total Value of Daily Liquid Assets:
i. Friday, week 1:
ii. Friday, week 2:
iii. Friday, week 3:
iv. Friday, week 4:
v. Friday, week 5 (if applicable):
b. Total Value of Weekly Liquid Assets (including Daily Liquid Assets):
i. Friday, week 1:
ii. Friday, week 2:
iii. Friday, week 3:
iv. Friday, week 4:
v. Friday, week 5 (if applicable):
Item A.14 Provide the following, to the nearest cent:
a. Cash. (See General Instructions E.)
b. Total Value of portfolio securities. (See General Instructions E.)
c. Total Value of other assets (excluding amounts provided in A.14.a– b.)
Item A.15 Total value of liabilities, to the nearest cent.
Item A.16 Net assets of the series, to the nearest cent.
Item A.17 Number of shares outstanding, to the nearest hundredth.
Item A.18 If the fund seeks to maintain a stable price per share, state the price the funds seeks to maintain.
Item A.19 Total percentage of shares outstanding, to the nearest tenth of one percent, held by the twenty largest shareholders of record.
Item A.20 7-day gross yield. Based on the 7 days ended on the last day of the prior month, calculate the fund's yield by determining the net change, exclusive of capital changes and income other than investment income, in the value of a hypothetical pre-existing account having a balance of one share at the beginning of the period and dividing the difference by the value of the account at the beginning of the base period to obtain the base period return, and then multiplying the base period return by (365/7) with the resulting yield figure carried to the nearest hundredth of one percent. The 7-day gross yield should not reflect a deduction of shareholders fees and fund operating expenses. For master funds and feeder funds, report the 7-day gross yield at the master-fund level.
Item A.21 Net asset value per share. Provide the net asset value per share, rounded to the fourth decimal place in the case of a fund with a $1.00 share price (or an equivalent level of accuracy for funds with a different share price), as of the close of business on each Friday during the month reported (if the reporting date falls on a holiday or other day on which the fund does not calculate the net asset value per share, provide the value as of the close of business on the date in that week last calculated):
a. Friday, week 1:

b. Friday, week 2:
c. Friday, week 3:
d. Friday, week 4:
e. Friday, week 5 (if applicable):

**Part B: Class-Level Information About the Fund**

For each Class of the Series (regardless of the number of shares outstanding in the Class), disclose the following:

Item B.1 EDGAR Class identifier.
Item B.2 Minimum initial investment.
Item B.3 Net assets of the Class, to the nearest cent.
Item B.4 Number of shares outstanding, to the nearest hundredth.
Item B.5 Net asset value per share. Provide the net asset value per share, rounded to the fourth decimal place in the case of a fund with a $1.00 share price (or an equivalent level of accuracy for funds with a different share price), as of the close of business on each Friday during the month reported (if the reporting date falls on a holiday or other day on which the fund does not calculate the net asset value per share, provide the value as of the close of business on the date in that week last calculated):
a. Friday, week 1:
b. Friday, week 2:
c. Friday, week 3:
d. Friday, week 4:
e. Friday, week 5 (if applicable):
Item B.6 Net shareholder flow. Provide the aggregate weekly gross subscriptions (including dividend reinvestments) and gross redemptions, rounded to the nearest cent, as of the close of business on each Friday during the month reported (if the reporting date falls on a holiday or other day on which the fund does not calculate the gross subscriptions or gross redemptions, provide the value as of the close of business on the date in that week last calculated):
a. Friday, week 1:
i. Weekly gross subscriptions (including dividend reinvestments):
ii. Weekly gross redemptions:
b. Friday, week 2:
i. Weekly gross subscriptions (including dividend reinvestments):
ii. Weekly gross redemptions:
c. Friday, week 3:
i. Weekly gross subscriptions (including dividend reinvestments):
ii. Weekly gross redemptions:
d. Friday, week 4:
i. Weekly gross subscriptions (including dividend reinvestments):
ii. Weekly gross redemptions:
e. Friday, week 5 (if applicable):
i. Weekly gross subscriptions (including dividend reinvestments):
ii. Weekly gross redemptions:
f. Total for the month reported:
i. Monthly gross subscriptions (including dividend reinvestments):
ii. Monthly gross redemptions:
Item B.7 7-day net yield, as calculated under Item 26(a)(1) of Form N–1A (§ 274.11A of this chapter).
Item B.8 During the reporting period, did any Person pay for, or waive all or part of the fund's operating expenses or management fees? [Y/N] If Yes, answer Item B.8.a.
a. Provide the name of the Person and describe the nature and amount of the expense payment or fee waiver, or both (reported in dollars).

**Part C: Schedule of Portfolio Securities and Other Information on Securities Sold**

*For each security held by the money market fund, disclose the following:*

Item C.1 The name of the issuer.
Item C.2 The title of the issue.
Item C.3 The CUSIP.
Item C.4 The LEI (if available). (See General Instruction E.)
Item C.5 Other identifier. In addition to CUSIP and LEI, provide at least one of the following other identifiers, if available:
a. The ISIN;
b. The CIK; or
c. Other unique identifier.
Item C.6 The category of investment. Indicate the category that most closely identifies the instrument from among the following: U.S. Treasury Debt; U.S. Government Agency Debt; Non U.S. Sovereign Debt; Non U.S. Sub-Sovereign Debt; Variable Rate Demand Note; Other Municipal Debt; Financial Company Commercial Paper; Asset-Backed Commercial Paper; Other Asset-Backed Security; Non-Financial Company Commercial Paper; Collateralized Commercial Paper; Certificate of Deposit (including Time Deposits and Euro Time Deposits); Structured Investment Vehicle Note; Other Note; U.S. Treasury Repurchase Agreement; Government Agency Repurchase Agreement; Other Repurchase Agreement; Insurance Company Funding Agreement; Investment Company; Other Instrument. If Other Instrument, include a brief description.
Item C.7 If the security is a repurchase agreement, is the fund treating the acquisition of the repurchase agreement as the acquisition of the underlying securities (*i.e.,* collateral) for purposes of portfolio diversification under rule 2a–7? [Y/N]
Item C.8 or all repurchase agreements, specify whether the repurchase agreement is ''open'' (*i.e.,* the repurchase agreement has no specified end date and, by its terms, will be extended or ''rolled'' each business day (or at another specified period) unless the investor chooses to terminate it), and describe the securities subject to the repurchase agreement (*i.e.,* collateral).
a. Is the repurchase agreement ''open''? [Y/N]
b. The name of the collateral issuer.
c. CUSIP.
d. LEI (if available).
e. Maturity date.
f. Coupon or yield.
g. The principal amount, to the nearest cent.
h. Value of collateral, to the nearest cent.
i. The category of investments that most closely represents the collateral, selected from among the following:

U.S. Treasury Debt; U.S. Government Agency Debt; Non U.S. Sovereign Debt; Non U.S. Sub-Sovereign Debt; Variable Rate Demand Note; Other Municipal Debt; Financial Company Commercial Paper; Asset-Backed Commercial Paper; Other Asset-Backed Security; Non-Financial Company Commercial Paper; Collateralized Commercial Paper; Certificate of Deposit (including Time Deposits and Euro Time Deposits); Structured Investment Vehicle Note; Equity; Corporate Bond; Exchange Traded Fund; Trust Receipt (other than for U.S. Treasuries); Derivative; Other Instrument. If Other Instrument, include a brief description.

If multiple securities of an issuer are subject to the repurchase agreement, the securities may be aggregated, in which case disclose: (a) the total principal amount and value and (b) the range of maturity dates and interest rates.

Item C.9 Rating. Indicate whether the security is a rated First Tier Security, rated Second Tier Security, an Unrated Security, or no longer an Eligible Security.
Item C.10 Name of each Designated NRSRO.
a. For each Designated NRSRO, disclose the credit rating given by the Designated NRSRO. If the instrument and its issuer are not rated by the Designated NRSRO, indicate ''NR.''
Item C.11 The maturity date determined by taking into account the maturity shortening provisions

of rule 2a–7(i) (*i.e.,* the maturity date used to calculate WAM under rule 2a–7(d)(1)(ii)).

Item C.12 The maturity date determined without reference to the exceptions in rule 2a–7(i) regarding interest rate readjustments (*i.e.,* the maturity date used to calculate WAL under rule 2a–7(d)(1)(iii)).

Item C.13 The maturity date determined without reference to the maturity shortening provisions of rule 2a–7(i) (*i.e.,* the final legal maturity date on which, in accordance with the terms of the security without regard to any interest rate readjustment or demand feature, the principal amount must unconditionally be paid).

Item C.14 Does the security have a Demand Feature on which the fund is relying to determine the quality, maturity or liquidity of the security? [Y/N] If Yes, answer Items C.14.a–14.f. Where applicable, provide the information required in Items C.14b–14.f in the order that each Demand Feature issuer was reported in Item C.14.a.

a. The identity of the Demand Feature issuer(s).
b. Designated NRSRO(s) for the Demand Feature(s) or provider(s) of the Demand Feature(s).
c. For each Designated NRSRO, disclose the credit rating given by the Designated NRSRO. If there is no rating given by the Designated NRSRO, indicate ''NR.''
d. The amount (*i.e.,* percentage) of fractional support provided by each Demand Feature issuer.
e. The period remaining until the principal amount of the security may be recovered through the Demand Feature.
f. Is the demand feature conditional? [Y/N]

Item C.15 Does the security have a Guarantee (other than an unconditional letter of credit disclosed in item C.14 above) on which the fund is relying to determine the quality, maturity or liquidity of the security? [Y/N] If Yes, answer Items C.15.a–15.d. Where applicable, provide the information required in Item C.15.b–15.d in the order that each Guarantor was reported in Item C.15.a.

a. The identity of the Guarantor(s).
b. Designated NRSRO(s) for the Guarantee(s) or Guarantor(s).
c. For each Designated NRSRO, disclose the credit rating given by the Designated NRSRO. If there is no rating given by the Designated NRSRO, indicate ''NR.''
d. The amount (*i.e.,* percentage) of fractional support provided by each Guarantor.

Item C.16 Does the security have any enhancements, other than those identified in Items C.14 and C.15 above, on which the fund is relying to determine the quality, maturity or liquidity of the security? [Y/N] If Yes, answer Items C.16.a–16.e. Where applicable, provide the information required in Items C.16.b–16.e in the order that each enhancement provider was reported in Item C.16.a.

a. The identity of the enhancement provider(s).
b. The type of enhancement(s).
c. Designated NRSRO(s) for the enhancement(s) or enhancement provider(s).
d. For each Designated NRSRO, disclose the credit rating given by the Designated NRSRO. If there is no rating given by the Designated NRSRO, indicate ''NR.''
e. The amount (*i.e.,* percentage) of fractional support provided by each enhancement provider.

Item C.17 The following information for each security held by the series (report items C.17.a–17.e separately for each lot purchased):

a. The total principal amount, to the nearest cent.
b. The purchase date(s).
c. The yield at purchase.
d. The yield as of the Form N–MFP reporting date (for floating or variable rate securities, if applicable).
e. The purchase price (as a percentage of par, rounded to the nearest one thousandth of one percent).

Item C.18 The total Value of the fund's position in the security, to the nearest cent: (See General Instruction E.)

a. *Including* the value of any sponsor support:
b. *Excluding* the value of any sponsor support:

Item C.19 The percentage of the money market fund's net assets invested in the security, to the nearest hundredth of a percent.

Item C.20 The security's level measurement (level 1, level 2, level 3) in the fair value hierarchy under U.S. Generally Accepted Accounting Principles (ASC 820, Fair Value Measurement)?

Item C.21 Is the security a Daily Liquid Asset? [Y/N]

Item C.22 Is the security a Weekly Liquid Asset? [Y/N]

Item C.23 Is the security an Illiquid Security? [Y/N]

Item C.24 Explanatory notes. Disclose any other information that may be material to other disclosures related to the portfolio security. If none, leave blank.

For any security sold during the reporting period, disclose the following:

Item C.25 The following information for each security sold by the series (report items C.25.a–25.e separately for each lot sold):

a. The total principal amount, to the nearest cent.
b. The purchase price (as a percentage of par, rounded to the nearest one thousandth of one percent).
c. The sale date(s).
d. The yield at sale.
e. The sale price (as a percentage of par, rounded to the nearest one thousandth of one percent).

**Signatures**

Pursuant to the requirements of the Investment Company Act of 1940, the registrant has duly caused this report to be signed on its behalf by the undersigned hereunto duly authorized.

_____
(Registrant)
Date _____

_____
(Signature)*
* Print name and title of the signing officer under his/her signature.

■ 17. Section 274.222 and Form N–CR are added to read as follows:

**Alternative 1**

**§ 274.222 Form N–CR, Current report of money market fund material events**

This form shall be used by registered investment companies that are regulated as money market funds under § 270.2a–7 of this chapter to file current reports pursuant to § 270.30b1–8 of this chapter within the time periods specified in the form.

**Note:** The text of Form N–CR will not appear in the Code of Federal Regulations.

**Form N–CR**

**Current Report Money Market Fund Material Events**

Form N–CR is to be used by registered open-end management investment companies, or series thereof, that are regulated as money market funds pursuant to rule 2a–7 under the Investment Company Act of 1940 (''Investment Company Act'') (17 CFR 270.2a–7) (''money market funds''), to file current reports with the Commission pursuant to rule 30b1–8 under the Investment Company Act (17 CFR 270.30b1–8). The Commission may use the information provided on Form

N–CR in its regulatory, disclosure review, inspection, and policymaking roles.

**General Instructions**

*A. Rule as to Use of Form N–CR*

Form N–CR is the public reporting form that is to be used for current reports of money market funds required by section 30(b) of the Act and rule 30b1–8 under the Act. A money market fund must file a report on Form N–CR upon the occurrence of any one or more of the events specified in Parts B–D of this form. Unless otherwise specified, a report is to be filed within one business day after occurrence of the event, and will be made public immediately upon filing. If the event occurs on a Saturday, Sunday, or holiday on which the Commission is not open for business, then the report is to be filed on the first business day thereafter.

*B. Application of General Rules and Regulations*

The General Rules and Regulations under the Act contain certain general requirements that are applicable to reporting on any form under the Act. These general requirements should be carefully read and observed in the preparation and filing of reports on this form, except that any provision in the form or in these instructions shall be controlling.

*C. Information To Be Included in Report Filed on Form N–CR*

Upon the occurrence of any one or more of the events specified in Parts B–D of Form N–CR, a money market fund must file a report on Form N–CR that includes information in response to each of the items in Part A of the form, as well as each of the items in the applicable Parts B–D of the form.

*D. Filing of Form N–CR*

A money market fund must file Form N–CR in accordance with rule 232.13 of Regulation S–T. Form N–CR must be filed electronically using the Commission's EDGAR system.

*E. Paperwork Reduction Act Information*

A registrant is not required to respond to the collection of information contained in Form N–CR unless the form displays a currently valid Office of Management and Budget (''OMB'') control number. Please direct comments concerning the accuracy of the information collection burden estimate and any suggestions for reducing the burden to the Secretary, Securities and Exchange Commission, 100 F Street NE., Washington, DC 20549–1090. The OMB has reviewed this collection of information under the clearance requirements of 44 U.S.C. 3507.

*F. Definitions*

References to sections and rules in this Form N–CR are to the Investment Company Act (15 U.S.C. 80a), unless otherwise indicated. Terms used in this Form N–CR have the same meaning as in the Investment Company Act or rule 2a–7 under the Investment Company Act, unless otherwise indicated. In addition, as used in this Form N–CR, the term ''Fund'' means the registrant or a separate series of the registrant.

**United States Securities and Exchange Commission Washington, DC 20549**

**Form N–CR Current Report Money Market Fund Material Events**

**Part A: General Information**

Item A.1 Report for [mm/dd/yyyy].
Item A.2 CIK Number of registrant.
Item A.3 EDGAR Series Identifier.
Item A.4 Securities Act File Number.
Item A.5 Provide the name, email address, and telephone number of the person authorized to receive information and respond to questions about this Form N–CR.

**Part B: Default or Event of Insolvency of Portfolio Security Issuer**

If the issuer of one or more of the Fund's portfolio securities, or the issuer of a Demand Feature or Guarantee to which one of the Fund's portfolio securities is subject, and on which the Fund is relying to determine the quality, maturity, or liquidity of a portfolio security, experiences a default or Event of Insolvency (other than an immaterial default unrelated to the financial condition of the issuer), and the portfolio security or securities (or the securities subject to the Demand Feature or Guarantee) accounted for at least ½ of 1 percent of the Fund's Total Assets immediately before the default or Event of Insolvency, disclose the following information:

Item B.1 Security or securities affected.
Item B.2 Date(s) on which the default(s) or Event(s) of Insolvency occurred.
Item B.3 Value of affected security or securities on the date(s) on which the default(s) or Event(s) of Insolvency occurred.
Item B.4 Percentage of the Fund's Total Assets represented by the affected security or securities.
Item B.5 Brief description of actions Fund plans to take in response to the default(s) or Event(s) of Insolvency.

*Instruction.* For purposes of Part B, an instrument subject to a Demand Feature or Guarantee will not be deemed to be in default (and an Event of Insolvency with respect to the security will not be deemed to have occurred) if: (i) in the case of an instrument subject to a Demand Feature, the Demand Feature has been exercised and the Fund has recovered either the principal amount or the amortized cost of the instrument, plus accrued interest; (ii) the provider of the Guarantee is continuing, without protest, to make payments as due on the instrument; or (iii) the provider of a Guarantee with respect to an Asset-Backed Security pursuant to rule 2a–7(a)(16)(ii) is continuing, without protest, to provide credit, liquidity or other support as necessary to permit the Asset-Backed Security to make payments as due.

**Part C: Provision of Financial Support to Fund**

If an affiliated person, promoter, or principal underwriter of the Fund, or an affiliated person of such a person, provides any form of financial support to the Fund (including, for example, any capital contribution, purchase of a security from the Fund in reliance on § 270.17a–9, purchase of any defaulted or devalued security at par, purchase of Fund shares, execution of letter of credit or letter of indemnity, capital support agreement (whether or not the Fund ultimately received support), or performance guarantee, or any other similar action to increase the value of the Fund's portfolio or otherwise support the Fund during times of stress), disclose the following information:

Item C.1 Description of nature of support.
Item C.2 Person providing support.
Item C.3 Brief description of relationship between the person providing support and the Fund.
Item C.4 Brief description of reason for support.
Item C.5 Date support provided.
Item C.6 Amount of support.
Item C.7 Security supported (if applicable).
Item C.8 Value of security supported on date support was initiated (if applicable).
Item C.9 Term of support.
Item C.10 Brief description of any contractual restrictions relating to support.

*Instruction.* If an affiliated person, promoter, or principal underwriter of the Fund, or an affiliated person of such a person, purchases a security from the Fund in reliance on § 270.17a–9, the

Fund must provide the purchase price of the security in responding to Item C.6.

**Part D: Deviation Between Current Net Asset Value per Share and Intended Stable Price per Share**

If a Fund is subject to the exemption provisions of rule 2a–7(c)(2) or rule 2a–7(c)(3), and its current net asset value per share (rounded to the fourth decimal place in the case of a fund with a $1.00 share price, or an equivalent level of accuracy for funds with a different share price) deviates downward from its intended stable price per share by more than ¼ of 1 percent, disclose:

Item D.1 Date(s) on which such deviation exceeded ¼ of 1 percent.

Item D.2 Extent of deviation between the Fund's current net asset value per share and its intended stable price per share.

Item D.3 Principal reason for the deviation, including the name of any security whose value calculated using available market quotations (or an appropriate substitute that reflects current market conditions) or sale price, or whose issuer's downgrade, default, or event of insolvency (or similar event), has contributed to the deviation.

**Signatures**

Pursuant to the requirements of the Investment Company Act of 1940, the registrant has duly caused this report to be signed on its behalf by the undersigned hereunto duly authorized.

_____

(Registrant)

Date _____

_____

(Signature) *

* Print name and title of the signing officer under his/her signature.

**Alternative 2**

**§ 274.222 Form N–CR, Current report of money market fund material events**

This form shall be used by registered investment companies that are regulated as money market funds under § 270.2a–7 of this chapter to file current reports pursuant to § 270.30b1–8 of this chapter within the time periods specified in the form.

**FORM N–CR**

**Current Report Money Market Fund Material Events**

Form N–CR is to be used by registered open-end management investment companies, or series thereof, that are regulated as money market funds pursuant to rule 2a–7 under the Investment Company Act of 1940 (''Investment Company Act'') (17 CFR 270.2a–7) (''money market funds''), to file current reports with the Commission pursuant to rule 30b1–8 under the Investment Company Act (17 CFR 270.30b1–8). The Commission may use the information provided on Form N–CR in its regulatory, disclosure review, inspection, and policymaking roles.

**General Instructions**

*A. Rule as to Use of Form N–CR*

Form N–CR is the public reporting form that is to be used for current reports of money market funds required by section 30(b) of the Act and rule 30b1–8 under the Act. A money market fund must file a report on Form N–CR upon the occurrence of any one or more of the events specified in Parts B–G of this form. Unless otherwise specified, a report is to be filed within one business day after occurrence of the event, and will be made public immediately upon filing. If the event occurs on a Saturday, Sunday, or holiday on which the Commission is not open for business, then the report is to be filed on the first business day thereafter.

*B. Application of General Rules and Regulations*

The General Rules and Regulations under the Act contain certain general requirements that are applicable to reporting on any form under the Act. These general requirements should be carefully read and observed in the preparation and filing of reports on this form, except that any provision in the form or in these instructions shall be controlling.

*C. Information To Be Included in Report Filed on Form N–CR*

Upon the occurrence of any one or more of the events specified in Parts B–G of Form N–CR, a money market fund must file a report on Form N–CR that includes information in response to each of the items in Part A of the form, as well as each of the items in the applicable Parts B–G of the form.

*D. Filing of Form N–CR*

A money market fund must file Form N–CR in accordance with rule 232.13 of Regulation S–T. Form N–CR must be filed electronically using the Commission's EDGAR system.

*E. Paperwork Reduction Act Information*

A registrant is not required to respond to the collection of information contained in Form N–CR unless the form displays a currently valid Office of Management and Budget (''OMB'') control number. Please direct comments concerning the accuracy of the information collection burden estimate and any suggestions for reducing the burden to the Secretary, Securities and Exchange Commission, 100 F Street NE., Washington, DC 20549–1090. The OMB has reviewed this collection of information under the clearance requirements of 44 U.S.C. 3507.

*F. Definitions*

References to sections and rules in this Form N–CR are to the Investment Company Act (15 U.S.C 80a), unless otherwise indicated. Terms used in this Form N–CR have the same meaning as in the Investment Company Act or rule 2a–7 under the Investment Company Act, unless otherwise indicated. In addition, as used in this Form N–CR, the term ''Fund'' means the registrant or a separate series of the registrant.

**United States Securities and Exchange Commission Washington, DC 20549**

**Form N–CR Current Report Money Market Fund Material Events**

**Part A: General Information**

Item A.1 Report for [mm/dd/yyyy].

Item A.2 CIK Number of registrant.

Item A.3 EDGAR Series Identifier.

Item A.4 Securities Act File Number.

Item A.5 Provide the name, email address, and telephone number of the person authorized to receive information and respond to questions about this Form N–CR.

**Part B: Default or Event of Insolvency of Portfolio Security Issuer**

If the issuer of one or more of the Fund's portfolio securities, or the issuer of a Demand Feature or Guarantee to which one of the Fund's portfolio securities is subject, and on which the Fund is relying to determine the quality, maturity, or liquidity of a portfolio security, experiences a default or Event of Insolvency (other than an immaterial default unrelated to the financial condition of the issuer), and the portfolio security or securities (or the securities subject to the Demand Feature or Guarantee) accounted for at least ½ of 1 percent of the Fund's Total Assets immediately before the default or Event of Insolvency, disclose the following information:

Item B.1 Security or securities affected.

Item B.2 Date(s) on which the default(s) or Event(s) of Insolvency occurred.

Item B.3 Value of affected security or securities on the date(s) on which

the default(s) or Event(s) of Insolvency occurred.

Item B.4 Percentage of the Fund's Total Assets represented by the affected security or securities.

Item B.5 Brief description of actions Fund plans to take in response to the default(s) or Event(s) of Insolvency.

*Instruction.* For purposes of Part B, an instrument subject to a Demand Feature or Guarantee will not be deemed to be in default (and an Event of Insolvency with respect to the security will not be deemed to have occurred) if: (i) in the case of an instrument subject to a Demand Feature, the Demand Feature has been exercised and the Fund has recovered either the principal amount or the amortized cost of the instrument, plus accrued interest; (ii) the provider of the Guarantee is continuing, without protest, to make payments as due on the instrument; or (iii) the provider of a Guarantee with respect to an Asset-Backed Security pursuant to rule 2a–7(a)(16)(ii) is continuing, without protest, to provide credit, liquidity or other support as necessary to permit the Asset-Backed Security to make payments as due.

**Part C: Provision of Financial Support to Fund**

If an affiliated person, promoter, or principal underwriter of the Fund, or an affiliated person of such a person, provides any form of financial support to the Fund (including, for example, any capital contribution, purchase of a security from the Fund in reliance on § 270.17a–9, purchase of any defaulted or devalued security at par, purchase of Fund shares, execution of letter of credit or letter of indemnity, capital support agreement (whether or not the Fund ultimately received support), or performance guarantee, or any other similar action to increase the value of the Fund's portfolio or otherwise support the Fund during times of stress), disclose the following information:

Item C.1 Description of nature of support.

Item C.2 Person providing support.

Item C.3 Brief description of relationship between the person providing support and the Fund.

Item C.4 Brief description of reason for support.

Item C.5 Date support provided.

Item C.6 Amount of support.

Item C.7 Security supported (if applicable).

Item C.8 Value of security supported on date support was initiated (if applicable).

Item C.9 Term of support.

Item C.10 Brief description of any contractual restrictions relating to support.

*Instruction.* If an affiliated person, promoter, or principal underwriter of the Fund, or an affiliated person of such a person, purchases a security from the Fund in reliance on § 270.17a–9, the Fund must provide the purchase price of the security in responding to Item C.6.

**Part D: Deviation Between Current Net Asset Value per Share and Intended Stable Price per Share**

If a Fund's current net asset value per share (rounded to the fourth decimal place in the case of a fund with a $1.00 share price, or an equivalent level of accuracy for funds with a different share price) deviates downward from its intended stable price per share by more than ¼ of 1 percent, disclose:

Item D.1 Date(s) on which such deviation exceeded ¼ of 1 percent.

Item D.2 Extent of deviation between the Fund's current net asset value per share and its intended stable price per share.

Item D.3 Principal reason for the deviation, including the name of any security whose value calculated using available market quotations (or an appropriate substitute that reflects current market conditions) or sale price, or whose issuer's downgrade, default, or event of insolvency (or similar event), has contributed to the deviation.

**Part E: Imposition of Liquidity Fee**

If, at the end of a business day, a Fund (except any Fund that is subject to the exemption provisions of rule 2a–7(c)(2)(iii) and that has chosen to rely on the rule 2a–7(c)(2)(iii) exemption provisions) has invested less than fifteen percent of its Total Assets in weekly liquid assets (as provided in rule 2a–7(c)(2)), disclose the following information:

Item E.1 Initial date on which the Fund invested less than fifteen percent of its Total Assets in weekly liquid assets.

Item E.2 If the Fund imposes a liquidity fee pursuant to rule 2a–7(c)(2)(i), date on which the Fund instituted the liquidity fee.

Item E.3 Brief description of the facts and circumstances leading to the Fund's investing less than fifteen percent of its Total Assets in weekly liquid assets.

Item E.4 Short discussion of the board of directors' analysis supporting its decision that imposing a liquidity fee pursuant to rule 2a–7(c)(2)(i) (or not imposing such a liquidity fee) would be in the best interest of the Fund.

*Instruction.* A Fund must file a report on Form N–CR responding to Items E.1 and E.2 on the first business day after the initial date on which the Fund has invested less than fifteen percent of its Total Assets in weekly liquid assets. A Fund must amend its initial report on Form N–CR to respond to Items E.3 and E.4 by the fourth business day after the initial date on which the Fund has invested less than fifteen percent of its Total Assets in weekly liquid assets.

**Part F: Suspension of Fund Redemptions**

If a Fund (except any Fund that is subject to the exemption provisions of rule 2a–7(c)(2)(iii) and that has chosen to rely on the rule 2a–7(c)(2)(iii) exemption provisions) that has invested less than fifteen percent of its Total Assets in weekly liquid assets (as provided in rule 2a–7(c)(2)) suspends the Fund's redemptions pursuant to rule 2a–7(c)(2)(ii), disclose the following information:

Item F.1 Initial date on which the Fund invested less than fifteen percent of its Total Assets in weekly liquid assets.

Item F.2 Date on which the Fund initially suspended redemptions.

Item F.3 Brief description of the facts and circumstances leading to the Fund's investing less than fifteen percent of its Total Assets in weekly liquid assets.

Item F.4 Short discussion of the board of directors' analysis supporting its decision to suspend the Fund's redemptions.

*Instruction.* A Fund must file a report on Form N–CR responding to Items F.1 and F.2 on the first business day after the initial date on which the Fund suspends redemptions. A Fund must amend its initial report on Form N–CR to respond to Items F.3 and F.4 by the fourth business day after the initial date on which the Fund suspends redemptions.

**Part G: Removal of Liquidity Fees and/or Resumption of Fund Redemptions**

If a Fund (except any Fund that is subject to the exemption provisions of rule 2a–7(c)(2)(iii) and that has chosen to rely on the rule 2a–7(c)(2)(iii) exemption provisions) that has imposed a liquidity fee and/or suspended the Fund's redemptions pursuant to rule 2a–7(c)(2) determines to remove such fee and/or resume fund redemptions, disclose the following, as applicable:

Item G.1 Date on which the Fund removed the liquidity fee and/or resumed Fund redemptions.

**Signatures**

Pursuant to the requirements of the Investment Company Act of 1940, the registrant has duly caused this report to be signed on its behalf by the undersigned hereunto duly authorized.

_____

(Registrant)

Date _____

_____

(Signature) *

* Print name and title of the signing officer under his/her signature.

## PART 279—FORMS PRESCRIBED UNDER THE INVESTMENT ADVISERS ACT OF 1940

■ 8. The authority citation for part 279 continues to read as follows:

**Authority:** The Investment Advisers Act of 1940, 15 U.S.C. 80b–1, *et seq.*

■ 19. Form PF (referenced in § 279.9) is amended by:

■ a. In General Instruction 15, removing the reference to Question 57 from the last bulleted sentence;

■ b. Revising section 3 to read as follows;

■ c. Redesignating Questions 65–79 in section 4 to 66–80;

■ d. In newly designated question 67(b) in section 4, revising the reference to ''Question 66(a)'' to read ''Question 67(a)'';

■ e. In newly designated question 76(b) in section 4, revising the reference to ''Question 75(a)'' to read ''Question 76(a)'';

■ f. In newly designated question 77(b) in section 4, revising the reference to ''Question 76(a)'' to read ''Question 77(a)''; and

■ g. In the Glossary of Terms, adding and revising certain terms.

The additions and revisions read as follows:

**Note:** The text of Form PF does not, and this amendment will not, appear in the Code of Federal Regulations.

**Form PF**

* * * * *

**Section 3**

BILLING CODE 8011–01–P

**Section 3: Information about *liquidity funds* that you advise.**

You must complete a separate Section 3 for each *liquidity fund* that you advise. However, with respect to *master-feeder arrangements* and *parallel fund structures*, you may report collectively or separately about the component funds as provided in the General Instructions.

**Item A. *Reporting fund* identifying and operational information**

51. (a) Name of the *reporting fund* ..... [ ]

(b) *Private fund* identification number of the *reporting fund* ..... [ ]

52. Does the *reporting fund* use the amortized cost method of valuation in computing its *net asset value*?

☐ Yes ☐ No

53. Does the *reporting fund* use the penny rounding method of pricing in computing its *net asset value*?

☐ Yes ☐ No

54. (a) Does the *reporting fund* have a policy of complying with the *risk limiting conditions* of *rule 2a-7*?

☐ Yes ☐ No

(b) If you responded "no" to Question 54(a) above, does the *reporting fund* have a policy of complying with the following provisions of *rule 2a-7*:

(i) the diversification conditions? ☐ Yes ☐ No

(ii) the credit quality conditions? ☐ Yes ☐ No

(iii) the liquidity conditions? ☐ Yes ☐ No

(iv) the maturity conditions? ☐ Yes ☐ No

**Item B. *Reporting fund* assets**

55. Provide the following information for each month of the *reporting period.*

| | | 1st Month | 2nd Month | 3rd Month |
|---|---|---|---|---|
| (a) | Net asset value of *reporting fund* as reported to current and prospective investors | | | |
| (b) | Net asset value per share of *reporting fund* as reported to current and prospective investors *(to the nearest hundredth of a cent)* | | | |
| (c) | Net asset value per share of *reporting fund (to the nearest hundredth of a cent; exclude the value of any capital support agreement or similar arrangement)* | | | |
| (d) | *WAM* of *reporting fund (in days)* | | | |
| (e) | *WAL* of *reporting fund (in days)* | | | |
| (f) | *7-day gross yield* of *reporting fund (to the nearest hundredth of one percent)* | | | |
| (g) | Dollar amount of the *reporting fund's* assets that are *daily liquid assets* | | | |
| (h) | Dollar amount of the *reporting fund's* assets that are *weekly liquid assets* | | | |
| (i) | Dollar amount of the *reporting fund's* assets that have a *maturity* greater than 397 days | | | |

**Item C. Financing information**

56. (a) Is the amount of total *borrowing* reported in response to Question 12 equal to or greater than 5% of the *reporting fund's net asset value*?

☐ Yes ☐ No

(b) If you responded "yes" to Question 56(a) above, divide the dollar amount of total *borrowing* reported in response to Question 12 among the periods specified below depending on the type of *borrowing*, the type of creditor and the latest date on which the reporting fund may repay the principal amount of the *borrowing* without defaulting or incurring penalties or additional fees.

*(If a creditor (or syndicate or administrative/collateral agent) is permitted to vary unilaterally the economic terms of the financing or to revalue posted collateral in its own discretion and demand additional collateral, then the* borrowing *should be*

*deemed to have a maturity of 1 day or less for purposes of this question. For amortizing loans, each amortization payment should be treated separately and grouped with other* borrowings *based on its payment date.)*

*(The total amount of* borrowings *reported below should equal approximately the total amount of* borrowing *reported in response to Question 12.)*

| | 1 day or less | 2 days to 7 days | 8 days to 30 days | 31 days to 397 days | Greater than 397 days |
|---|---|---|---|---|---|
| (i) *Unsecured borrowing* | | | | | |
| (A) *U.S. financial institutions* | | | | | |
| (B) *Non-U.S. financial institutions* | | | | | |
| (C) Other U.S. creditors | | | | | |
| (D) Other non-U.S. creditors | | | | | |
| (ii) *Secured borrowing* | | | | | |
| (A) *U.S. financial institutions* | | | | | |
| (B) *Non-U.S. financial institutions* | | | | | |
| (C) Other U.S. creditors | | | | | |
| (D) Other non-U.S. creditors | | | | | |

57. (a) Does the *reporting fund* have in place one or more committed liquidity facilities?

☐ Yes ☐ No

(b) If you responded "yes" to Question 57(a), provide the aggregate dollar amount of commitments under the liquidity facilities.....

**Item D. Investor information**

58. Specify the number of outstanding shares or units of the *reporting fund's* stock or similar securities .....

59. Provide the following information regarding investor concentration.

*(For purposes of this question, if you know that two or more beneficial owners of the* reporting fund *are* affiliated *with each other, you should treat them as a single beneficial owner.)*

(a) Specify the percentage of the *reporting fund's* equity that is beneficially owned by the beneficial owner having the largest equity interest in the *reporting fund*.....

(b) How many investors beneficially own 5% or more of the *reporting fund's* equity?

60. Provide a good faith estimate, as of the *data reporting date*, of the percentage of the *reporting fund's* outstanding equity that was purchased using *securities lending collateral* ..... [ ]

61. Provide the following information regarding the restrictions on withdrawals and redemptions by investors in the *reporting fund*.

*(For Questions 61 and 62, please note that the standards for imposing suspensions and restrictions on withdrawals/redemptions may vary among funds. Make a good faith determination of the provisions that would likely be triggered during conditions that you view as significant market stress.)*

As of the *data reporting date*, what percentage of the *reporting fund's net asset value*, if any:

(a) May be subjected to a suspension of investor withdrawals/redemptions by an adviser or fund governing body *(this question relates to an adviser's or* [ ]

62. Investor liquidity (as a % of *net asset value*):

*(Divide the* reporting fund's net asset value *among the periods specified below depending on the shortest period within which investors are entitled, under the fund documents, to withdraw invested funds or receive redemption payments, as applicable. Assume that you would impose gates where applicable but that you would not completely suspend withdrawals/redemptions and that there are no redemption fees. Please base on the notice period before the valuation date rather than the date proceeds would be paid to investors. The total should add up to 100%.)*

| | **% of *NAV* locked for** |
|---|---|
| 1 day or less ..... | |
| 2 days – 7 days..... | |
| 8 days – 30 days ..... | |
| 31 days – 90 days ..... | |
| 91 days – 180 days ..... | |
| 181 days – 365 days..... | |
| Longer than 365 days..... | |

**Item E. Portfolio Information**

63. For each security held by the *reporting fund*, provide the following information for each month of the *reporting period*.

(a) Name of the issuer .....

(b) Title of the issue .....

(c) CUSIP. .....

(d) *LEI*, if available .....

(e) In addition to CUSIP and *LEI*, provide at least one of the following other identifiers, if available:

ISIN .....

CIK .....

Other unique identifier .....

(f) The category of investment that most closely identifies the instrument .....

*(Select from among the following categories of investment: U.S. Treasury Debt; U.S. Government Agency Debt; Non U.S. Sovereign Debt; Non U.S. Sub-Sovereign Debt; Variable Rate Demand Note; Other Municipal Debt; Financial Company Commercial Paper; Asset Backed Commercial Paper; Other Asset Backed Security; Non-Financial Company Commercial Paper; Collateralized Commercial Paper; Certificate of Deposit (including Time Deposits and Euro Time Deposits); Structured Investment Vehicle Note; Other Note; U.S. Treasury Repurchase Agreement; Government Agency Repurchase Agreement; Other Repurchase Agreement; Insurance Company Funding Agreement; Investment Company; Other Instrument. If Other Instrument, include a brief description.)*

(g) For repos, specify whether the repo is "open" (*i.e.*, the repo has no specified end date and, by its terms, will be extended or "rolled" each business day (or at another specified period) unless the investor chooses to terminate it), and provide the following information about the securities subject to the repo (*i.e.*, the collateral):

*(If multiple securities of an issuer are subject to the repo, the securities may be aggregated, in which case provide: (i) the total principal amount and value and (ii) the range of maturity dates and interest rates.)*

Whether the repo is "open" .....

Name of the collateral issuer .....

CUSIP .....

*LEI*, if available .....

Maturity date .....

Coupon or yield .....

The principal amount, to the nearest cent.....

Value of the collateral, to the nearest cent.....

The category of investment that most closely represents the collateral .....

*(Select from among the following categories of investment: U.S. Treasury Debt; U.S. Government Agency Debt; Non U.S. Sovereign Debt; Non U.S. Sub-Sovereign Debt; Variable Rate Demand Note; Other Municipal Debt; Financial Company Commercial Paper; Asset Backed Commercial Paper; Other Asset Backed Security; Non-Financial Company Commercial Paper; Collateralized Commercial Paper; Certificate of Deposit (including Time Deposits and Euro Time Deposits); Structured Investment Vehicle Note; Equity; Corporate Bond; Exchange Traded Fund; Trust Receipt (other than for U.S. Treasuries); Derivative; Other Instrument. If Other Instrument, include a brief description.)*

(h) If the rating assigned by a *credit rating agency* played a substantial role in the *reporting fund's* (or its adviser's) evaluation of the quality, maturity or liquidity of the security, provide the name of each *credit rating agency* and the rating each assigned to the security.

(i) The maturity date used to calculate *WAM*.....

(j) The maturity date used to calculate *WAL* .....

(k) The final legal maturity date (*i.e.*, the date on which, in accordance with the terms of the security without regard to any interest rate readjustment or *demand feature*, the principal amount must unconditionally be paid) ...

(l) If the security has a *demand feature* on which the *reporting fund* (or its adviser) is relying when evaluating the quality, maturity, or liquidity of the security, provide the following information:

*(If the security does not have such a* demand feature*, enter "NA.")*

Identity of the *demand feature* issuer(s) .....

If the rating assigned by a *credit rating agency* played a substantial role in the *reporting fund's* (or its adviser's) evaluation of the quality, maturity or liquidity of the *demand feature*, its issuer, or the security to which it relates, provide the name of each *credit rating agency* and the rating assigned by each *credit rating agency*.....

The period remaining until the principal amount of the security may be recovered through the *demand feature* .....

The amount (*i.e.*, percentage) of fractional support provided by each *demand feature* issuer.....

Whether the *demand feature* is a *conditional demand feature* .....

(m) If the security has a *guarantee* (other than an unconditional letter of credit reported in response to Question 63(l) above) on which the *reporting fund* (or its adviser) is relying when evaluating the quality, maturity, or liquidity of the security, provide the following information:

*(If the security does not have such a* guarantee*, enter NA.")*

Identity of the *guarantor(s)* .....

If the rating assigned by a *credit rating agency* played a substantial role in the *reporting fund's* (or its adviser's) evaluation of the quality, maturity or liquidity of the *guarantee*, the *guarantor*, or the security to which the *guarantee* relates, provide the name of each *credit rating agency* and the rating assigned by each *credit rating agency* .....

The amount (*i.e.*, percentage) of fractional support provided by each *guarantor* .....

(n) If the security has any enhancements, other than those identified in response to Questions 63(l) and (m) above, on which the *reporting fund* (or its adviser) is relying when evaluating the quality, maturity, or liquidity of the security, provide the following information:

*(If the security does not have such an enhancement, enter "NA.")*

Identity of the enhancement provider(s) .....

The type of enhancement(s) .....

If the rating assigned by a *credit rating agency* played a substantial role in the *reporting fund's* (or its adviser's) evaluation of the quality, maturity or liquidity of the enhancement, its provider, or the security to which it relates, provide the name of each *credit rating agency* and the rating assigned by the *credit rating agency* ...

The amount (*i.e.*, percentage) of fractional support provided by each enhancement provider.....

(o) The following information for each security held by the *reporting fund*, reported separately for each lot purchased:

The total principal amount, to the nearest cent.....

The purchase date(s) .....

The yield at purchase.....

The yield as of the end of each month during the *reporting period* (for floating or variable rate securities, if applicable) .....

The purchase price (as a percentage of par, rounded to the nearest one thousandth of one percent) .....

(p) The total *value* of the *reporting fund's* position in the security, and separately, if the *reporting fund* uses the amortized cost method of valuation, the amortized cost value, in both cases to the nearest cent:

Including the value of any sponsor support.....

Excluding the value of any sponsor support.....

(q) The percentage of the *reporting fund's* net assets invested in the security, to the nearest hundredth of a percent.....

(r) Is the security categorized as a level 1, 2, or 3 asset or liability in

Question 14?

(s) Is the security a *daily liquid asset*?

(t) Is the security a *weekly liquid asset*?

(u) Is the security an *illiquid security*?

(v) Explanatory notes. Disclose any other information that may be material to other disclosures related to the portfolio security.

*(If none, leave blank.)*

**Item F. Securities Sold During the *Reporting Period***

| | | |
|---|---|---|
| (a) | The total principal amount, to the nearest cent..... | |
| (b) | The purchase price (as a percentage of par, rounded to the nearest one thousandth of one percent) ..... | |
| (c) | The sale date(s) ..... | |
| (d) | The yield at sale..... | |
| (e) | The sale price (as a percentage of par, rounded to the nearest one thousandth of one percent)..... | |

**Item G. Parallel Money Market Funds**

| | |
|---|---|
| 65. If the *reporting fund* pursues substantially the same investment objective and strategy and invests side by side in substantially the same positions as a *money market fund* advised by you or any of your *related persons*, provide the *money market fund's* EDGAR series identifier ..... *(If neither you nor any of your* related persons *advise such a* money market fund*, enter "NA.")* | |

* * * * *

**GLOSSARY OF TERMS**

* * * * *

*Conditional demand feature* Has the meaning provided in *rule 2a–7.*

* * * * *

*Credit rating agency* Any nationally recognized statistical rating organizations, as that term is defined in section 3(a)(62) of the Securities Exchange Act of 1934.

* * * * *

*Demand feature* Has the meaning provided in *rule 2a–7.*

* * * * *

*Guarantee* For purposes of Question 63, has the meaning provided in paragraph (a)(16)(i) of *rule 2a–7.*

*Guarantor* For purposes of Question 63, the provider of any *guarantee.*

* * * * *

*Illiquid security* Has the meaning provided in *rule 2a–7.*

* * * * *

*Maturity* The maturity of the relevant asset, determined without reference to the maturity shortening provisions contained in paragraph (i) of *rule 2a–7* regarding interest rate readjustments.

* * * * *

*Risk limiting conditions* The conditions specified in paragraph (d) of *rule 2a–7.*

* * * * *

*WAL* Weighted average portfolio maturity of a *liquidity fund* calculated taking into account the maturity shortening provisions contained in paragraph (i) of *rule 2a–7,* but determined without reference to the exceptions in paragraph (i) of *rule 2a–7* regarding interest rate readjustments.

*WAM* Weighted average portfolio maturity of a *liquidity fund* calculated taking into account the maturity shortening provisions contained in paragraph (i) of *rule 2a–7*

By the Commission.

Dated: June 5, 2013.

**Elizabeth M. Murphy,**

*Secretary.*

[FR Doc. 2013–13687 Filed 6–18–13; 8:45 am]

BILLING CODE 8011–01–P