

SECURITIES AND EXCHANGE COMMISSION

17 CFR Parts 270 and 274

[Release No. IC-29132; File Nos. S7-11-09, S7-20-09]

RIN 3235-AK33

Money Market Fund Reform

AGENCY: Securities and Exchange Commission.

ACTION: Final rule.

SUMMARY: The Securities and Exchange Commission (“Commission” or “SEC”) is adopting amendments to certain rules that govern money market funds under the Investment Company Act of 1940. The amendments will tighten the risk-limiting conditions of rule 2a-7 by, among other things, requiring funds to maintain a portion of their portfolios in instruments that can be readily converted to cash, reducing the maximum weighted average maturity of portfolio holdings, and improving the quality of portfolio securities; require money market funds to report their portfolio holdings monthly to the Commission; and permit a money market fund that has “broken the buck” (i.e., re-priced its securities below \$1.00 per share), or is at imminent risk of breaking the buck, to suspend redemptions to allow for the orderly liquidation of fund assets. The amendments are designed to make money market funds more resilient to certain short-term market risks, and to provide greater protections for investors in a money market fund that is unable to maintain a stable net asset value per share.

DATES: The rules, rule amendments, and form are effective May 5, 2010. The expiration date for 17 CFR 270.30b1-6T is extended from September 17, 2010 to December 1, 2010. Compliance dates are discussed in Section III of the **SUPPLEMENTARY INFORMATION.**

FOR FURTHER INFORMATION CONTACT: Office of Regulatory Policy, 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 adopting amendments to rules 2a-7 [17 CFR 270.2a-7], 17a-9 [17 CFR 270.17a-9] and 30b1-6T [17 CFR 270.30b1-6T], new rules 22e-3 [17 CFR 270.22e-3] and 30b1-7 [17 CFR 270.30b1-7], and new Form N-MFP [17 CFR 274.201] under the Investment

Company Act of 1940 (“Investment Company Act” or “Act”).¹

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I. Background

On June 30, 2009, the Commission issued a release proposing new rules and rule amendments governing the operation of money market funds.² Money market funds are open-end management investment companies that are registered under the Investment Company Act. They invest in high-quality, short-term debt instruments such as commercial paper, Treasury bills and repurchase agreements. Money market funds pay dividends that reflect prevailing short-term interest rates and, unlike other investment companies, maintain a stable net asset value per share (or “NAV”), typically \$1.00 per

¹ 15 U.S.C. 80a. 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, are to Title 17, Part 270 of the Code of Federal Regulations [17 CFR 270]. References to “current” rules relate to rules in their current form [17 CFR Part 270 (2009 version)], and references to “amended” rules relate to rules as they will be amended by this Release.

² Money Market Fund Reform, Investment Company Act Release No. 28807 (June 30, 2009) [74 FR 32688 (July 8, 2009)] (“Proposing Release”). All references to “proposed” rules relate to rules as proposed in the Proposing Release.

share. Money market funds have over \$3.3 trillion dollars in assets under management, and comprise over 30 percent of the assets of registered investment companies.³

All money market funds are subject to rule 2a-7 under the Investment Company Act. Rule 2a-7, among other things, facilitates money market funds’ ability to maintain a stable net asset value per share by permitting them to use the amortized cost method of valuation and the penny-rounding method of pricing.⁴ But for rule 2a-7, the Investment Company Act and our rules would require a money market fund to calculate its current net asset value per share by valuing portfolio securities at their current value (“mark-to-market”).⁵

Under the amortized cost method, portfolio securities generally are valued at cost plus any amortization of premium or accumulation of discount. The basic premise underlying money market funds’ use of the amortized cost method of valuation is that high-quality, short-term debt securities held until maturity will eventually return to their amortized cost value, regardless of any current disparity between the amortized cost value and market value, and would not ordinarily be expected to fluctuate significantly in value.⁶ Therefore, the rule permits money market funds to value portfolio securities at their amortized cost so long as the deviation between the portfolio’s amortized cost

³ See Investment Company Institute, *Trends in Mutual Fund Investing*, Nov. 2009, available at http://www.ici.org/research/stats/trends/trends_11_09.

⁴ Current rule 2a-7(a)(2) defines the amortized cost method as the method of calculating an investment company’s net asset value per share (or “NAV”) whereby portfolio securities are valued at the fund’s acquisition cost as adjusted for amortization of premium or accretion of discount rather than at their value based on current market factors. The penny-rounding method of pricing means the method of computing a fund’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. See current rule 2a-7(a)(18).

⁵ See section 2(a)(41) of the Act (defining “value” of fund assets); rule 2a-4 (defining “current net asset value” for use in computing the current price of a redeemable security); and rule 22c-1 (generally requiring open-end funds to sell and redeem their shares at a price based on the funds’ current net asset value as next computed after receipt of a redemption, purchase, or sale order).

⁶ See 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”) at nn.3-7 and accompanying text; 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. 12206 (Feb. 1, 1982) [47 FR 5428 (Feb. 5, 1982)] at nn.3-4 and accompanying text.

and current market value *remains* minimal and results in the computation of a share price that represents fairly the current net asset value per share of the fund.⁷

To reduce the likelihood of a material deviation occurring between the amortized cost value of a portfolio and its market-based value, the rule contains several conditions (which we refer to as “risk-limiting conditions”) that limit the fund’s exposure to certain risks, such as credit, currency, and interest rate risks.⁸ In addition, the rule includes certain procedural requirements overseen by the fund’s board of directors. One of the most important is the requirement that the fund periodically “shadow price” the amortized cost net asset value of the fund’s portfolio against the mark-to-market net asset value of the portfolio.⁹ If there is a difference of more than one-half of one percent (or \$0.005 per share), the fund’s board of directors must consider promptly what action, if any, should be taken, including whether the fund should discontinue the use of the amortized cost method of valuation and re-price the securities of the fund below (or above) \$1.00 per share, an event colloquially known as “breaking the buck.”¹⁰

As discussed in significant detail in the Proposing Release, during 2007–2008 money market funds were exposed to substantial losses, first as a result of exposure to debt securities issued by structured investment vehicles (“SIVs”),

⁷ See amended rule 2a–7(c)(1), (c)(8)(ii)(B)–(C) (requiring, among other things, that the fund’s board of directors promptly consider what action, if any, should be taken if the deviation between the money market fund’s current market value and the fund’s amortized cost price per share exceeds ½ of 1%).

⁸ For example, the current rule requires, among other things, that a money market fund’s portfolio securities meet certain credit quality requirements, such as being rated in the top one or two rating categories by nationally recognized statistical rating organizations (“NRSROs”). A fund, moreover, may only invest a limited portion of its portfolio in securities rated in the second highest rating category. See current rule 2a–7(c)(3). The current rule also places limits on the remaining maturity of securities in the fund’s portfolio. A fund generally may not acquire, for example, any securities with a remaining maturity greater than 397 days, and the dollar-weighted average maturity of the securities owned by the fund may not exceed 90 days. See current rule 2a–7(c)(2).

⁹ See current rule 2a–7(c)(7) (requiring that such shadow pricing be calculated at such intervals as the board of directors determines appropriate and reasonable in light of current market conditions).

¹⁰ See current rule 2a–7(c)(7)(ii)(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. Current rule 2a–7(c)(7)(ii)(C). See 1983 Adopting Release, *supra* note 6, at nn.51–52 and accompanying text.

and then as a result of the default of debt securities issued by Lehman Brothers Holdings Inc. (“Lehman Brothers”). All but one of the funds that were exposed to losses from SIV and Lehman Brothers securities obtained support of some type from their advisers or other affiliated persons, which absorbed the losses or provided a guarantee covering a sufficient amount of losses to prevent the fund from breaking the buck. The Reserve Primary Fund, which held a \$785 million position in Lehman Brothers debt, ultimately did not have a sponsor with sufficient resources to support it, and on September 16, 2008 the fund announced that it would re-price its securities at \$0.97 per share.¹¹ It subsequently suspended redemptions as of September 17, 2008.¹²

The cumulative effect of these events, when combined with general turbulence in the financial markets, led to a run primarily on institutional taxable prime money market funds, which contributed to severe dislocations in short-term credit markets and strains on the businesses and institutions that obtain funding in those markets.¹³ During the week of September 15, 2008, investors withdrew approximately \$300 billion from taxable prime money market funds, or 14 percent of the assets held in those funds.¹⁴ In the final two weeks

¹¹ See Proposing Release, *supra* note 2, at n.44 and accompanying text. The Reserve Primary Fund distributed the bulk of its assets, and investors have received more than \$0.98 on the dollar. See Press Release, SEC, Reserve Primary Fund Distributes Assets to Investors (Jan. 29, 2010) available at [http://www.sec.gov/news/press/2010-16.htm](http://www.sec.gov/news/press/2010/2010-16.htm).

¹² In response to a request by The Reserve Fund, the Commission issued an order permitting the suspension of redemptions in certain Reserve funds, to permit their orderly liquidation. See In the Matter of The Reserve Fund, Investment Company Act Release No. 28386 (Sept. 22, 2008) [73 FR 55572 (Sept. 25, 2008)] (order). Several other Reserve funds also obtained an order from the Commission on October 24, 2008 permitting them to suspend redemptions to allow for their orderly liquidation. See Reserve Municipal Money-Market Trust, et al., Investment Company Act Release No. 28466 (Oct. 24, 2008) [73 FR 64993 (Oct. 31, 2008)] (order).

¹³ See *Minutes of the Federal Open Market Committee*, Federal Reserve Board, Oct. 28–29, 2008, at 5, available at <http://www.federalreserve.gov/monetarypolicy/files/fomcminutes20081029.pdf> (“FRB Open Market Committee Oct. 28–29 Minutes”). See also Press Release, Federal Reserve Board, Board Announces Creation of the Commercial Paper Funding Facility (CPFF) to Help Provide Liquidity to Term Funding Markets (Oct. 7, 2008), available at <http://www.federalreserve.gov/newsevents/press/monetary/20081007c.htm>.

¹⁴ 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); see also Investment Company Institute, *Money Market Mutual Fund Assets Historical Data*, available at <http://www.ici.org/pdf/>

of September 2008, money market funds reduced their holdings of top-rated commercial paper by \$200.3 billion, or 29 percent.¹⁵

On September 19, 2008, the U.S. Department of the Treasury (“Treasury Department”) and the Board of Governors of the Federal Reserve System (“Federal Reserve Board”) announced an unprecedented intervention in the short-term markets. The Treasury Department announced its Temporary Guarantee Program for Money Market Funds (“Guarantee Program”), which temporarily guaranteed certain investments in money market funds that decided to participate in the program.¹⁶ This program has now expired.¹⁷ The Federal Reserve Board announced the creation of its Asset-Backed Commercial Paper Money Market Mutual Fund Liquidity Facility (“AMLF”), through which it extended credit to U.S. banks and bank holding companies to finance their purchases of high-quality asset backed commercial paper from money market funds.¹⁸ These programs were effective in containing the run on institutional prime money market funds and providing additional liquidity to money market funds.¹⁹

mm_data_2010.pdf (“ICI Mutual Fund Historical Data”).

¹⁵ See 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=a5hvnKFC_pQ.

¹⁶ See Press Release, Treasury Department, Treasury Announces Guaranty Program for Money Market Funds (Sept. 19, 2008), available at <http://www.treas.gov/press/releases/hp1147.htm>. The Program insured investments in money market funds, to the extent of their shareholdings as of September 19, 2008, if the fund chose to participate in the Program. We adopted, on an interim final basis, a temporary rule, rule 22e–3T, to facilitate the ability of money market funds to participate in the Guarantee Program. The rule permitted a participating fund to suspend redemptions if it broke the buck and liquidated under the terms of the Program. 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)].

¹⁷ See Press Release, U.S. Department of the Treasury, Treasury Announces Expiration of Guaranty Program for Money Market Funds (Sept. 18, 2009), available at <http://www.treas.gov/press/releases/tg293.htm>. The Program expired on September 19, 2009, and rule 22e–3T expired on October 18, 2009.

¹⁸ See Press Release, Federal Reserve Board, Federal Reserve Board Announces Two Enhancements to its Programs to Provide Liquidity to Markets (Sept. 19, 2008), available at <http://www.federalreserve.gov/newsevents/press/monetary/20080919a.htm>. The AMLF expired on February 1, 2010. See Press Release, Federal Reserve Board, FOMC Statement (Jan. 27, 2010), available at <http://www.federalreserve.gov/newsevents/press/monetary/20100127a.htm>.

¹⁹ During the week ending September 18, 2008, taxable institutional money market funds

The severity of the problems experienced by money market funds during 2007 and 2008 prompted us to review our regulation of money market funds. We sought to better understand how we might revise rule 2a–7 to reduce the susceptibility of money market funds to runs and reduce the consequences of a run on fund shareholders. Our staff consulted extensively with staff from other members of the President’s Working Group on Financial Markets. We talked to many market participants, and reviewed a report from a “Money Market Fund Working Group” assembled by the Investment Company Institute (“ICI Report”), which recommended a number of changes.²⁰

Our June 2009 proposals were the product of that review and were, we explained, a first step to addressing regulatory concerns we identified. They were designed to make money market funds more resilient and less likely to break a buck as a result of disruptions such as those that occurred in the fall of 2008. They would give us better tools to oversee money market funds. If a money market fund did break a buck, they would facilitate an orderly liquidation in order to protect fund shareholders and help contain adverse effects on the capital markets and other money market funds. In addition, throughout the Proposing Release we requested comment on additional regulatory changes aimed at further strengthening the stability of money market funds.

We received approximately 120 comments on the rule, including approximately 45 comments from investment companies and their representatives, 22 from debt security issuers, and 30 from individuals, including investors and academics. The comment letters reflected a wide variety of views on most of the topics discussed in the Proposing Release. The investment companies generally supported those aspects of the proposal that were similar to those recommended in the ICI Report.²¹ Most of them

experienced net outflows of \$165 billion. See *Money Fund Assets Fell to \$3.4T in Latest Week*, Associated Press, Sept. 18, 2008. Almost \$80 billion was withdrawn from prime money market funds even after the announcement of the Guarantee Program on September 19, 2008. See Diana B. Henriques, *As Cash Leaves Money Funds, Financial Firms Sign Up for U.S. Protection*, N.Y. Times, Oct. 2, 2008, at C10. By the end of the week after the announcement, however, net outflows from taxable institutional money market funds had ceased. See *Money Fund Assets Fell to \$3.398T in Latest Week*, Associated Press, Sept. 25, 2008.

²⁰ ICI Report, *supra* note 14.

²¹ See, e.g., Comment Letter of T. Rowe Price Associates, Inc. (Sept. 8, 2009) (“T. Rowe Price Comment Letter”); Comment Letter of UBS Global

strongly objected to changes that would affect the stable net asset value that today is the principal characteristic of a money market fund.²² Most debt security issuers who wrote to us objected to changes designed to increase the credit quality of money market fund portfolios by precluding funds from investing in second tier securities (as defined by the rule).²³ Many fund commenters pointed to the historical stability of funds and urged us to be modest in our changes to rule 2a–7.²⁴ Some others, however, pointed to the near-cataclysmic events of September 2008 in supporting more substantial changes.²⁵

As we stated in the Proposing Release, we recognize that the events of 2007–2008 raise the question of whether further changes to the regulatory structure governing money market funds may be warranted. Accordingly, in the Proposing Release we requested comment on additional, more fundamental regulatory changes, some of which we recognized could transform the business and regulatory model on which money market funds have been operating for more than 30 years.²⁶ For example, we requested comment on whether money market funds should move to the “floating net asset value” used by other open-end investment companies.²⁷ We received over 75 comment letters addressing this issue. We have continued to explore possible more significant changes to the regulation of money market funds in light of these comments and through the staff’s work with members of the President’s Working Group. We expect

Asset Management (Americas) Inc. (Sept. 8, 2009); Comment Letter of The Vanguard Group, Inc. (Aug. 19, 2009) (“Vanguard Comment Letter”).

²² See, e.g., Comment Letter of BlackRock Inc. (Sept. 4, 2009) (“BlackRock Comment Letter”); Comment Letter of the Dreyfus Corporation (Sept. 8, 2009) (“Dreyfus Comment Letter”); Comment Letter of Goldman Sachs Asset Management, L.P. (Sept. 8, 2009) (“Goldman Sachs Comment Letter”).

²³ See, e.g., Comment Letter of American Electric Power Company, Inc. (Sept. 8, 2009) (“Am. Elec. P. Comment Letter”); Comment Letters of the U.S. Chamber of Commerce and Joint Treasurer Signatories (Sept. 3 & Sept. 24, 2009) (“Chamber/Tier 2 Issuers Comment Letter”); Comment Letter of Dominion Resources Services, Inc. (Sept. 8, 2009) (“Dominion Res. Comment Letter”).

²⁴ See, e.g., Comment Letter of Fidelity Investments (Aug. 24, 2009) (“Fidelity Comment Letter”); T. Rowe Price Comment Letter; Comment Letter of USAA Investment Management Company (Sept. 8, 2009) (“USAA Comment Letter”).

²⁵ See, e.g., Comment Letter of Deutsche Investment Management Americas Inc. (Aug. 31, 2009) (“Deutsche Comment Letter”); Comment Letter of Jeffrey N. Gordon, Professor of Law, Columbia Law School (Sept. 9, 2009); Comment Letter of John R. Jay, CFA (Sept. 8, 2009).

²⁶ See Proposing Release, *supra* note 2, at Section III.

²⁷ See *id.* at Section III.A.

to issue a release addressing these issues and proposing further reform to money market fund regulation.

II. Discussion

Today we are adopting the amendments we proposed last June to the rules governing money market funds, with several changes made in response to the comments we received. As described below in more detail, we believe these amendments will make money market funds more resilient and less likely to break the buck. They will further limit the risks money market funds may assume by, among other things, requiring them to increase the credit quality of fund portfolios and to reduce the maximum weighted average maturity of their portfolios, and by requiring for the first time that all money market funds maintain liquidity buffers that will help them withstand sudden demands for redemptions. The rule amendments require fund managers to stress test their portfolios against potential economic shocks such as sudden increases in interest rates, heavy redemptions, and potential defaults. They provide investors with more timely, relevant information about fund portfolios to hold fund managers more accountable for the risks they take. They will improve our ability to oversee money market funds. And finally, they provide a means to wind down the operations of a fund that does break the buck or suffers a run, in an orderly way that is fair to the fund’s investors and reduces the risk of market losses that could spread to other funds. We believe that these reforms collectively will better protect money market fund investors in times of financial market turmoil and lessen the possibility that the money market fund industry will not be able to withstand stresses similar to those experienced in 2007–08. Thus, we believe that each of the rules and rule amendments we are adopting is necessary or appropriate in the public interest and consistent with the protection of investors and the policies and purposes of the Investment Company Act.²⁸

A. Portfolio Quality

Rule 2a–7 limits a money market fund to investing in securities that are, at the time of their acquisition, “eligible securities,” which means that securities must have been rated in either of the two highest short-term debt ratings categories from the relevant NRSROs or are comparable to securities that have

²⁸ See section 6(c) of the Investment Company Act (under which rule 22e–3 and amendments to rules 2a–7 and 17a–9 are adopted).

been so rated in these categories.²⁹ Before a fund may invest in an “eligible security,” a fund’s board of directors (or its delegate) must also determine that the security presents minimal credit risks, which must be based on factors pertaining to credit quality in addition to any rating assigned to a security.³⁰

We are amending rule 2a–7 to reduce the amount of credit risk a money market fund may assume by limiting the securities in which money market funds may invest. We are also amending provisions of rule 2a–7 that address how NRSRO ratings are used in the rule.

1. Second Tier Securities

We are amending rule 2a–7 to further limit money market funds’ investments in “second tier securities.”³¹ Under the amendments, we are reducing permissible money market fund investments in second tier securities by (i) lowering the permitted percentage of a fund’s “total assets” that may be invested in second tier securities from five percent to three percent and (ii) lowering the permitted concentration of its total assets in second tier securities of a single issuer from the greater of one percent or \$1 million to one-half of one percent.³² In addition, money market funds will not be permitted to acquire any second tier security with a remaining maturity in excess of 45 days.³³

Last June, we proposed to prohibit money market funds from acquiring second tier securities, based on our analysis of the risks that these securities can pose to money market funds. We noted that second tier securities trade in thinner markets, generally have a weaker credit quality profile, and exhibited credit spreads that widened more dramatically than those of first tier securities during the 2008 financial turmoil.³⁴ During times of financial

market stress, we understand that these securities tend to become illiquid and sell in the secondary market, if at all, only at prices substantially discounted from their amortized cost value.³⁵ This additional risk created by the credit and liquidity profile of second tier securities increases the possibility that a fund holding these securities could break the buck in times of financial market turmoil, with a detrimental impact on fund investors.

Commenters were evenly divided between those supporting our proposed elimination of money market funds’ ability to acquire second tier securities and those against our proposal. In general, most money market fund sponsors who commented supported elimination,³⁶ while most issuers of second tier securities who commented opposed elimination.³⁷ Those supporting elimination argued that it would be an effective way to increase the safety of money market funds and would reduce the likelihood that a fund would break the buck. Some commenters noted that the money market funds they manage have not acquired second tier securities historically³⁸ because of second tier issuers’ weaker credit profiles, smaller issuer program sizes, and lower market liquidity.³⁹ A few commenters noted that eliminating money market funds’ ability to acquire second tier securities should result in minimal market

such spreads to spike shortly before and during recessions); Comment Letter of the Investment Company Institute (Sept. 8, 2009) (“ICI Comment Letter”) (noting that the market for Tier 2 commercial paper is less deep with fewer issuers than the Tier 1 market).

²⁹ See, e.g., Comment Letter of Invesco AIM Advisors, Inc. (Sept. 4, 2009) (“Invesco Aim Comment Letter”) (noting that it has historically avoided the second tier market due to, among other factors, the less overall market liquidity of second tier securities); ICI Comment Letter. See also Proposing Release, *supra* note 2, at Section II.A.1 for a discussion of the wider credit spreads of second tier securities during the fall of 2008, indicating the extent to which such securities traded at a discounted price.

³⁰ See, e.g., Comment Letter of Bankers Trust Company, N.A. (Aug. 28, 2009) (“Bankers Trust Comment Letter”); BlackRock Comment Letter; Comment Letter of Charles Schwab Investment Management, Inc. (Sept. 4, 2009) (“Charles Schwab Comment Letter”); Dreyfus Comment Letter; Vanguard Comment Letter. *But see* Comment Letter of Federated Investors, Inc. (Sept. 8, 2009) (“Federated Comment Letter”); Fidelity Comment Letter (opposing elimination).

³¹ See, e.g., Comment Letter of the American Securitization Forum (Sept. 8, 2009) (“Am. Securit. Forum Comment Letter”); Comment Letter of the U.S. Chamber of Commerce, Center for Capital Markets Competitiveness (Sept. 8, 2009) (“Chamber Comment Letter”); Dominion Res. Comment Letter; Comment Letter of XTO Energy Inc. (Sept. 3, 2009) (“XTO Energy Comment Letter”).

³² See, e.g., Dreyfus Comment Letter; Invesco Aim Comment Letter.

³³ See, e.g., Invesco Aim Comment Letter.

disruption because money market funds currently hold small amounts of such securities.⁴⁰

Commenters that opposed the proposal disagreed that second tier securities significantly increase risk at money market funds,⁴¹ argued that a complete ban would not be justified on a cost-benefit basis,⁴² and stated that a ban would have a material adverse impact on second tier security issuers.⁴³ Some commenters noted that in a report of default rates through 2006, second tier securities have default rates substantially similar to those of first tier securities.⁴⁴ These commenters also noted that rating agencies require that second tier security issuers establish backup liquidity lines of credit providing 100 percent coverage for any issuance.⁴⁵ Several commenters agreed

⁴⁰ See, e.g., ICI Comment Letter; Comment Letter of TD Asset Management (Sept. 8, 2009) (“TDAM Comment Letter”).

⁴¹ See, e.g., Comment Letter of the Association for Financial Professionals (Sept. 8, 2009) (“Assoc. Fin. Professionals Comment Letter”); Chamber/Tier 2 Issuers Comment Letter; Dominion Res. Comment Letter.

⁴² See, e.g., Comment Letter of Fund Democracy and the Consumer Federation of America (Sept. 8, 2009) (“CFA/Fund Democracy Comment Letter”); Chamber Comment Letter; Dominion Res. Comment Letter. *But see* TDAM Comment Letter (stating that the benefits of eliminating second tier securities will far outweigh any disadvantages).

⁴³ See, e.g., Chamber Comment Letter; Dominion Res. Comment Letter; Comment Letter of Treasury Strategies, Inc. (Sept. 8, 2009) (“Treasury Strategies Comment Letter”).

⁴⁴ Chamber Comment Letter; Chamber/Tier 2 Issuers Comment Letter. These commenters were citing the following study: Moody’s Investors Service, *Short-Term Corporate and Structured Finance Rating Transition Rates, 1972–2006* (June 2007), available at http://www.moody.com/cust/content/content.aspx?source=staticcontent/free%20pages/regulatory%20affairs/documents/st_corp_and_struct_transition_rates_06_07.pdf (showing, for example, a default rate for P–1 rated commercial paper over a 365 day time horizon of 0.02% versus a default rate for P–2 rated commercial paper of 0.10% over the same time horizon).

⁴⁵ We note, however, that commenters did not discuss conditions under which those issuers would not be permitted to draw on those backup liquidity facilities. It is our understanding that such backup liquidity facilities typically do not provide a full backstop of liquidity support because they contain conditions limiting an issuer’s ability to draw on the facility if the issuer has experienced a “material adverse change,” which would often occur if the financial situation of the issuer had declined due to financial market or other economic turmoil. *See also* Hahn, *supra* note 34 (stating that backup lines of credit generally will not be useful for a firm whose operating and financial condition has deteriorated to the point where it is about to default on its short-term liabilities because credit agreements often contain “material adverse change” clauses that allow banks to cancel credit lines if the financial condition of the firm changes significantly); Pu Shen, *Why Has the Nonfinancial Commercial Paper Market Shrunk Recently?*, Federal Reserve Bank of Kansas City Economic Review, at 69 (First Quarter 2003) (stating that

Continued

²⁹ Amended rule 2a–7(a)(12) (eligible security).

³⁰ Amended rule 2a–7(c)(3)(i) (portfolio quality).

³¹ 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* amended rule 2a–7(a)(24) (defining “second tier security”); amended rule 2a–7(a)(23) (defining “requisite NRSROs”).

³² *See* amended rule 2a–7(c)(3)(ii) (portfolio quality—second tier securities); amended rule 2a–7(c)(4)(i)(C) (portfolio diversification—second tier securities); amended rule 2a–7(a)(27) (defining “total assets”).

³³ *See* amended rule 2a–7(c)(3)(ii) (portfolio quality—second tier securities).

³⁴ *See* Proposing Release, *supra* note 2, at Section II.A.1. *See also* Thomas K. Hahn, *Commercial Paper* (Federal Reserve Bank of Richmond, Economic Quarterly Vol. 79/2, Spring 1993), at Fig. 4 (showing historical spreads between A–1/P–1 commercial paper and A–2/P–2 commercial paper between 1974 and 1992, including the tendency of

with our statement in the Proposing Release that second tier securities were not the direct cause of strains on money market funds during the 2007–2008 period.⁴⁶ A few stated that banning the acquisition of second tier securities would reduce diversification of money market fund portfolio holdings and thus increase risk, noting in particular that a greater percentage of second tier security issuers are not financial institutions, compared to first tier security issuers.⁴⁷

Commenters also asserted that prohibiting the acquisition of second tier securities would have unintended consequences for the capital markets. They stated that it might discourage investors other than money market funds from investing in second tier securities, causing a more substantial reduction in the issuance of second tier securities.⁴⁸ Some argued that if second

tier issuers are not able to issue sufficient commercial paper, they will be forced to borrow more from banks, which is a less flexible and more costly alternative that will increase borrowing costs.⁴⁹ Finally, two commenters stated that a complete ban on the acquisition of second tier securities by money market funds might have a negative effect on those issuers of first tier securities that are viewed as presenting a higher risk of being downgraded, because money market funds may elect not to invest in those securities out of concern that the securities might soon become second tier securities.⁵⁰

The focus of our concerns is and must be on the risk to money market funds and their shareholders from their investments in second tier securities. While, as commenters noted,⁵¹ second tier securities do not appear to be subject to substantially greater default risk than first tier securities they present

greater credit spread risk and trade in thinner markets,⁵² all of which can lead to greater price volatility and illiquidity in times of market stress.⁵³ While these characteristics may not pose the same degree of risk to money market funds as the likelihood that a security could default and become worthless, they can adversely affect money market funds' ability to maintain a stable net asset value. This is particularly the case given money market funds' narrow margin for deviation between the mark-to-market value of their assets and the amortized cost value of those assets, and the significant negative impact on money market funds and their investors if a fund breaks the buck.

Several commenters asserted that there are high-quality second tier securities available and that money market funds conducting a thorough credit risk analysis may conclude that certain second tier securities provide a higher yield than first tier securities while still maintaining a risk profile consistent with investment objectives for money market fund investment.⁵⁴ In these circumstances, investment in higher yielding second tier securities may benefit fund investors. These commenters suggested that, given these benefits, it may be more appropriate for

commercial paper backup facilities are only meant to provide emergency assistance for short-term liquidity difficulties and not to enhance the credit quality of issues); Standard & Poor's, *2008 Corporate Criteria: Commercial Paper*, at 3 (Apr. 15, 2008) ("Given the size of the CP market, backup facilities could not be relied on with a high degree of confidence in the event of widespread disruption.").

⁴⁶ See, e.g., Chamber/Tier 2 Issuers Comment Letter; Federated Comment Letter; Fidelity Comment Letter.

⁴⁷ See, e.g., Treasury Strategies Comment Letter; USAA Comment Letter; XTO Energy Comment Letter. We note that while a greater *percentage* of second tier security issuers do appear to be non-financial companies, there are a much greater *number* of non-financial first tier issuers and thus it is not clear that money market funds would not be able to achieve sufficient diversification in their portfolio holdings even if limited to acquiring first tier securities. The Chamber/Tier 2 Issuers Comment Letter also states that prohibiting money market funds from acquiring second tier securities would "cut the pool of *potential issuers* by 43%" (emphasis added). Any diversification is not driven only by the *number* of *potential* issuers, however. It is also determined by the amount of money market fund *assets* that can be *actually* allocated to different issuers. For example, while there are over 200 P–2 rated commercial paper programs, only approximately half of these programs are active in issuing *any* commercial paper and only 16 programs have an average quarterly outstanding issuance in excess of \$500 million. See American Securit. Forum Comment Letter. In addition, during the market turmoil of 2007 and 2008, second tier securities did not exhibit less risky or countervailing economic metrics relevant to money market funds maintaining a stable net asset value compared to first tier securities. See Proposing Release, *supra* note 2, at Section II.A.1, at n.98 and accompanying text and chart. In fact, AA-rated non-financial commercial paper did exhibit significantly greater price stability than A2/P2-rated non-financial commercial paper during the fall of 2008. See Federal Reserve Board, Commercial Paper Data, available at <http://www.federalreserve.gov/DataDownload/Choose.aspx?rel=CP> ("Federal Reserve Commercial Paper Data"). See also V.V. Chari, L. Christiano & P. Kehoe, *Facts and Myths about the Financial Crisis of 2008*, Federal Reserve Bank of Minneapolis Working Paper 666, at Fig. 7B (Oct. 2008).

⁴⁸ See, e.g., Chamber Comment Letter; Dominion Res. Comment Letter; Treasury Strategies Comment

Letter. Commenters asserted that eliminating money market funds' ability to acquire second tier securities might have a substantially greater adverse impact on second tier issuers, and thus potentially on capital formation because other investors in second tier securities or lesser quality first tier securities might avoid investment in those securities as a result of our rule amendments. Investor behavior in this regard is difficult to predict. It is equally likely that investors in second tier paper would demand higher yields, increasing issuers' financing costs. As discussed below, however, we are not precluding money market funds from investing in second tier securities. Accordingly, we do not need to reach a conclusion on this matter.

⁴⁹ See, e.g., Am. Elec. P. Comment Letter; Chamber/Tier 2 Issuers Comment Letter; Dominion Res. Comment Letter; XTO Energy Comment Letter. We note that money market funds hold a relatively low percentage of outstanding second tier commercial paper. See Bank of America Merrill Lynch, Tier-2 US Commercial Paper Market Update (Oct. 15, 2009) (attached to the Am. Securit. Forum Comment Letter) (indicating that over 75% of Tier-2 commercial paper is held by insurance firms, corporations and banks, and that only 11% is held by the asset management industry, which would include money market funds as well as other mutual funds and asset managers).

⁵⁰ Fidelity Comment Letter; USAA Comment Letter. Two other commenters suggested that the Commission should consider the effect of banning the acquisition of second tier securities on tax-exempt money market funds, and in particular single-State funds. See Dreyfus Comment Letter; Federated Comment Letter. As discussed further in the cost benefit analysis section of this Release, based on our review of money market fund portfolios in September 2008, very few money market funds, including tax-exempt funds, will be impacted by our amendments relating to second tier securities. The greatest potential impact on tax-exempt funds will be the 45-day maturity limitation for acquisition of second tier securities. Given the prevalence of variable rate demand notes among municipal securities, however, we believe that tax-exempt funds should be able to effectively manage the 45-day maturity limit without a substantial impact. Accordingly, we do not believe that a special accommodation for tax-exempt money market funds is required with respect to second tier securities.

⁵¹ See *supra* note 44 and accompanying text.

⁵² A few commenters argued that the increase in spreads of Tier 2 commercial paper over Tier 1 commercial paper during the fall of 2008 was due to the Federal Reserve Board's announcement of its creation of the Commercial Paper Funding Facility (CPFF) on October 7, 2008, which only supported issuance of 90-day Tier 1 commercial paper. See Chamber Comment Letter; Chamber/Tier 2 Issuers Comment Letter; Dominion Res. Comment Letter. We note, however, that spreads between Tier 1 and Tier 2 commercial paper widened significantly (by well over 300 basis points) immediately after the bankruptcy of Lehman Brothers was announced on September 14, 2008—well before the CPFF was announced on October 7. See Federal Reserve Commercial Paper Data, *supra* note 47 (comparing AA and A2/P2 rated 30-day and 60-day nonfinancial commercial paper rates).

⁵³ We note that second tier securities are also more likely to be downgraded than first tier securities. See Moody's Investors Service, *Short-Term Corporate and Structured Finance Rating Transition Rates*, *supra* note 44, cited in Chamber/Tier 2 Issuers Comment Letter (showing that for each time period, commercial paper with a P–2 rating had a greater percentage chance of being downgraded than commercial paper with a P–1 rating, and that this gap widened over time—for example, P–2 rated commercial paper had a 1.09% chance of being downgraded over a 60-day period compared to a 0.72% chance of P–1 commercial paper being downgraded (a 0.37% difference); P–2 rated commercial paper had a 2.07% chance of being downgraded over a 120-day period compared to a 1.46% chance of P–1 commercial paper being downgraded (a 0.61% difference); and P–2 rated commercial paper had a 4% chance of being downgraded over a 270-day period compared to a 3.18% chance of P–1 commercial paper being downgraded (a 0.82% difference)).

⁵⁴ See, e.g., Fidelity Comment Letter; Comment Letter of Thrivent Mutual Funds (Sept. 8, 2009) ("Thrivent Comment Letter").

us to preserve money market funds' ability to invest in second tier securities, but to a reduced degree.⁵⁵

In light of these considerations, we believe that it is not necessary to prohibit money market funds from acquiring second tier securities. Instead, we believe that a better approach is to further limit money market funds' exposure to the risks presented by second tier securities. We expect that this treatment will both satisfy our policy objectives, as further discussed below, while mitigating some of the possible negative consequences noted by commenters that could result from eliminating money market funds' ability to acquire second tier securities. This approach is reflected in three amendments we are adopting to rule 2a-7.

First, as suggested by some commenters,⁵⁶ we are reducing the amount of second tier securities that money market funds can acquire from five to three percent of their total assets, in order to reduce money market funds' aggregate exposure to the risks posed by second tier securities.⁵⁷ We are concerned that a limit of less than three percent could be equivalent to eliminating money market funds' ability to acquire second tier securities because we understand that investing in second tier securities requires an additional amount of credit analysis.⁵⁸

⁵⁵ See, e.g., Federated Comment Letter (suggesting, as an alternative to eliminating money market funds' ability to acquire second tier securities, further limitations including reducing the percentage of fund assets permitted to be invested in second tier securities and limiting the final maturity of permissible second tier securities). See also, e.g., Am. Elec. P. Comment Letter; Fidelity Comment Letter; USAA Comment Letter (each suggesting, as an alternative to eliminating money market funds' ability to acquire second tier securities, limiting the final maturity of permissible second tier securities to 90 days).

⁵⁶ See Federated Comment Letter; Comment Letter of the Sargent Shriver National Center on Poverty Law (Jul. 13, 2009) ("Shriver Poverty Law Ctr. Comment Letter"). These commenters did not suggest a particular percentage level to which the permissible aggregate amount of second tier securities that could be acquired should be reduced.

⁵⁷ The amendments apply the new limit on second tier securities holdings to all money market funds, including tax-exempt funds. See amended rule 2a-7(c)(3). Current rule 2a-7 limits tax-exempt funds' holdings of second tier securities only with respect to conduit securities (i.e., securities issued by a municipal issuer involving an arrangement or agreement entered into with a person other than the issuer that provides for or secures repayment of the security). See current rule 2a-7(c)(3)(ii)(B).

⁵⁸ In light of our decision not to prohibit the acquisition of second tier securities and after review of comments we received, we are persuaded that the current requirements regarding the rating standards in rule 2a-7 for certain long-term securities with remaining maturities of less than 397 days ("stub securities") are sufficient. We proposed to permit money market funds to acquire only those stub securities that had received a long-

term rating in the highest two categories rather than the highest three categories, as permitted under the current rule. See current rule 2a-7(a)(10)(ii)(A). Commenters largely opposed our proposal asserting that standards associated with long-term ratings referenced in the current rule generally are correlated with the standards associated with the highest categories of short-term ratings. See BlackRock Comment Letter; Charles Schwab Comment Letter; ICI Comment Letter.

Second, we are reducing the amount of second tier securities of any one issuer that a money market fund can acquire from one percent of the fund's total assets or \$1 million (whichever is greater), to one-half of one percent of the fund's total assets.⁵⁹ We requested comment in the Proposing Release on whether the issuer diversification limitations under rule 2a-7 should be further reduced and, if so, to what level.⁶⁰ Most commenters focused their response on whether there should be a general increase in the diversification limits under rule 2a-7 for all eligible securities. Many argued against an increase because it would require funds to invest in securities of lower credit quality in order to increase the number of issuers of portfolio securities and satisfy the greater diversification requirement.⁶¹ One commenter, however, recommended that funds not be able to acquire more than one-half of

term rating in the highest two categories rather than the highest three categories, as permitted under the current rule. See current rule 2a-7(a)(10)(ii)(A). Commenters largely opposed our proposal asserting that standards associated with long-term ratings referenced in the current rule generally are correlated with the standards associated with the highest categories of short-term ratings. See BlackRock Comment Letter; Charles Schwab Comment Letter; ICI Comment Letter.

⁵⁹ Amended rule 2a-7(c)(4)(i)(C). The limitation also applies to tax-exempt funds, which under the current rule are only subject to the issuer diversification requirement with respect to conduit securities that are second tier. We also are amending rule 2a-7(c)(4)(i)(B) to prohibit each "single State fund" from acquiring more than 1/2 of 1% of its total assets in second tier securities. We also discussed modification to the guarantor and demand feature diversification provisions under rule 2a-7 in Section II.D of the Proposing Release. In addition to the reduction in the ability of money market funds to acquire second tier securities of any particular issuer, we are proportionately reducing by half the ability of a money market fund to acquire "demand features" or "guarantees" of a single issuer that are second tier securities from 5% to 2.5% of the money market fund's total assets. See amended rule 2a-7(c)(4)(iii)(B). We believe that this reduction will provide appropriate protection to money market funds against exposure to any particular guarantor or demand feature provider. We do not believe that we need to reduce this limitation to 1/2 of 1%, as we are doing with other individual second tier issuer exposures, because in these cases a security holder has recourse to both the security issuer and the issuer of the demand feature or guarantee, and thus there is a lesser chance that an individual company's default or distress will adversely impact the security. We received no comments on this aspect of the Proposing Release.

⁶⁰ See Proposing Release, *supra* note 2, at Section II.D.

⁶¹ See, e.g., Charles Schwab Comment Letter; Invesco Aim Comment Letter.

one percent of their assets in *second tier securities* of any particular issuer as a method of limiting money market funds' exposure to the risks of second tier securities.⁶²

We are adopting this commenter's suggestion because we believe the limitation will enhance the resilience of money market funds. It should decrease the likelihood that the default of, or significant distress experienced by, any particular second tier issuer alone will cause a money market fund to break the buck. While a money market fund can break the buck due to simultaneous stresses across its portfolio, it also can break the buck due to a sudden decline in the market-based price of a particular security in its portfolio, as was the case with respect to securities of Lehman Brothers during September 2008.⁶³ In addition, unlike in the case of imposing a one-half of one percent diversification limitation on *all* issuers held in a money market fund's portfolio, given the other limitations on holdings of second tier securities that we are adopting today, a diversification limitation of one-half of one percent that applies only to second tier securities should not require money market funds to invest in a substantially greater number of issuers, and thus should not expose the fund to investing in securities of lower credit quality.⁶⁴ In sum, we believe this tightened limitation on exposure to any particular second tier security issuer will provide additional protection to the stability of money market funds.

Third, we are limiting money market funds to acquiring second tier securities with remaining maturities of 45 days or less.⁶⁵ Several commenters urged us to adopt this approach to limiting money market funds' exposure to risk from second tier securities.⁶⁶ The risks of

⁶² See Comment Letter of James J. Angel, Professor of Finance, Georgetown University (Sept. 8, 2009). Two other commenters also generally supported greater restrictions on money market funds' ability to acquire securities of any particular issuer. See Shriver Poverty Law Ctr. Comment Letter; Comment Letter of C. Stephen Wesselkamper (Sept. 3, 2009) ("C. Wesselkamper Comment Letter").

⁶³ See *supra* text accompanying note 11.

⁶⁴ Under the current rule, a taxable money market fund could invest the greater of 1% or \$1 million of its assets in second tier securities of a single issuer. Under the amendments we are adopting today, a money market fund maximizing its investment ability in second tier securities and trying to concentrate its holdings in as few issuers as possible would hold securities of six different second tier security issuers, rather than five second tier issuers under the current rule.

⁶⁵ Amended rule 2a-7(c)(3)(ii). We requested comment on this approach in the Proposing Release. See Proposing Release, *supra* note 2, at Section II.A.1.

⁶⁶ See, e.g., Am. Elec. P. Comment Letter; Fidelity Comment Letter; USAA Comment Letter (all

second tier securities discussed above can be substantially limited by restricting the length of time that a money market fund is exposed to the risks of that particular security. Securities 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. Moreover, second tier securities with shorter maturities are less likely to be downgraded.⁶⁷ In recognition of the role that a shorter maturity can play in reducing second tier securities' risk, the market typically has demanded that such securities be issued at shorter maturities than first tier securities.⁶⁸ We believe that limiting the risk arising out of second tier securities through limiting their permissible maturity is appropriate and that a 45-day maturity limit will provide additional protection to investors without causing undue market disruption.⁶⁹

suggesting that permissible second tier security maturities be limited to a 90-day maximum); Thrivent Comment Letter (suggesting that permissible second tier security maturities be limited to a 45-day maximum). Given the need for money market funds to adjust quickly to changes in market risk to avoid breaking the buck (and given that based on historical experience second tier securities are unlikely to be issued with a 90-day maturity limit), we believe that a 45-day maturity limit is more prudent than a 90-day maturity limit.

⁶⁷ See Moody's Investors Service, *Short-Term Corporate and Structured Finance Rating Transition Rates*, *supra* note 44 (showing that P-2 rated commercial paper had a 98.79% chance of being rated P-2 or higher over a 30-day period, but a 96.31% chance of being rated P-2 or higher over a 90-day period, and a 92.75% chance of maintaining this rating level over a 180-day period).

⁶⁸ For example, the average maturity of outstanding non-asset backed second tier commercial paper as of November 20, 2009 was 25.6 days compared to 52.2 days for non-asset backed first tier commercial paper. See Federal Reserve Board, *Average Maturity by Category for Outstanding Commercial Paper*, available at <http://www.federalreserve.gov/releases/cp/maturity.htm> (last visited Dec. 2009). The Federal Reserve Board also has reported that during each of 2007, 2008, and 2009, on average over 96% of non-financial A2/P2 commercial paper had a maturity of 40 days or less at issuance. See Federal Reserve Board, *Volume Statistics for Commercial Paper, A2/P2 Nonfinancial*, available at <http://www.federalreserve.gov/releases/cp/volumestats.htm> (last visited Dec. 2009).

⁶⁹ One commenter asserted that because so little of second tier commercial paper currently is issued with a maturity of greater than 45 days, imposing a maturity limitation of 45 days on second tier securities eligible for money market fund investment would have little effect on a fund's overall exposure to credit risk. See ICI Comment Letter. We disagree. It is true that in recent years, second tier commercial paper has been issued largely at maturities of less than 45 days. See *supra* note 68. This fact may mean that there will be less cost impact from our amendments limiting money market funds to acquiring second tier securities with maturities of 45 days or less. It does not mean,

We believe that the above combination of limitations on money market funds' ability to acquire second tier securities will achieve an appropriate balance between reducing the risk that money market funds will not be able to maintain a stable price per share and allowing fund investors to benefit from the higher returns that limited exposure to second tier securities can provide.

2. Eligible Securities

We are amending rule 2a-7 to require that the board of directors of each money market fund (i) designate four or more NRSROs, any one or more of whose short-term credit ratings the fund would look to under the rule in determining whether a security is an eligible security, and (ii) determine at least once each calendar year that the designated NRSROs issue credit ratings that are sufficiently reliable for that use.⁷⁰ In addition, funds must identify the designated NRSROs in the fund's statement of additional information ("SAI").⁷¹ Under the amendments, funds may, but are not required to, consider (or monitor) the ratings of other NRSROs under other provisions of the rule.⁷²

As we have stated on several occasions, we are concerned with the authority that references to NRSRO ratings in our rules have given certain rating agencies, and whether such references have inadvertently placed an "official seal of approval" on ratings that could adversely affect the quality of due diligence and investment analysis.⁷³

however, that this historical maturity distribution will hold true in the future, and that money market funds will not seek in the future to invest in longer term second tier securities to achieve a higher yield, which would expose money market funds to the higher risks associated with longer term second tier securities.

⁷⁰ Amended rule 2a-7(a)(11)(i). As under the definition of "NRSRO" in current rule 2a-7, a designated NRSRO may not be an affiliated person of the issuer of, or any insurer or provider of credit support for, the security. Amended rule 2a-7(a)(11)(ii). The definition of "designated NRSRO" incorporates the definition of NRSRO in section 3(a)(62) of the Securities Exchange Act of 1934 ("Exchange Act") [15 U.S.C. 78c(a)(62)]. Amended rule 2a-7(a)(11).

⁷¹ Amended rule 2a-7(a)(11)(iii) (requiring the fund to disclose in its SAI its designated NRSROs and any limitations with respect to the fund's use of such designation). See Part B of Form N-1A. In addition, funds must identify designated NRSROs in Form N-MFP with respect to each of the fund's portfolio securities. See *infra* Section II.E.2.

⁷² See *infra* notes 116-118, 121 and accompanying text.

⁷³ See, e.g., *References to Ratings of Nationally Recognized Statistical Rating Organizations*, Investment Company Act Release No. 28327 (July 1, 2008) [73 FR 40124 (July 11, 2008)] ("NRSRO References Proposing Release"); *References to Ratings of Nationally Recognized Statistical Rating Organizations*, Investment Company Act Release

The debt crisis of 2007-2008 also has given us concern about the reliability of these ratings.⁷⁴ Accordingly, we asked in the Proposing Release and in 2008 in a separate release whether we should eliminate or alter our use of ratings by NRSROs in rule 2a-7.⁷⁵

The Proposing Release requested comment on alternative approaches. One approach would have eliminated any references to ratings in rule 2a-7, the effect of which would be to eliminate the floor established by the "eligible security" requirement and rely entirely on fund boards (and their delegates) to determine whether investment in a security involved minimal credit risks. An alternative approach would have maintained references to credit ratings in the rule, but shifted responsibility to fund boards to determine at least annually which NRSROs were sufficiently reliable for the fund to use to determine whether a security is an eligible security that could be considered for investment. Among other things, we requested comment on the minimum number of credit rating agencies we should require that a board designate for this purpose.

Each time we have solicited comments, a substantial majority of commenters has strongly supported retaining the references to NRSRO ratings in the rule.⁷⁶ Among other reasons, commenters argued that using credit ratings as a floor for credit quality limits money market fund advisers from taking greater risks that could weaken the rule's risk limiting conditions and thus the protection of investors.⁷⁷ Many urged us instead to address the "root causes" of ratings failures rather than remove the safety net provided by the

No. 28939 (Oct. 5, 2009) [74 FR 52358 (Oct. 9, 2009)] ("NRSRO References Adopting Release").

⁷⁴ See NRSRO References Proposing Release, *supra* note 73, at text following n.6.

⁷⁵ See Proposing Release, *supra* note 2, at text following n.110; NRSRO References Proposing Release, *supra* note 73, at Section III.A.

⁷⁶ See, e.g., Comment Letter of Calvert Group, Ltd. (Sept. 8, 2009) ("Calvert Comment Letter"); Federated Comment Letter; ICI Comment Letter. See also Comment Letter of the American Bar Association (Committee on Federal Regulation of Securities and Committee on Securitization and Structured Finance) (Sept. 12, 2008) (available in File No. S7-19-08); Comment Letter of the Institutional Money Market Funds Association (Sept. 5, 2008) (available in File No. S7-19-08); Comment Letter of the Securities Industry and Financial Markets Association (Dec. 8, 2009) (available in File No. S7-19-08). Comment letters submitted in File No. S7-19-08 are available on the Commission's Web site at: <http://www.sec.gov/comments/s7-19-08/s71908.shtml>.

⁷⁷ See, e.g., Dreyfus Comment Letter; ICI Comment Letter; Comment Letter of J.P. Morgan Asset Management (Sept. 8, 2009) ("J.P. Morgan Asset Mgt. Comment Letter"). See also Proposing Release, *supra* note 2, at nn.108-110 and accompanying text.

credit ratings requirements of the rule.⁷⁸ Some disputed suggestions that inclusion of ratings in rule 2a–7 encourages fund managers to over-rely on the ratings, pointing to provisions in the rule that specifically require independent analysis by fund managers.⁷⁹ One commenter argued that NRSRO ratings provide “an additional, independent check on the investment manager’s judgment.”⁸⁰ By acting as a floor, the commenter argued, these ratings keep all money market funds operating at or above the same level,⁸¹ and they restrain any particular money market fund from taking (and exposing investors to) greater risks than other competing money market funds in order to gain a competitive advantage in a highly yield-sensitive market.⁸²

Only a few commenters have supported removing references to NRSRO ratings.⁸³ These commenters

principally asserted that removing credit ratings references would prevent fund boards and advisers from overreliance on NRSRO ratings and encourage advisers to make independent decisions about whether a security presents a credit risk.⁸⁴ Other commenters, however, countered that eliminating NRSRO ratings from the rule would do nothing to prevent a fund manager from being highly dependent upon NRSRO ratings in making its minimal credit risk determination.⁸⁵

Commenters did, however, largely support the approach of allowing funds to designate a minimum number of NRSROs that the fund would look to under rule 2a–7 in determining whether a security is an eligible security. They asserted that NRSRO designation would encourage competition among NRSROs to achieve designation and reduce the cost of subscribing to all NRSROs’ ratings.⁸⁶ They also noted that this approach would permit funds to focus better on standards, methods, and current ratings levels developed by designated NRSROs.⁸⁷ Several commenters expressed concern, however, that requiring designation of only three NRSROs would result in funds designating the three largest NRSROs, which could further entrench their market dominance.⁸⁸ Other commenters stated that designating NRSROs could disadvantage small NRSROs with well-developed capabilities regarding certain investments and suggested that the fund should have flexibility to rely on the particular NRSROs it determines have the best expertise to evaluate a particular security.⁸⁹ Some commenters, while supporting designation of

NRSROs, asserted that fund boards are unprepared to make such determinations and urged that fund advisers be given the responsibility.⁹⁰

The Commission is committed to reevaluating the use of NRSRO ratings in our rules. Recently we eliminated references to NRSRO ratings in several rules where we concluded that they were no longer warranted as serving their intended purposes and where the elimination was consistent with the protection of investors.⁹¹ Today, as discussed in more detail below, we are eliminating the only provision in rule 2a–7 that limits money market funds to investing in a type of security *only* if it is rated.⁹² We continue to work to further the goals of the Credit Rating Agency Reform Act in order to improve the quality and reliability of securities ratings.⁹³

We have found no evidence that suggests that over-reliance on NRSRO ratings contributed to the problems that money market funds faced during the debt crisis. Our staff closely examined, for example, why some money market funds held securities issued by certain SIVs that became distressed in 2007. The staff exams appear to indicate that the minimal creditworthiness evaluations of SIVs made by advisers to funds that held those SIVs differed from the evaluations made by advisers to funds that did not invest in those SIVs in the emphasis the advisers gave to particular elements of the analysis.⁹⁴ Had fund managers relied too heavily on credit rating agencies, we would have expected to see far more funds

⁷⁸ See, e.g., Comment Letter of the Northern Funds and Northern Institutional Funds—Independent Trustees (Sept. 8, 2009) (“Northern Funds Indep. Trustees Comment Letter”); Comment Letter of the Tamarack Funds Trust (Sept. 8, 2009) (“Tamarack Funds Comment Letter”). See also Comment Letter of Charles Schwab & Co., Inc. (Sept. 5, 2008) (available in File No. S7–19–08); Comment Letter of Dechert LLP (Sept. 5, 2008) (available in File No. S7–19–08); Comment Letter of Realpoint (Aug. 14, 2008) (available in File No. S7–19–08). We have recently adopted rule amendments designed to improve our regulation and oversight of NRSROs, which help address the integrity of their rating procedures and methodologies. See Amendments to Rules for Nationally Recognized Statistical Rating Organizations, Exchange Act Release No. 61050 (Nov. 23, 2009) [74 FR 63832 (Dec. 4, 2009)]; Amendments to Rules for Nationally Recognized Statistical Rating Organizations, Exchange Act Release No. 59342 (Feb. 2, 2009) [74 FR 6456 (Feb. 9, 2009)]; Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations, Exchange Act Release No. 55857 (June 5, 2007) [72 FR 33564 (June 18, 2007)].

⁷⁹ See ICI Comment Letter; TDAM Comment Letter.

⁸⁰ See ICI Comment Letter.

⁸¹ See, e.g., Comment Letter of State Street Global Advisors (Sept. 8, 2009) (“State Street Comment Letter”); Vanguard Comment Letter.

⁸² See ICI Comment Letter. See also J.P. Morgan Asset Mgt. Comment Letter; Comment Letter of Stradley Ronon Stevens & Young, LLP (Sept. 8, 2009) (“Stradley Ronon Comment Letter”).

⁸³ See Comment Letter of James B. Burnham, Business School Professor, Duquesne University (Aug. 27, 2009) (“J. Burnham Comment Letter”); Comment Letter of Moody’s Investors Service (Sept. 8, 2009) (“Moody’s Comment Letter”); Comment Letter of James L. Nesfield (Jul. 4, 2009) (“J. Nesfield Comment Letter”); Comment Letter of the Shadow Financial Regulatory Committee (Sept. 14, 2009) (“Shadow FRC Comment Letter”); Comment Letter of John M. Winters, CFA (Jul. 23, 2009). See also Comment Letter of Professor Lawrence J. White (Sept. 5, 2008) (available in File No. S7–19–08); Comment Letter of Professor Frank Partnoy (Sept. 5, 2008) (available in File No. S7–19–08); Comment Letter of the Government Finance Officers Association (Sept. 5, 2008) (available in File No. S7–19–08); Comment Letter of the Financial Economists Roundtable (Dec. 1, 2008) (available in File No. S7–19–08).

⁸⁴ See J. Burnham Comment Letter; Moody’s Comment Letter; J. Nesfield Comment Letter; Shadow FRC Comment Letter. One commenter asserted that transparency of portfolio holdings was a better approach than using references to NRSRO ratings. J. Nesfield Comment Letter. We note that we are amending rule 2a–7 to require money market funds to disclose information about their portfolio holdings each month on their Web sites. See *infra* Section II.E.1.

⁸⁵ Stradley Ronon Comment Letter (removing the references would not prevent advisers from relying too heavily on NRSRO ratings under their own internal credit risk analysis).

⁸⁶ See, e.g., Federated Comment Letter; Fidelity Comment Letter; ICI Comment Letter.

⁸⁷ See Am. Secur. Forum Comment Letter.

⁸⁸ See, e.g., Comment Letter of DBRS Limited (Sept. 8, 2009) (“DBRS Comment Letter”); Comment Letter of Wells Fargo Funds Management, LLC (Sept. 8, 2009) (“Wells Fargo Comment Letter”). Three of the 10 NRSROs registered with the Commission issued approximately 97% of all outstanding ratings across all categories reported to the Commission for 2008. See SEC, Annual Report on Nationally Recognized Statistical Rating Organizations (Sept. 2008) at 10.

⁸⁹ See Tamarack Funds Comment Letter; TDAM Comment Letter.

⁹⁰ See Comment Letter of the American Bar Association (Committee on Federal Regulation of Securities) (Sept. 9, 2009) (“ABA Comment Letter”); Comment Letter of the Mutual Fund Directors Forum (Sept. 8, 2009) (“MFDF Comment Letter”); Comment Letter of Northern Funds and Northern Institutional Funds (Sept. 8, 2009) (“Northern Funds Comment Letter”).

⁹¹ See NRSRO References Adopting Release, *supra* note 73.

⁹² Compare amended rule 2a–7(a)(12) with current rule 2a–7(a)(10)(i)(B).

⁹³ See, e.g., Proposed Rules for Nationally Recognized Statistical Rating Organizations, Exchange Act Release No. 61051 (Nov. 23, 2009) [74 FR 63866 (Dec. 4, 2009)] (proposing rule amendments and a new rule requiring each NRSRO to: (1) Furnish an annual report describing the steps taken by the firm’s designated compliance officer during the fiscal year with respect to certain compliance matters; (2) disclose additional information about sources of revenues on Form NRSRO; and (3) make publicly available information about revenues of the NRSRO attributable to persons paying the NRSRO for the issuance or maintenance of a credit rating).

⁹⁴ See Proposing Release, *supra* note 2, at note 135.

holding Lehman Brothers commercial paper when it defaulted than we did.⁹⁵

The current provisions of rule 2a-7 were designed to prevent excess reliance on credit rating agencies.⁹⁶ Under rule 2a-7, adequate ratings alone do not provide a basis for eligibility. As we have noted before, a determination that a security is an eligible security is a necessary but not sufficient finding in order for a fund to acquire the security.⁹⁷ The rule also requires fund boards (which typically rely on the fund's adviser) to determine that the security presents minimal credit risks, and specifically requires that determination "be based on factors pertaining to credit quality in addition to any ratings assigned to such securities by an NRSRO."⁹⁸ Thus, credit ratings provide an important *but not exclusive* input into the investment decision-making process,⁹⁹ and the unreliability or low quality of ratings issued by one or more NRSROs can (and should) be addressed by an investment adviser providing a thorough analysis of the security to determine if it involves minimal credit risks. The use of these ratings provides an independent perspective on the creditworthiness of short-term securities that we have considered, in part, when determining whether to exercise our exemptive authority to permit money market funds to use the amortized cost method of valuation.¹⁰⁰

This is not to say, however, that we are content with the current approach of

⁹⁵ See *Fitch: Market Challenges Offer 'Lessons' for Rated Money Market Funds*, Business Wire (Oct. 1, 2008) ("Most funds were able to eliminate or minimize their exposure to securities issued by SIVs and Lehman Brothers by limiting their absolute exposures and/or taking measures to scale back their risk as the credit picture deteriorated."). See Bloomberg Terminal Database, LEH (Equity) CRPR (historical short-term credit ratings for credit rating agencies, including Moody's and Fitch, indicate that these agencies did not downgrade their ratings of Lehman Brothers debt before the company filed for bankruptcy); Bob Ivry, Mark Pittman & Christine Harper, *Sleep-At-Night-Money Lost in Lehman Lesson Missing \$63 Billion*, Bloomberg (Sept. 8, 2009), available at http://www.bloomberg.com/apps/news?pid=email_en&sid=aLhi.S5xkemY (historical short-term credit ratings for Moody's and Fitch indicate that these credit rating agencies did not downgrade their ratings of Lehman Brothers debt before the company filed for bankruptcy); David Segal, *The Silence of the Oracle*, New York Times (Mar. 18, 2009) (noting Moody's rated Lehman Brothers' debt A2 before the firm's bankruptcy).

⁹⁶ See Revisions to Rules Regulating Money Market Funds, Investment Company Act Release No. 18005 (Feb. 20, 1991) [56 FR 8113 (Feb. 27, 1991)] ("1991 Adopting Release") at Section II.A.

⁹⁷ See, e.g., *id.* at text accompanying n.18.

⁹⁸ Current rule 2a-7(c)(3)(i).

⁹⁹ See 1991 Adopting Release, *supra* note 96, at Section II.A.

¹⁰⁰ See 1983 Adopting Release, *supra* note 6, at paragraphs following n.31.

rule 2a-7. Any one of the growing number of NRSROs, regardless of its expertise in rating short-term securities of the type held by money market funds, could have deemed a security unfit for a money market fund to acquire or, conversely, deemed a security to be eligible for investment by a money market fund. To address this concern, we are adopting amendments to rule 2a-7 that shift responsibility to money market fund boards for deciding which NRSROs they will use in determining whether a security is an eligible security for purposes of the rule.

The amendments are designed, among other things, to foster greater competition among NRSROs to produce the most reliable ratings in order to obtain designation by money market fund boards. Accordingly, we believe this approach will improve the utility of the rule's use of NRSRO ratings as threshold investment criteria, and is consistent with the goals of Congress in passing the Credit Rating Agency Reform Act.¹⁰¹

a. Number of Designated NRSROs

Under amended rule 2a-7, each money market fund must designate in its registration statement¹⁰² at least four

¹⁰¹ See Senate Committee on Banking, Housing, and Urban Affairs, Credit Rating Agency Reform Act of 2006, S. Rep. 109-326, at 1 (2006) ("Senate Report No. 109-326") ("The purpose of the 'Credit Rating Agency Reform Act' * * * is to improve ratings quality for the protection of investors and in the public interest by fostering accountability, transparency, and competition in the credit rating industry."). In 2007, pursuant to the Credit Rating Agency Reform Act, we adopted rules to implement a program for registration and Commission oversight of NRSROs ("NRSRO Rules"). Oversight of Credit Rating Agencies Registered as Nationally Recognized Statistical Rating Organizations, Exchange Act Release No. 55857 (June 5, 2007) [72 FR 33564 (June 18, 2007)] ("NRSRO Rules Adopting Release"). Our rule amendments regarding NRSROs have been designed, among other things, to foster greater competition among NRSROs and to encourage more of them to enter the market. See, e.g., Amendments to Rules for Nationally Recognized Statistical Rating Organizations, Exchange Act Release No. 61050 (Nov. 23, 2009) [74 FR 63832 (Dec. 4, 2009)], at nn.1-3 and accompanying text (*citing* Senate Report No. 109-326, at 1).

¹⁰² The fund must disclose the designated NRSROs, including any limitations with respect to the fund's use of such designation, in the fund's SAI. Amended rule 2a-7(a)(11)(iii). In response to our request for comment on whether to require disclosure of designated NRSROs in money market funds' SAI, see Proposing Release, *supra* note 2, at text accompanying n.115, several commenters suggested we require disclosure of designated NRSROs in the fund's registration statement. See, e.g., Fidelity Comment Letter (recommending disclosure in the fund's SAD); Invesco Aim Comment Letter (same); ICI Comment Letter (recommending disclosure in the fund's prospectus or Web site). In contrast, one commenter objected to disclosure of designated NRSROs in the fund's registration statement on the grounds that investors do not consider this information to be material and

NRSROs that the fund will use to determine, among other things, whether a security is an eligible security.¹⁰³ Several commenters expressed concern that permitting funds to designate only three NRSROs (which was recommended by the ICI Report) would simply embrace the current market for ratings, which is dominated by three rating agencies.¹⁰⁴ We share these commenters' concerns and thus are requiring funds to designate at least four NRSROs, an approach recommended by commenters as a way to foster competition among NRSROs to develop a specialized service of providing short-term ratings to money market funds and improve independent credit ratings for purposes of the rule.¹⁰⁵ We also believe that the designation of at least four NRSROs will allow funds to designate smaller NRSROs that specialize in rating particular investments.

Under the amendments, a fund could designate an NRSRO with respect to short-term credit ratings for only certain types of issuers or securities.¹⁰⁶ This

stickering the fund's prospectus for each change in designation would be too costly. See Federated Comment Letter. We believe that the identity of each designated NRSRO is not essential information for investors, but that some investors may find it useful, and therefore are requiring it in the SAI. See generally Form N-1A at General Instruction C.2(b) (noting that the purpose of the SAI is to provide additional information about a fund that is not necessary to be in the prospectus but that some investors may find useful).

¹⁰³ Amended rule 2a-7(a)(11). A fund may designate only credit rating agencies that are registered as NRSROs with the Commission under the Exchange Act and the rules adopted under those provisions. See section 15E of the Exchange Act [15 U.S.C. 78o-7]; 17 CFR 240.17g-1. In response to our request for comment, one commenter recommended permitting designation of unregistered credit rating agencies on the grounds that this could promote competition. See Moody's Comment Letter. Two commenters opposed designation of an unregistered credit rating agency, and one of these commenters argued that the potential for introducing under-researched data into the marketplace could disrupt the orderly functioning of markets. See DBRS Comment Letter; Invesco Aim Comment Letter. In light of the enhanced disclosure obligations and ongoing rulemaking initiatives designed to improve the quality and reliability of ratings issued by registered NRSROs, we are maintaining the requirement that only credit rating agencies registered as NRSROs with the Commission may be designated under the rule. See, e.g., *supra* note 93.

¹⁰⁴ See, e.g., DBRS Comment Letter; Wells Fargo Comment Letter; C. Wesselkamper Comment Letter.

¹⁰⁵ See DBRS Comment Letter; Fidelity Comment Letter. In response to our request for comment on the appropriate number of NRSROs a board should designate, another commenter requested we require funds to designate at least five NRSROs as a way to encourage new entrants to the market. See Federated Comment Letter. See also Proposing Release, *supra* note 2, at text following n.113 and at n.117 and accompanying text (requesting comment).

¹⁰⁶ Amended rule 2a-7(a)(11)(i)(A) (providing that a money market fund's board of directors may designate an NRSRO whose short-term credit ratings with respect to any obligor or security or

would allow a fund, for example, to designate an NRSRO that specializes in securities issued by insurance companies or banks.¹⁰⁷ This approach, which was supported by several of the commenters,¹⁰⁸ may further encourage new entrants among NRSROs that fund managers might not otherwise consider designating due to lack of confidence in ratings outside the NRSROs' areas of expertise.

b. Board Designation and Annual Determination

The amendments require each money market fund's board of directors to designate the NRSROs on which the fund will rely for purposes of the rule. In addition, the board must determine at least once each calendar year that each designated NRSRO issues credit ratings that are sufficiently reliable for such use.¹⁰⁹ Before designating an NRSRO and before making its annual determination, a board should have the benefit of the adviser's evaluation regarding the quality of the NRSRO's short-term ratings.¹¹⁰ We would anticipate that the board's designations and annual determinations would be based on recommendations of the fund adviser and its credit analysts, who would have evaluated each NRSRO based on their experiences in addition to any information provided by the NRSRO. We would expect the adviser's annual evaluation to be based, among other things, on an examination of the methodology an NRSRO uses to rate securities, including the risks they measure, and the NRSRO's record with respect to the types of securities in which the fund invests, including asset backed securities.¹¹¹ The reliability of a

particular obligors or securities will be used by the fund to determine whether a security is an eligible security).

¹⁰⁷ A fund that has designated an NRSRO to use in determining the eligibility of insurance company-issued securities need not review or monitor any class of ratings that the NRSRO issued with respect to other securities or their issuers in which the fund may invest. A fund adviser (under delegated authority) would be free (but not required) to consider these ratings in determining whether the non-insurance company-issued security (or its issuer) presents minimal credit risks. Amended rule 2a-7(c)(3)(i).

¹⁰⁸ See DBRS Comment Letter; Moody's Comment Letter; Wells Fargo Comment Letter.

¹⁰⁹ Amended rule 2a-7(a)(11)(i). We are requiring funds to perform the annual determination once each calendar year to simplify compliance so that a fund is not in violation of the rule if the board's determination occurs soon after the year anniversary of the previous determination.

¹¹⁰ Fund boards may, however, also find an NRSRO's record with respect to long-term securities to be helpful in evaluating the overall quality of the organization.

¹¹¹ See Moody's Comment Letter (advocating that any board designation be "based on the board's assessment of ratings' attributes, such as quality,

newly registered NRSRO could be evaluated based upon the quality and relevant experience of the personnel conducting the rating. Even with the recommendations of the fund adviser, we recognize that ultimately, a board's determination whether an NRSRO's ratings are "sufficiently reliable" for use in determining whether a security is an eligible security will be a matter of judgment.

Many commenters expressed concern that a money market fund's board of directors does not have the necessary expertise to designate NRSROs, and urged that we delegate the authority to fund advisers to make the designation.¹¹² A number of these commenters seem to assume that we would require fund boards to engage in the type of analysis that we expect the adviser will provide the board for its consideration. We believe that it will be useful for boards to consider the designation of NRSROs, a role not unlike the role that many boards play in approving other matters of substantial significance to the operation of the fund.¹¹³ Board designation and determination (at least once a calendar year) will serve as a check on fund

comparability and historical performance." We have recently adopted rule amendments relating to NRSROs that should help fund advisers and their credit analysts in performing their evaluations. Our amendments require NRSROs, among other things, to disclose information about their ratings methodology, experience and performance. For example, NRSROs must disclose in their applications their ratings experience, performance in assessing the creditworthiness of securities and obligors, procedures and methodologies used in determining credit ratings, the types of conflicts NRSROs face and how they manage those conflicts, and the qualifications of the NRSRO's credit analysts. See Items 6, 7 and Exhibits 1, 2, 6, 7, 8 of Form NRSRO. In addition, NRSROs currently are required to disclose on a public Web site a random sample of 10% of the ratings histories of issuer paid ratings in each class of credit ratings for which the NRSRO is registered and has issued 500 or more issuer paid credit ratings. Rule 17g-2(a)(8) and (d) [17 CFR 240.17g-2(a)(8) and (d)]. In June of this year, these public disclosures will have to include ratings action histories for all credit ratings initially determined on or after June 26, 2007. See Amendments to Rules for Nationally Recognized Statistical Ratings Organizations, Exchange Act Release No. 61050 (Nov. 23, 2009) [74 FR 63832 (Dec. 4, 2009)] at text following n.19 and compliance date.

¹¹² See, e.g., ABA Comment Letter; MFDF Comment Letter; Northern Funds Comment Letter. These commenters responded to our discussion of this approach in the Proposing Release. See Proposing Release, *supra* note 2, at text following n. 118.

¹¹³ See, e.g., amended rule 2a-7(c)(8) (requiring the fund's board of directors to establish procedures to stabilize the fund's NAV, including procedures providing for, among other things, the board's periodic review of the fund's shadow price, the methods used for calculating shadow price, and what action, if any, the board should initiate if the fund's shadow price exceeds amortized cost by more than 1/2 of 1%).

managers that may have conflicts of interest in selecting an NRSRO from which the manager seeks a rating for the fund (in order to facilitate marketing the fund),¹¹⁴ or an NRSRO that may accommodate the fund's investment in higher yielding, riskier securities.¹¹⁵

c. Operation of the Rule

Once a board has designated the NRSROs, the fund could look to the designated NRSROs whenever it has to consider credit ratings under rule 2a-7 unless and until the board changes the designation.¹¹⁶ A fund must look to only the designated NRSROs to determine whether the security is an eligible security, a rated security,¹¹⁷ and whether it is a first tier or a second tier

¹¹⁴ See Wells Fargo Comment Letter.

¹¹⁵ See Moody's Comment Letter (noting that the more narrowly defined the categories of ratings for which a designation can be obtained, the "easier it could be for mutual funds to game the system, e.g., by dropping an NRSRO from its list of designated NRSROs for a particular class of ratings because the NRSRO has introduced a more conservative ratings methodology.").

¹¹⁶ We have changed the term from "NRSRO" to "designated NRSRO" throughout the rule each time it is used. As a consequence, changes in the fund's designated NRSROs may affect the ability of the fund to purchase a new security or roll over a current holding, and may require the fund to reassess promptly whether the security continues to present minimal creditworthiness and dispose of a current holding. This is because a new designation of an NRSRO (or a removal of a designated NRSRO) is now treated under the rule as the equivalent of a credit event requiring the fund board or adviser to consider the rating of the newly designated NRSRO (or preclude the consideration of a formerly designated NRSRO). For example, if a fund acquires an unrated security (i.e., a security (or its issuer) that does not have a short-term rating from a designated NRSRO) that the fund considered to be equivalent to a first tier security and the fund thereafter designates a new NRSRO that has rated the security as a second tier security, the fund must then treat the security as a second tier security. The fund would not be required to dispose of the security (although it would be required to perform a credit assessment, which might prompt it to dispose of the security) even if the position in the security exceeds the fund's limits on second tier securities, because compliance with the limits on second tier securities is determined immediately after the fund acquires the security. See amended rule 2a-7(c)(3)(ii); 2a-7(c)(4)(i)(C). The fund could only roll over the position to the extent that immediately after the rollover the fund would meet the rule's limits on second tier securities. See amended rule 2a-7(a)(1) (defining "acquisition" to include a rollover of a position in security).

¹¹⁷ Amended rule 2a-7(a)(23) (defining the term "requisite NRSROs"). For purposes of determining whether a rated security is an eligible security and a first tier security, rule 2a-7 requires the fund to determine whether the security (or its issuer) has received a short-term rating from the requisite NRSROs. Amended rule 2a-7(a)(12)(i). Under the amended rule, the requisite NRSROs must be drawn from the designated NRSROs. Amended rule 2a-7(a)(23). Thus, for example, a security that is rated as a first tier security by two NRSROs, only one of which is a designated NRSRO, and as a second tier security by another designated NRSRO, is a split-rated security and thus a second tier security. *Id.*

security.¹¹⁸ Under the amendments, a security is an unrated security if neither the security nor its issuer has received a short-term rating from any of the designated NRSROs.¹¹⁹ Accordingly, before investing in the security, the fund adviser must make a determination that the security is of comparable quality to a rated security.¹²⁰ After a money market fund acquires a security, the fund manager must monitor only the ratings of designated NRSROs to determine whether a change in those ratings requires the board to reassess promptly whether the security continues to present minimal credit risks or to dispose of a portfolio security that is no longer an eligible security.¹²¹

3. Asset Backed Securities

We are amending rule 2a-7 to eliminate a requirement that an asset backed security (“ABS”) be rated by at least one NRSRO in order to be an eligible security that a money market fund may acquire.¹²² As a consequence, funds may acquire an unrated asset backed security that otherwise meets the requirements of rule 2a-7, including those requirements that apply to unrated securities.¹²³

In 1996, we limited funds to investing in rated ABSs because we thought that NRSROs played a beneficial role in

assuring that assets underlying an ABS were properly valued and would support the cash flows required to fund the ABS, and we were concerned that fund advisers may not be in as good a position to perform the legal, structural, and credit analysis that the rating agencies performed.¹²⁴ As discussed in the Proposing Release, NRSROs rapidly downgraded ABSs from their status as first tier securities over a short time period during 2007–2008.¹²⁵ The NRSROs thus did not seem to play a role in buttressing the minimal credit risk analysis of fund management sufficient to warrant a requirement that all ABSs be rated to be eligible for money market fund investment. We would otherwise have expected a slower, more orderly downgrading process for these ABSs, which would have permitted money market funds to gradually roll off the paper.

We received only a few comments on this approach.¹²⁶ One NRSRO commenter supported removing this requirement.¹²⁷ Two urged us to keep the ratings requirement for ABSs,¹²⁸ and one of those asserted that ratings “under appropriate criteria” enhance the liquidity of ABSs and provide credit and structural expertise and research that benefit investors.¹²⁹ As noted above, we do not believe that NRSRO ratings of ABSs served this function during the 2007–2008 turmoil in the ABS marketplace, and we no longer believe that the provision of rule 2a-7 that has required such ratings for all ABSs is warranted as serving its intended purpose, and thus we are eliminating this requirement.¹³⁰

¹²⁴ Revisions to Rules Regulating Money Market Funds, Investment Company Act Release No. 21837 (Mar. 21, 1996) [61 FR 13956 (Mar. 28, 1996)] at Section II.E.4; Revisions to Rules Regulating Money Market Funds, Investment Company Act Release No. 19959 (Dec. 17, 1993) [58 FR 68585 (Dec. 28, 1993)] (“1993 Proposing Release”) at nn.110–112 and accompanying text.

¹²⁵ See Proposing Release, *supra* note 2, at Section II.A.4. See also Standard & Poor’s, *Global Structured Finance Default and Transition Study—1978–2008: Credit Quality of Global Structured Securities Fell Sharply in 2008 Amid Capital Market Turmoil* (Feb. 25, 2009), available at <http://www2.standardandpoors.com/portal/site/sp/en/ca/page/article/3,3,3,0,1204847668460.html> (showing greater default rate and significantly greater downgrades in structured finance securities).

¹²⁶ We also solicited comment generally on whether, and if so how, we should amend rule 2a-7 to generally address the risks presented by ABSs. We received a number of comments in response to this request, and will consider them in developing further amendments to rule 2a-7.

¹²⁷ See Moody’s Comment Letter.

¹²⁸ See Am. Securit. Forum Comment Letter; Shriver Poverty Law Ctr. Comment Letter.

¹²⁹ See Am. Securit. Forum Comment Letter.

¹³⁰ See Statement of Lawrence J. White, SEC Roundtable to Examine Oversight of Credit Rating Agencies at 2 (Apr. 15, 2009) (initial ratings on

We do note, however, that as part of the minimal credit risk analysis that any money market fund must conduct before investing in an ABS, the board of directors (or its delegate) should: (i) Analyze the underlying ABS assets to ensure that they are properly valued and provide adequate asset coverage for the cash flows required to fund the ABS under various market conditions; (ii) analyze the terms of any liquidity or other support provided by the sponsor of the ABS; and (iii) otherwise perform the legal, structural, and credit analyses required to determine that the particular ABS involves appropriate risks for the money market fund.¹³¹

B. Portfolio Maturity

We are adopting amendments to rule 2a-7 to further restrict the maturity limitations on a money market fund’s portfolio in order to reduce the exposure of money market fund investors to certain risks, including interest rate risk, spread risk, and liquidity risk. First, we are reducing the maximum weighted average portfolio maturity permitted by the rule from 90 days to 60 days. Second, we are adopting a 120-day limit on the weighted average life of a money market fund’s portfolio, which will limit the portion of a fund’s portfolio that could be held in longer term adjustable-rate securities. Finally, we are deleting a provision in the rule that permitted certain money market funds to acquire Government securities with extended maturities of up to 762 calendar days.

1. Weighted Average Maturity

We are amending rule 2a-7 to require that each money market fund maintain a dollar-weighted average portfolio maturity (WAM) appropriate to its objective of maintaining a stable net asset value or price per share, but in no case greater than 60 days.¹³² We believe that such a limit on the maximum WAM will result in money market funds that are more resilient to changes in interest rates that may be accompanied by other market shocks, and thus reduce the likelihood of a run and better protect money market fund investors. As we explained in the Proposing Release, a portfolio weighted towards securities with longer maturities increases the fund’s exposure to interest rate risk, amplifies spread risk, and decreases the

bonds securitized from subprime residential mortgages “proved to be excessively optimistic”—especially for the bonds based on mortgages originated in 2005 and 2006).

¹³¹ See 1993 Proposing Release, *supra* note 124, at nn.108–111 and preceding and accompanying text.

¹³² See amended rule 2a-7(c)(2).

¹¹⁸ Amended rule 2a-7(a)(12) (defining “eligible security”); amended rule 2a-7(a)(14) (defining “first tier security”); and amended rule 2a-7(a)(24) (defining “second tier security”).

¹¹⁹ Amended rule 2a-7(a)(30) (defining “unrated security” by reference to amended rule 2a-7(a)(21), which defines a “rated security” as, among other things, a security that has received or been issued by an issuer that has received a short-term rating by a designated NRSRO).

¹²⁰ Amended rule 2a-7(a)(12) (defining “eligible security”).

¹²¹ Amended rule 2a-7(c)(7)(i)(A) (requiring a fund’s board of directors to reassess promptly whether the security continues to present minimal credit risks and cause the fund to take action if: (i) The security ceases to be a first tier security because it no longer has the highest rating from the requisite NRSROs or, in the case of an unrated security, the board determines it is no longer of comparable quality to a first tier security, or (ii) the security is an unrated security or second tier security and the fund’s investment adviser (or portfolio manager) becomes aware since acquisition of the security that any designated NRSRO has given it a rating below the designated NRSRO’s second highest short-term rating); amended rule 2a-7(c)(7)(ii)(B) (requiring a fund to dispose of a security that ceases to be an eligible security as soon as practicable consistent with achieving an orderly disposition of the security, 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).

¹²² We are thus amending current rule 2a-7(a)(10)(ii) to eliminate paragraph (B) and renumber paragraph 2a-7(a)(10)(ii)(A) as 2a-7(a)(12)(ii).

¹²³ See, e.g., amended rule 2a-7(a)(12)(ii); (c)(3)(iv)(C); (c)(7)(i)(A)(1). As under the current rule, if an asset backed security is a rated security, it will be required to satisfy the rule’s ratings criteria. Amended rule 2a-7(a)(12)(i).

ability of a fund to pay redeeming shareholders.¹³³

Most commenters that addressed this proposal supported further reducing the maximum WAM of fund portfolios in order to reduce the funds' exposure to related risk. Those commenters were divided between those supporting the 60-day maximum WAM that we proposed¹³⁴ and those supporting a reduction to 75 days.¹³⁵ Other commenters argued for no reduction at all (*i.e.*, leaving the limit at 90 days).¹³⁶ Commenters supporting a maximum WAM limitation of 60 days believed that such a reduction would be appropriate to increase the stability and liquidity of money market funds¹³⁷ and would reduce funds' exposure to interest rate risk.¹³⁸ One asserted that a 60-day limitation is appropriate as it prioritizes a money market fund's safety and liquidity over yield.¹³⁹

Commenters supporting a maximum WAM of 75 days argued that such a limitation would achieve the Commission's goal of reducing funds' exposure to interest rate risk while providing funds with sufficient flexibility to invest in high quality securities when shorter term investments are scarce.¹⁴⁰ Some expressed concern about whether a 60-day WAM would reduce a money market fund's ability to generate sufficient yield.¹⁴¹ Still others argued that a shorter WAM could make some money market funds more risky because of the alternative investment strategies they might employ as a result.¹⁴²

¹³³ See Proposing Release, *supra* note 2, at Section II.B.1.

¹³⁴ See, *e.g.*, Goldman Sachs Comment Letter; Comment Letter of the Institutional Money Market Funds Association (Sept. 8, 2009) ("IMMFA Comment Letter"); Northern Funds Indep. Trustees Comment Letter.

¹³⁵ See, *e.g.*, Charles Schwab Comment Letter; Comment Letter of GE Asset Management Incorporated (Sept. 8, 2009) ("GE Asset Mgt. Comment Letter"); T. Rowe Price Comment Letter.

¹³⁶ See, *e.g.*, State Street Comment Letter; Comment Letter of Victory Capital Management (Sept. 8, 2009) ("Victory Cap. Mgt. Comment Letter"); Wells Fargo Comment Letter.

¹³⁷ See Tamarack Funds Comment Letter.

¹³⁸ See TDAM Comment Letter.

¹³⁹ See Invesco Aim Comment Letter.

¹⁴⁰ See, *e.g.*, Charles Schwab Comment Letter; GE Asset Mgt. Comment Letter; ICI Comment Letter.

¹⁴¹ See, *e.g.*, Charles Schwab Comment Letter; Comment Letter of Crane Data LLC and Money Fund Intelligence (Aug. 31, 2009) ("Crane Data Comment Letter"); T. Rowe Price Comment Letter.

¹⁴² One commenter noted that a WAM limitation longer than 60 days would allow a fund to improve the credit profile of its portfolio by substituting longer term Government securities for shorter term corporate securities. See BlackRock Comment Letter. Another commenter argued that a reduction would lead to fund portfolios with a "barbelled" maturity structure in which the fund balanced the low yield offered by the large amount of very short-

term securities it would be required to hold with an offsetting amount of riskier longer term securities, which could increase the riskiness of fund portfolios. See Comment Letter of Waddell & Reed/Ivy Fund Portfolio Managers (Sept. 8, 2009) ("Waddell & Reed Comment Letter"). Another stated that higher risk issuers tend to be limited to issuing shorter maturity securities, so a shorter WAM limitation could increase a fund's credit risk profile. See Wells Fargo Comment Letter.

Finally, two commenters opposing any change in the maximum WAM permitted by rule 2a-7 argued that liquidity risk to funds is more appropriately limited by other aspects of our amendments to rule 2a-7, and that the resulting reduction in yield would "homogenize" money market funds to such an extent that investors may be driven to invest in unregulated funds, thus increasing systemic risk.¹⁴³ We believe that the maximum WAM permissible for money market funds should be reduced to 60 days in order to reduce the likelihood of funds breaking the buck. The increased resilience to simultaneous stresses from interest rate and other risks that a money market fund would achieve through a maximum WAM of 60 days is significant. A fund with a 90-day WAM could withstand an instantaneous change in interest rates of 200 basis points before breaking the buck.¹⁴⁴ In contrast, a fund with a WAM of 60 days could withstand an interest rate change of 300 basis points without breaking the buck.¹⁴⁵ Although an interest rate change of such a magnitude may be unlikely to occur,¹⁴⁶ funds must also be

able to withstand multiple shocks occurring simultaneously, such as those that occurred in September 2008 when there was a simultaneous increase in LIBOR rates and widening spreads due to credit deterioration and liquidity pressures, together with extraordinary redemptions.¹⁴⁷

A fund with a lower WAM has significantly greater protection in the circumstances described above. For example, a fund with a 90-day WAM facing a change in credit spreads of 50 basis points and redemptions of 10 percent would break the buck with an interest rate change of a little more than 100 basis points.¹⁴⁸ Greater shocks from an even larger increase in spreads or redemptions would only lessen that interest rate cushion—last fall increases in spreads and redemptions were considerably above this level.¹⁴⁹ A fund with a 60-day WAM would be in a better position to withstand multiple shocks without breaking the buck than if it maintained a 90-day or 75-day WAM.¹⁵⁰

We disagree with those commenters that asserted that a reduction of maximum permissible WAM would have a significant adverse effect on money market funds' investment strategies or yield. We have not observed such adverse effect in funds with WAMs below 60 days or a greater tendency to invest in riskier short-term

the economy recovers or to strengthen the U.S. dollar.

¹⁴⁷ See Proposing Release, *supra* note 2, at nn.47-48, 53, 63, 66-67 and accompanying text. See also *infra* note 178 (discussing the increase in LIBOR during the financial crisis). Many money market fund portfolio holdings at the time were tied to LIBOR.

¹⁴⁸ This assumes a weighted average life limitation of 120 days. A fund with a 75-day WAM could withstand a 50 basis point increase in credit spreads across its portfolio, 10% redemptions, and an increase in interest rates of 125 basis points before breaking the buck, assuming a 120-day weighted average life.

¹⁴⁹ In addition, we note that spreads have widened to significant degrees in the past. See, *e.g.*, Benjamin N. Friedman & Kenneth N. Kuttner, *Why Does the Paper-Bill Spread Predict Real Economic Activity?*, NBER Working Paper No. 3879, at Fig. 1 (Oct. 1991) (showing historical spreads for 6-month commercial paper over 6-month Treasury bill rates from 1959 to 1990).

¹⁵⁰ Based on staff review of various stress test scenarios, a fund with a 60-day WAM could withstand a 50 basis point increase in credit spreads across its portfolio, 10% redemptions, and an increase in interest rates of over 150 basis points before breaking the buck, again assuming a weighted average life limitation of 120 days. Others have recognized that exposure to multiple stresses may call for a lower WAM. See, *e.g.*, Standard & Poor's, *Fund Ratings Criteria: Market Price Exposure*, at 3 (2007), available at <http://www2.standardandpoors.com/spf/pdf/events/MMX709.pdf> (stating that money market funds with a greater liquidity risk due to a smaller asset size or shareholder composition may need to maintain a lower WAM than 60 days).

¹⁴³ See Fidelity Comment Letter; State Street Comment Letter. Several commenters also asserted that any reduction in WAM would increase issuers' reliance on short-term funding, also increasing systemic risk. See, *e.g.*, Am. Securit. Forum Comment Letter; State Street Comment Letter; Wells Fargo Comment Letter.

¹⁴⁴ See Fidelity Comment Letter.

¹⁴⁵ Our staff supplemented stress test analysis conducted by commenters with more data points and stress scenarios to illustrate the impact on a money market fund's net asset value per share from multiple stresses on that fund's portfolio. A fund with a 75-day WAM could withstand an interest rate change of less than 250 basis points without breaking the buck. We note that these scenarios also represent the most conservative scenarios because they assume that the money market fund started with a market-based net asset value of \$1.00. It is our understanding that at any point in time, a large number of money market funds will not start from a market-based net asset value of \$1.00—many will start with a market-based net asset value of less than a dollar and thus a smaller interest rate change will cause the funds to break the buck.

¹⁴⁶ Interest rate shocks of a 300 basis point magnitude over a relatively short period of time have occurred, although not since the late 1970s. See Federal Reserve Bank of New York, *Historical Changes of the Target Federal Funds and Discount Rates, 1971 to present*, available at <http://www.newyorkfed.org/markets/statistics/dlyrates/fedrate.html>. In low interest rate environments (such as today), a shock in interest rates could occur if the Federal Reserve determines to raise interest rates quickly, for example, to stave off inflation as

securities or to follow riskier portfolio strategies to increase yield. These funds do not appear to have had great difficulties in creating portfolios that generated competitive yields and attracted investors.¹⁵¹ Indeed, many domestic money market funds currently limit their WAM to a maximum of 60 days voluntarily, a limit they likely would have discontinued if they had experienced the management or competitive difficulties suggested by commenters.¹⁵² No commenter reported to us that any of these funds were doing so. We acknowledge that one consequence of our amendments may be to further “homogenize” fund portfolios as managers have fewer avenues to acquire yield by exposing the funds to risk, but we believe that the level of potential homogenization is justified to reduce the risk to investors that a money market fund will break the buck. In addition, we are not persuaded by comments that a likely consequence of a shortened maximum WAM will be riskier portfolios. Accordingly, we are adopting the 60-day WAM limitation as proposed.

2. Weighted Average Life

We are adopting, as proposed, a requirement that limits the dollar-weighted average life to maturity of a

¹⁵¹ Similarly, European stable value money market funds do not appear to have had these difficulties. As the Institutional Money Market Fund Association (IMMFA) notes in its comment letter, IMMFA funds (which manage a significant amount of stable value money market fund assets in Europe) have been required to maintain a maximum WAM of 60 days since 2002. The recent proposals by the European Union’s Committee of European Securities Regulators to create common requirements for European money market funds would impose a maximum 60-day WAM for short-term money market funds. See Committee of European Securities Regulators Consultation Paper, *A Common Definition of European Money Market Funds*, CESR/09-850 (Oct. 20, 2009), available at http://www.cesr.eu/index.php?page=consultation_details&id=151.

¹⁵² For some time and through various interest rate and market environments a large portion of domestic money market funds have maintained a maximum WAM of less than 60 days. According to data provided by the ICI, from January 1998 through April 2009, even the 75th percentile of prime money market funds has maintained an average WAM of 53 days and the 90th percentile of prime money market funds has maintained an average WAM of 65 days. Investment Company Institute, *Average Maturity of Taxable Prime Money Market Funds, 1998–2009*, available at <http://www.sec.gov/comments/s7-11-09/s71109-14.htm>. The 75th percentile of these funds only reported a WAM in excess of 60 days on 8 monthly occasions out of the 136 monthly time periods reported. We also note that to obtain a top rating from an NRSRO, money market funds must maintain a WAM of no greater than 60 days. According to the iMoneyNet Money Market Fund Analyzer Database, as of November 17, 2009, 61% of money market fund assets were held in funds that were top rated by at least one NRSRO and 34% of money market funds had a top rating from at least one NRSRO.

money market fund’s portfolio to 120 calendar days.¹⁵³ Unlike weighted average maturity, the weighted average life (or “WAL”) of a portfolio is measured without reference to any rule 2a–7 provision that otherwise permits a fund to shorten the maturity of an adjustable-rate security by reference to its interest rate reset dates.¹⁵⁴ The WAL limitation thus restricts the extent to which a fund can invest in longer term securities that may expose a fund to spread risk.¹⁵⁵

We proposed the WAL limitation because we were concerned that the traditional WAM limitation of rule 2a–7 does not require that a manager of a money market fund limit the spread risk associated with longer term adjustable-rate securities.¹⁵⁶ These securities are

¹⁵³ See amended rule 2a–7(c)(2)(iii). This limitation will apply to all money market funds (including taxable and tax-exempt funds).

¹⁵⁴ The Fidelity Comment Letter, the Comment Letter of HighMark Capital Management, Inc. (Sept. 8, 2009) (“HighMark Capital Comment Letter”), and the ICI Comment Letter requested that the Commission amend rule 2a–7 to specify how cash balances held by money market funds would be treated under the WAM and WAL limitations. For purposes of the WAM and WAL limitations, cash balances have a maturity of one day. The Tamarack Funds Comment Letter also suggested that the Commission address extendible notes. For purposes of the WAM and WAL limitations, in calculating the final legal maturity of a security extendible at the option of the issuer the security should be deemed fully extended. See amended rule 2a–7(d) (final maturity is determined with reference to the time at which a fund will unconditionally receive payment); see also Revisions to Rules Regulating Money Market Funds, Investment Company Act Release No. 21837 (Mar. 21, 1996) [61 FR 13956 (Mar. 28, 1996)] at n. 151 and accompanying text (discussing the unconditional right to receive payment with respect to demand features).

¹⁵⁵ See Morgan Stanley, *Weighted Average Life: Enhancing Money Market Fund Transparency* (2009), available at http://www.morganstanley.com/msang/msmintl/docs/en_US/common/comm/200907_mmm_update.pdf (“Morgan Stanley Investment Management is introducing WAL to supplement our WAM reporting. The WAL calculation is based on a security’s stated final maturity date or, when relevant, the date of the next demand feature when the fund may receive payment of principal and interest (such as a put feature). Accordingly, WAL reflects how a portfolio would react to deteriorating credit (widening spreads) or tightening liquidity conditions. We believe that when viewed alongside WAM, the supplemental WAL disclosure will provide investors with a further degree of insight into our portfolios’ structure.”).

¹⁵⁶ For example, if the market perceived an issuer’s credit risk as deteriorating, the spreads on that issuer’s 30-day floating-rate securities would likely widen to a lesser extent than the spreads on that issuer’s 397-day floating-rate securities because the longer term securities have a much longer exposure to the issuer’s credit risk (assuming neither security had a Demand Feature). Because the WAM limitation allows the use of interest rate reset dates to shorten the maturity of a security, each of the 397-day floating-rate securities and the 30-day floating-rate securities would be considered to have a maturity of one day. In contrast, under the WAL limitation we are today adopting each adjustable-rate security without a Demand Feature

more sensitive to credit spreads than short-term securities with final maturities equal to the reset date of the longer term security.¹⁵⁷ The WAL limitation will provide an extra layer of protection for funds and their shareholders against spread risk, particularly in volatile markets. We proposed a 120-day limit as a prudent limit recommended to us in the ICI Report and one that we understand is currently used by some money market fund managers.¹⁵⁸ We requested comment on whether a higher or lower WAL limitation would be more appropriate.

Twenty-one commenters supported adding a WAL limit to the rule.¹⁵⁹ One large money market fund manager, for example, described the WAL as “a very prudent addition to the rule that, combined with the minimum liquidity requirements * * * represents an important and substantive risk reduction in the permissible construction of a money fund portfolio.”¹⁶⁰ Another acknowledged that “the risk that such a security will begin to deviate significantly from its Amortized Cost increases with its maturity,” and agreed that “the new 120-day WAL limit should control this risk.”¹⁶¹

Two commenters generally opposed a WAL limitation.¹⁶² One urged us to consider, instead, revising the maturity-shortening provisions of rule 2a–7 to require money market funds to measure the maturity of adjustable-rate securities by reference to their final legal maturity date rather than the date at which the interest rate resets.¹⁶³ Such a change

would have a maturity equal to its final legal maturity. As a result, if spreads on these securities widen to different degrees due to changing market perceptions of credit risk or liquidity, the WAL limitation will capture these different risk exposures.

¹⁵⁷ See Proposing Release, *supra* note 2, at Section II.B.2.

¹⁵⁸ See, e.g., HighMark Capital Comment Letter (“We have been calculating a WAL for years and believe it will more appropriately reflect the total interest rate and spread risk of a portfolio.”). See also JPMorgan Prime Money Market Fund Quarterly Fact Sheet (Dec. 31, 2009), available at <https://www.jpmmorganfunds.com/cm/BlobServer/FS-PMMP.PDF?blobcol=urldata&blobtable=MungoBlobs&blobkey=id&blobwhere=1158572105887&blobheader=application%2FPDF&blobheadername1=Content-Disposition&ssbinary=true&blobheadervalue=inline;filename=FS-PMMP.PDF> (showing the fund’s WAL over the previous year).

¹⁵⁹ See, e.g., Bankers Trust Comment Letter; Goldman Sachs Comment Letter; Northern Funds Trustees Comment Letter.

¹⁶⁰ See BlackRock Comment Letter.

¹⁶¹ See Federated Comment Letter.

¹⁶² See Thrivent Comment Letter; USAA Comment Letter.

¹⁶³ See USAA Comment Letter. Amended rule 2a–7(d) allows money market funds to shorten the

would dramatically reduce the ability of money market funds to invest in floating rate securities, and as we discuss below, such a reduction may be unnecessary.¹⁶⁴ Another commenter asserted that the WAL limitation was unnecessarily restrictive of prime retail funds and disagreed with our assessment of the spread risk posed by floating-rate Government securities.¹⁶⁵ The commenter, however, offered no explanation of why the exposure to spread risk would have less harmful consequences for a prime retail fund than for other types of funds and thus be of less concern.

Most commenters supported the proposed WAL limit of 120 days,¹⁶⁶ which the ICI comment letter described as “flexible enough even during ‘normal’ market conditions to not unduly restrict a fund’s ability to offer a diversified portfolio of short-term, high quality debt securities.”¹⁶⁷ Four commenters supported a WAL with a longer term, with two of these commenters suggesting a longer WAL for government money market funds than for other money market funds.¹⁶⁸ One of these commenters argued that the spread risk associated with Government floating-rate securities is different from the spread risk associated with non-Government securities.¹⁶⁹ Another commenter only supported a WAL limitation applicable to Government securities with maturities of more than two years, arguing that applying a 120-day WAL to all adjustable-rate Government securities would disrupt the short-term debt markets and hinder

maturity of an adjustable-rate portfolio security for purposes of the WAM limitation by referring to the security’s interest rate reset date, rather than the final legal maturity of the security, if the security has a final maturity of 397 days or less (for corporate securities) or an interest rate that adjusts no less frequently than every 397 days for Government securities.

¹⁶⁴ This comment also implies that rule 2a–7 should only have a WAL limitation (and not a separate WAM limitation). We believe that the WAM and WAL limitations address different risks (with the WAM primarily aimed at limiting interest rate risk and the WAL primarily aimed at limiting spread risk) and thus believe having both limitations in rule 2a–7 protects money market funds and their investors.

¹⁶⁵ See Thrivent Comment Letter.

¹⁶⁶ See, e.g., BlackRock Comment Letter; Invesco Aim Comment Letter; Comment Letter of Ridge Worth Capital Management, Inc. (“RidgeWorth Comment Letter”).

¹⁶⁷ ICI Comment Letter.

¹⁶⁸ See Fidelity Comment Letter (supporting a 150-day WAL for government money market funds and a 120-day WAL for all other money market funds); Victory Cap. Mgt. Comment Letter (supporting a 150-day WAL); C. Wesselkamper Comment Letter (supporting a 180-day WAL for government money market funds and a 150-day WAL for all other money market funds); Wells Fargo Comment Letter (supporting a 180-day WAL).

¹⁶⁹ See Fidelity Comment Letter.

the ability of Government security issuers to meet internal funding needs.¹⁷⁰

On balance, we conclude that 120 days is an appropriate length of time for the WAL limitation. A WAL limitation of, for example, 90 days appears to be unnecessarily restrictive to money market funds because it could significantly constrain the range of high-quality, short-term debt securities in which money market funds may invest, particularly when combined with our new minimum liquidity requirements.¹⁷¹ Such a short WAL limitation also may provide spread risk protection beyond what is reasonably necessary to enhance the stability of money market funds. For a money market fund to break the buck while maintaining a WAL of 90 days, average spreads on *all* securities in the fund’s portfolio would have to widen beyond 200 basis points.¹⁷² Other securities held by money market funds may not simultaneously face such spread widening even if the commercial paper market is under stress.¹⁷³ Accordingly, protection across an *entire* money market fund portfolio against spread widening of the magnitude experienced in the commercial paper market during the fall of 2008 may be unnecessary.

On the other hand, we are not convinced that a WAL significantly longer than 120 days would be appropriate for a money market fund that is seeking to maintain a stable net

¹⁷⁰ See Comment Letter of Fannie Mae (Sept. 3, 2009) (“Fannie Mae Comment Letter”). One commenter also argued that a 120-day WAL would limit Government security issuers’ ability to meet their funding needs. See Fidelity Comment Letter.

¹⁷¹ One commenter stated that the Commission should not impose a WAL shorter than 120 days, asserting that a shorter limitation would be unnecessarily restrictive and limit a fund’s ability to maintain a diversified portfolio of high quality short-term debt securities. See Charles Schwab Comment Letter. No commenters supported a shorter WAL than 120 days.

¹⁷² This assumes that there are no other simultaneous shocks to the fund’s portfolio from redemption pressures or otherwise. In order to evaluate commenters’ discussion about the appropriate length of time for a WAL limitation in the context of the shocks a money market fund might face, we again referred to stress test scenarios.

¹⁷³ Such spread widening even in commercial paper has been rare and commercial paper typically only comprises a portion of money market funds’ portfolios. Spreads between 3-month commercial paper and the 3-month Treasury bill widened to approximately 300 basis points at the height of the financial crisis in the fall of 2008 and widened similarly in the mid-1970s, but otherwise have rarely widened by 200 basis points in the last 50 years. This analysis is based on commercial paper spread data contained in Bradley T. Ewing, Gerald J. Lynch & James E. Payne, *Monetary Volatility and the Paper-Bill Spread*, in Progress in Economics Research (2006), at p. 58, supplemented with data from Bloomberg on spreads between yields of 3-month commercial paper and the 3-month Treasury bill.

asset value. For example, with a 150-day WAL, a money market fund would break the buck with a spread widening of just over 120 basis points (assuming no other simultaneous stresses on the fund’s portfolio).¹⁷⁴ Historically, commercial paper spreads, for example, have widened to that extent fairly frequently.¹⁷⁵ Given this limited resilience to spread widening, and given that a money market fund would break the buck even earlier if any other shocks to the fund’s portfolio occurred simultaneously, we have determined not to adopt a longer WAL, such as a 150- or 180-day WAL. We note that the European Union’s Committee of European Securities Regulators has also recently proposed requiring that short-term money market funds adhere to a maximum 120-day WAL.¹⁷⁶

Finally, we are not providing for a longer WAL for money market funds that primarily invest in Government securities. While some commenters asserted that adjustable-rate Government securities have a more benign credit risk profile,¹⁷⁷ they are still exposed to widening interest rate spreads to the same extent as non-Government securities and, as we noted in the Proposing Release, spreads on certain adjustable-rate Government securities did widen during the fall of

¹⁷⁴ This is based on our staff’s analysis of stress test scenarios.

¹⁷⁵ See Ewing *et al.*, *supra* note 173, at 58.

¹⁷⁶ See Committee of European Securities Regulators Consultation Paper, *A Common Definition of European Money Market Funds*, CESR/09–850 (Oct. 20, 2009), available at http://www.cesr.eu/index.php?page=consultation_details&id=151. In addition, Europe’s Institutional Money Market Fund Association (IMMFA) recently has adopted changes to its code of conduct that will require IMMFA money market funds to adhere to a maximum 120-day WAL. See IMMFA Code of Practice, at Section 40, available at <http://www.immfa.org/About/Codefinal.pdf>.

We also note that the rating agencies have taken varied approaches to limiting the WAL of rated money market funds. Fitch has adopted revised ratings requirements limiting top-rated money market funds to a WAL of 120 days, but allowing longer WALs for lesser rated money market funds. See Fitch Ratings, *Global Money Market Fund Rating Criteria* (Oct. 5, 2009), available at http://www.fitchratings.com/creditesk/reports/report_frame.cfm?rpt_id=470368. Standard & Poor’s has proposed more restrictive requirements that would limit top-rated money market funds to a WAL of 90 days, subject to upward adjustment to no more than 120 days depending on the extent of Government securities in the money market fund’s portfolio. See Standard & Poor’s, *Principal Stability Fund Rating Criteria* (Jan. 5, 2010), available at <http://www2.standardandpoors.com/spf/pdf/events/FITcon11410RFC.pdf>.

¹⁷⁷ See, e.g., Fidelity Comment Letter. But see BlackRock Comment Letter (recent events have shown that spread relationships can be variable for agency securities); Wells Fargo Comment Letter (credit spreads on Government securities widened to a significant degree in 2008).

2008.¹⁷⁸ In addition, many prime money market funds also hold a sizeable portion of Government securities (and may hold even more Government securities after the adoption of rule 2a-7's new liquidity requirements). Given this fact, allowing government money market funds to have a longer WAL solely because they hold more Government securities than prime funds do, does not appear to us to be an approach that treats the risks attendant to longer term, adjustable-rate Government securities equally, and thus appears inappropriate.

3. Maturity Limit for Government Securities

The Commission is deleting a provision of rule 2a-7 that has permitted a fund that relied exclusively on the penny-rounding method of pricing to acquire Government securities with remaining maturities of up to 762 days, rather than the 397-day limit otherwise provided by the rule.¹⁷⁹ As we noted in the Proposing Release,¹⁸⁰ we are unaware of any money market fund that currently relies solely on the penny-rounding method of pricing, and none that holds *fixed-rate* Government securities with remaining maturities of two years, which would involve the assumption of a substantial amount of interest rate risk. We received one comment on this topic, which supported the change.¹⁸¹ Accordingly, we are adopting this change as proposed.¹⁸²

¹⁷⁸ See Proposing Release, *supra* note 2, at Section II.B.2. We understand that many floating-rate securities issued by Federal agencies and outstanding during the financial crisis had rates tied to LIBOR. As noted in the Proposing Release, the "TED" spread (the difference between the U.S. Treasury Bill rate and LIBOR) reached a high of 463 basis points on October 10, 2008. See *id.*, at n.67. We understand that most adjustable-rate Government securities held by money market funds had a final maturity of two years or less and thus limiting the WAL limitation to adjustable-rate Government securities with final maturities greater than two years would not address these securities' spread risk.

¹⁷⁹ See current rule 2a-7(c)(2)(ii). In a conforming change, we also are amending as proposed the maturity-shortening provision of the rule for variable-rate Government securities to require that the variable rate of interest is readjusted no less frequently than every 397 days, instead of 762 days as the rule has permitted. See amended rule 2a-7(d)(1).

¹⁸⁰ See Proposing Release, *supra* note 2, at Section II.B.3.

¹⁸¹ See BlackRock Comment Letter.

¹⁸² We also requested comment in the Proposing Release on whether we should impose a limitation on the maximum final legal maturity of adjustable-rate Government securities that money market funds are permitted to acquire. We received only two comments on this proposal. One commenter encouraged us to constrain any limitation on adjustable-rate Government securities with a final legal maturity in excess of two years. See Fannie

C. Portfolio Liquidity

We are amending rule 2a-7 to require that money market funds maintain a sufficient degree of liquidity necessary to meet reasonably foreseeable redemption requests and reduce the likelihood that a fund will have to meet redemptions by selling portfolio securities into a declining market. As discussed in the Proposing Release, money market funds generally have a higher and less predictable volume of redemptions than other open-end investment companies.¹⁸³ Their ability to maintain a stable net asset value will depend, in part, on their ability to convert portfolio holdings to cash to pay redeeming shareholders without having to sell them at a loss. The liquidity of fund portfolios became a critical factor in permitting them to absorb very heavy redemption demands in the fall of 2008 when the secondary markets for many short-term securities seized up.

Commenters generally agreed with our analysis of the liquidity needs of money market funds. They emphasized the importance of liquidity for money market funds and their ability to meet shareholder redemptions.¹⁸⁴ Several also acknowledged the need to place outside limits on the risks money market funds may take.¹⁸⁵ Most commenters supported amending the rule to impose more robust liquidity requirements, but many disagreed with our specific proposals.¹⁸⁶ Some asserted that the proposed requirements might negatively affect funds' ability to manage their portfolios, place excessive

Mae Comment Letter. Another asserted that the WAL limitation provided a sufficient limitation on the risks posed by long-term adjustable-rate Government securities. See Federated Comment Letter. We are aware that WAL creates some limitation of this risk, but that even with a 120-day WAL limitation, a fund would still have some ability to acquire longer term adjustable-rate Government securities. No commenters provided us with any data on the extent of adjustable-rate Government securities outstanding from time to time. Two commenters indicated that these securities experienced variable spreads during the financial crisis. See BlackRock Comment Letter; Wells Fargo Comment Letter. In the future, we may reconsider whether to limit the maximum maturity of adjustable-rate Government securities that can be held by money market funds after obtaining additional data.

¹⁸³ See Proposing Release, *supra* note 2, at n.172 and accompanying text.

¹⁸⁴ See, e.g., Comment Letter of the Securities Industry and Financial Markets Association (Sept. 8, 2009) ("SIFMA Comment Letter"); State Street Comment Letter.

¹⁸⁵ See, e.g., Federated Comment Letter; Comment Letter of the Independent Directors Council (Sept. 8, 2009) ("IDC Comment Letter").

¹⁸⁶ See, e.g., State Street Comment Letter (opposing a general liquidity standard and different minimum liquidity thresholds for retail and institutional funds); Invesco Aim Comment Letter (same).

burdens on the board of directors, and affect the markets of some portfolio securities.¹⁸⁷ Others argued that the proposals are not sufficient to meet money market funds' liquidity concerns.¹⁸⁸

After reviewing the comments, and based on our analysis of redemption activity during the 2008 run on money market funds, we are amending rule 2a-7 to add three new provisions, substantially as proposed, which address different aspects of portfolio liquidity.¹⁸⁹ Together, we believe they will result in money market funds that are better able to absorb large amounts of redemptions.

1. General Liquidity Requirement

We are amending rule 2a-7, as proposed, to require that each money market fund hold securities that are sufficiently liquid to meet reasonably foreseeable shareholder redemptions in light of its obligations under section 22(e) of the Act and any commitments the fund has made to shareholders (the "general liquidity requirement").¹⁹⁰ Depending upon the volatility of its cash flows (particularly shareholder redemptions), this new provision may require a fund to maintain greater liquidity than would be required by the daily and weekly minimum liquidity requirements set forth in the rule and discussed below.

Most commenters who addressed this proposal supported the addition of a general liquidity requirement.¹⁹¹ They agreed that funds should be required to assess appropriate levels of liquidity above the minimums set forth in the rule.¹⁹² Some commenters, however, expressed concerns that the proposed requirement was too vague,¹⁹³ or was

¹⁸⁷ See, e.g., Fidelity Comment Letter; ICI Comment Letter; Shadow FRC Comment Letter.

¹⁸⁸ See, e.g., Fund Democracy/CFA Comment Letter (requesting that the Commission mandate private liquidity insurance for money market funds); HighMark Capital Comment Letter (suggesting a private liquidity bank or that Treasury continue to provide emergency liquidity as possible solutions to address liquidity concerns); Vanguard Comment Letter (asserting that the proposed rule does not address liquidity risk arising from factors other than size of accounts, such as geographical concentration of the shareholders); Waddell & Reed Comment Letter (recommending some type of permanent backstop be available to money market funds); Wells Fargo Comment Letter (suggesting the Federal Reserve set up a secured lending facility to serve as a lender of last resort).

¹⁸⁹ See Proposing Release, *supra* note 2, at Section II.C.1-2.

¹⁹⁰ Amended rule 2a-7(c)(5).

¹⁹¹ See, e.g., ICI Comment Letter; Northern Funds Indep. Trustees Comment Letter; Tamarack Funds Comment Letter.

¹⁹² See, e.g., Federated Comment Letter; ICI Comment Letter.

¹⁹³ See, e.g., Charles Schwab Comment Letter; Dreyfus Comment Letter. We note, however, that

unnecessary in light of the minimum daily and weekly liquidity requirements.¹⁹⁴ We disagree. Funds will have different liquidity needs that we cannot sufficiently anticipate and codify in a rule beyond the minimums we are adopting today.¹⁹⁵ Therefore, we believe it is incumbent upon the management of each fund and its board of directors to evaluate the fund's liquidity needs and to protect the fund and its shareholders from the harm that can occur from failure to properly anticipate and provide for those needs.

To comply with this general liquidity requirement, we would expect money market fund managers to consider factors that could affect the fund's liquidity needs, including characteristics of a money market fund's investors and their likely redemptions.¹⁹⁶ For example, some shareholders may have regularly recurring liquidity needs, such as to meet monthly or more frequent payroll requirements. Others may have liquidity needs that are associated with particular annual events, such as holidays or tax payment deadlines. A fund also would need to consider the extent to which it may require greater liquidity at certain times when investors' liquidity needs may coincide. In addition, a volatile or more concentrated shareholder base would require a fund to maintain greater liquidity than a stable shareholder base consisting of thousands of retail investors.¹⁹⁷

similar general requirements in rule 2a-7 have not hampered fund managers. *See, e.g.*, current rule 2a-7(c)(2) (requiring a money market fund to maintain a dollar-weighted average portfolio maturity appropriate to its objective of maintaining a stable net asset value per share or price per share). Thus, we do not share commenters' concerns that the general liquidity standard could expose a money market fund to liability based on hindsight review of the fund's subjective determinations and market events.

¹⁹⁴ *See, e.g.*, TDAM Comment Letter. Another commenter asserted that money market funds are already subject to this requirement under section 22(e) of the Act. *See* State Street Comment Letter. The general liquidity requirement, together with rule 2a-7's specific obligations related to illiquid securities and daily and weekly liquid assets, identifies the liquidity obligations that are specific to money market funds.

¹⁹⁵ For example, suggestions that we require each fund to maintain sufficient liquidity to meet redemptions by the largest shareholders seem inadequate because they assume that only those shareholders will redeem. *See* Stradley Ronon Comment Letter; SIFMA Comment Letter.

¹⁹⁶ *See* Proposing Release, *supra* note 2, at text following n.205.

¹⁹⁷ *See* Thrivent Comment Letter (suggesting that we approach portfolio liquidity on the basis of concentration among a fund's shareholders). In determining the amount of liquidity available to meet the requirements of rule 2a-7, funds should not consider the fund's ability to access overdraft protection, lines of credit, and inter-fund borrowing arrangements. *See* Federated Comment Letter

Thus, to comply with rule 2a-7, as amended, money market funds should adopt policies and procedures designed to assure that appropriate efforts are undertaken to identify risk characteristics of shareholders.¹⁹⁸ In other words, fund boards should make sure that the adviser is monitoring and planning for "hot money." In their consideration of these procedures and in the oversight of their implementation, fund boards should appreciate that, in some cases, fund managers' interests in attracting additional fund assets may be in conflict with their overall duty to manage the fund in a manner consistent with maintaining a stable net asset value.¹⁹⁹ We urge directors to consider the need for establishing guidelines that address this conflict.

As some commenters noted, identification of these risks may be more challenging when share ownership is less transparent because the shares are held in omnibus accounts.²⁰⁰ Funds may seek access to information about the investors who hold their interests through omnibus accounts in addition to considering information about the omnibus accounts, including their aggregate historical redemption patterns

(suggesting that we adopt the opposite approach). A fund that borrowed to satisfy redemptions would leverage its holdings, thus amplifying the risk of shareholder losses if the fund eventually broke the buck.

¹⁹⁸ Upon adoption of these amendments, such policies and procedures are, we believe, required under rule 38a-1 under the Investment Company Act (the "compliance rule"). Although two commenters suggested that the requirement to adopt the policies and procedures should be incorporated in rule 2a-7, we do not see a reason to duplicate the requirements for policies and procedures encompassed in the compliance rule. *See* Dreyfus Comment Letter; Comment Letter of Fifth Third Asset Management, Inc. (Sept. 8, 2009) ("Fifth Third Comment Letter"). One commenter recommended that "know your customer" policies apply only to shareholders whose redemptions (in their entirety) would have a material impact on the fund's ability to satisfy redemptions. Stradley Ronon Comment Letter. *See also* SIFMA Comment Letter. Another commenter argued that the relevant shareholder characteristics should be limited to clearly defined parameters such as historical net flows. *See* RidgeWorth Comment Letter. We are not identifying specific characteristics that should be addressed in a fund's policies and procedures because we believe that money market funds are in a better position to do so. For example, concurrent redemptions of several shareholders may have a material effect on a fund's ability to satisfy redemptions even if the shareholders' individual redemptions alone would not have such an effect. Nor are we setting limits as to the scope of the policies and procedures because different money market funds may have different needs in this regard.

¹⁹⁹ *See* Proposing Release, *supra* note 2, at n.180 and accompanying text.

²⁰⁰ *See, e.g.*, Comment Letter of the Coalition of Mutual Fund Investors (Sept. 10, 2009) ("CMFI Comment Letter"); HighMark Capital Comment Letter.

and the account recordholder's ability to redeem the entire account.²⁰¹

2. Limitation on Acquisition of Illiquid Securities

We are amending rule 2a-7 to further limit a money market fund's investments in illiquid securities (*i.e.*, securities that cannot be sold or disposed of in the ordinary course of business within seven days at approximately the value ascribed to them by the money market fund).²⁰² Under the amended rule, a money market fund cannot acquire illiquid securities if, immediately after the acquisition, the fund would have invested more than five percent of its total assets in illiquid securities.²⁰³

In light of the risk that liquid assets would become illiquid thereby impairing the ability of a money market fund to meet redemption demands, we proposed to prohibit funds from acquiring securities that were, at the time of their acquisition, already illiquid. Many fund commenters objected, arguing such a limitation could preclude them from investing in certain high quality illiquid securities in which money market funds have historically invested,²⁰⁴ make it more difficult for tax-exempt funds to construct a well-diversified, high quality portfolio,²⁰⁵ and prevent funds from investing in new types of securities that are illiquid until a market for them has been established.²⁰⁶ Others asserted that a ban may be unnecessary in light

²⁰¹ Some commenters argued that we should require greater transparency of investments held through financial intermediaries to allow funds to better monitor client profiles. *See, e.g.*, BlackRock Comment Letter; CMFI Comment Letter. Funds may seek to access this information in contractual arrangements with their financial intermediaries.

²⁰² We have construed section 22(e) of the Investment Company Act, which requires registered investment companies to satisfy redemption requests within seven days, to restrict a money market fund from investing more than 10% of its assets in illiquid securities. *See* 1983 Adopting Release, *supra* note 6, at nn.37-38 and accompanying text; Acquisition and Valuation of Certain Portfolio Instruments by Registered Investment Companies (Mar. 12, 1986) [51 FR 9773 (Mar. 21, 1986)], at n.21 and accompanying text; Proposing Release, *supra* note 2, at n.171 and accompanying text.

²⁰³ Amended rule 2a-7(c)(5)(i).

²⁰⁴ These include, among other securities, term repurchase agreements, some time deposits, and insurance company funding agreements. *See, e.g.*, Am. Bankers Assoc. Comment Letter; Comment Letter of New York Life Investments (Sept. 14, 2009); Comment Letter of Promontory Interfinancial Network, LLC (Sept. 8, 2009); Wells Fargo Comment Letter.

²⁰⁵ *See* Stradley Ronon Comment Letter; Wells Fargo Comment Letter.

²⁰⁶ *See, e.g.*, Deutsche Comment Letter; Stradley Ronon Comment Letter; USAA Comment Letter.

of the new daily and weekly liquidity standards.²⁰⁷

These comments persuaded us that prohibiting funds from acquiring *any* illiquid securities may have undesirable consequences for money market funds. Instead, we are further limiting the circumstances under which a money market fund may acquire illiquid securities. Under the amended rule, a fund cannot acquire an illiquid security if, after the purchase, more than five percent of the fund's total assets would consist of illiquid securities.²⁰⁸ Several commenters suggested that we lower the existing 10 percent limit as an alternative to our proposal.²⁰⁹ We are reducing by half the existing limit in order to strike a balance between our concern regarding liquidity risk, *i.e.*, a fund's ability to satisfy redemption demands if it is holding illiquid securities, and funds' concerns that they retain some ability to make investments in high quality illiquid securities.

We are also amending the rule to define the term "illiquid security" as a security that cannot be sold or disposed of in the ordinary course of business within seven days at approximately the value ascribed to it by the money market fund. At the suggestion of commenters, we would not treat as illiquid a security that could not be sold at amortized cost.²¹⁰

3. Minimum Daily and Weekly Liquidity Requirements

The Commission is adopting new liquidity requirements that mandate each money market fund maintain a portion of its portfolio in cash and securities that can readily be converted

into cash. More specifically, we are amending rule 2a-7 to require all *taxable* money market funds to hold at least 10 percent of their total assets in "daily liquid assets" and *all* money market funds to hold at least 30 percent of their total assets in "weekly liquid assets."²¹¹ A money market fund must comply with the daily and weekly liquidity standards at the time each security is acquired.²¹²

As we explained in the Proposing Release, current liquidity standards applicable to money market funds presume that a fund is able to find a buyer of its securities.²¹³ Our new approach would include as a "daily liquid asset" or "weekly liquid asset" only cash or securities that can readily be converted to cash (as discussed below). Thus, a fund should be able to use those assets to pay redeeming shareholders even in market conditions (such as those that occurred in September and October 2008) in which money market funds cannot rely on a secondary or dealer market to provide immediate liquidity.

Commenters who addressed the issue largely supported the introduction of daily and weekly liquidity standards.²¹⁴ One large sponsor of money market funds asserted that it "recognize[d] that a meaningful and sustained level of liquidity has the potential to ease concerns of investors and may be useful for unforeseen events."²¹⁵ Another agreed that "mandating liquidity requirements will bolster investor confidence in the ability of money market funds to sustain prolonged redemption pressures with increased

levels of immediate cash on hand, both on a daily and weekly basis."²¹⁶ One commenter, however, urged us to rely solely on the general liquidity requirement, arguing that requiring a minimum requirement would require unnecessary levels of liquidity at times that will not be sufficient during a severe market crisis.²¹⁷

Markets can become illiquid very rapidly in response to events that money market fund managers may not anticipate. The failure of a single fund to anticipate such conditions may lead to a run of the sort we saw in September 2008 affecting all or many funds. We think it would be ill-advised to rely solely on the ability of managers to anticipate liquidity needs, which may arise from events the money market fund manager cannot anticipate or control. We acknowledge our minimum standards alone may not establish sufficient liquidity to allow funds to meet every liquidity crisis, which is why we also are adopting a general liquidity requirement (discussed above) to supplement the minimum requirements.

Distinguishing between Retail and Institutional Funds. In the Proposing Release, we observed that institutional money market funds need (and typically maintain) greater portfolio liquidity. These funds had substantially greater redemption pressure on them in the fall of 2008. During the four-week period ending October 8, 2008, prime institutional funds (or share classes) experienced 30 percent net outflows compared to only 4.6 percent outflows of prime retail funds, according to data compiled by the ICI.²¹⁸ Consequently, we proposed to impose substantially lower liquidity requirements on retail funds because the higher thresholds appeared unnecessary and would have resulted in higher costs on them in terms of lower yields. For example, instead of 30 percent "weekly liquid assets," we proposed to require that

²⁰⁷ See, e.g., Charles Schwab Comment Letter; TDAM Comment Letter.

²⁰⁸ Amended rule 2a-7(c)(5)(i).

²⁰⁹ See Federated Comment Letter; J.P. Morgan Asset Mgt. Comment Letter; Vanguard Comment Letter; Wells Fargo Comment Letter (all recommending a 5% percent limit). See also TDAM Comment Letter (recommending that we reduce the existing limit). Other commenters argued that we should maintain the 10% limit. See, e.g., Charles Schwab Comment Letter; Deutsche Comment Letter.

²¹⁰ See amended rule 2a-7(a)(19). See, e.g., Charles Schwab Comment Letter; Wells Fargo Comment Letter. The proposed rule defined "liquid security" with reference to the security's "amortized cost value." See proposed rule 2a-7(a)(18). Under the amended rule, a money market fund using the amortized cost method will be able to treat as liquid a security that the fund can sell at a price that deviates from the security's amortized cost value, as long as the price approximates the market-based value that the fund has ascribed to the security for purposes of determining its shadow price. Because the market-based value assigned by a money market fund to its securities is the measure that ultimately justifies the fund's use of a stable net asset value, a money market fund should treat as illiquid any security that cannot be sold at a price approximating such market-based value. See 1983 Adopting Release, *supra* note 6, at n.37 and paragraphs following n.39.

²¹¹ See amended rule 2a-7(c)(5)(ii)-(iii). See also amended rule 2a-7(a)(8) (defining "daily liquid assets"); 2a-7(a)(32) (defining "weekly liquid assets"); *infra* notes 229-243 and accompanying text. "Total assets" means with respect to a money market fund using the amortized cost method, the total amortized cost of its assets and, with respect to any other money market fund, the total market-based value of its assets. See amended rule 2a-7(a)(27).

²¹² See amended rule 2a-7(a)(8); 2a-7(a)(32). One commenter recommended that the minimum liquidity standards apply on an ongoing basis, which could require money market funds with holdings that fall below the requirements to sell securities in order to meet the requisite daily and weekly liquid asset thresholds. See Fund Democracy/CFA Comment Letter. We do not agree with such an approach. A money market fund whose portfolio does not meet the minimum daily or weekly liquidity standards is not in violation of the rule, but may not acquire any assets other than daily or weekly liquid assets. See Dreyfus Comment Letter (requesting that the standards incorporate some flexibility to allow funds not to comply with them under unforeseeable circumstances).

²¹³ See Proposing Release, *supra* note 2, at Section II.C.2.

²¹⁴ See, e.g., Calvert Comment Letter; Vanguard Comment Letter.

²¹⁵ J.P. Morgan Asset Mgmt. Comment Letter.

²¹⁶ Invesco Aim Comment Letter.

²¹⁷ See Wells Fargo Comment Letter. See also T. Rowe Price Comment Letter (the weekly liquidity standard is overly restrictive in light of the daily liquidity standard and other proposed changes to rule 2a-7).

²¹⁸ See ICI, *Money Market Mutual Fund Assets Historical Data*, available at http://www.ici.org/pdf/mm_data_2010.pdf. See also Proposing Release, *supra* note 2, at n.63 and accompanying text. The Proposing Release also noted that on September 17, 2008, approximately 4% of prime retail money market funds (or share classes) and 25% of prime institutional money market funds had outflows greater than 5%; on September 18, 2008, approximately 5% of prime retail funds and 30% of prime institutional funds had outflows greater than 5%; and on September 19, 2008, approximately 5% of prime retail funds and 22% of prime institutional funds had outflows greater than 5%. Proposing Release, *supra* note 2, at n.185.

retail prime money market funds maintain 15 percent “weekly liquid assets.” We proposed to require that each money market fund’s board make an annual determination whether a fund was an institutional fund (and thus subject to the higher liquidity requirements) based on the nature of record owners of shares, minimum initial investment requirements, and cash flows from purchases and redemptions.²¹⁹

Most commenters representing money market funds argued against drawing such a regulatory distinction, asserting that there are inherent difficulties in determining the difference between the two types of funds within a generally applicable definition.²²⁰ Commenters asserted that many money market funds include both types of shareholders, and even if one could distinguish a fund with an institutional rather than a retail shareholder base, not all shareholders behave in the same manner and present the same liquidity challenges as their peers.²²¹ Others expressed concern that the fund’s board is not in the best position to make these determinations.²²² The difficulty in drawing bright lines led some commenters to express concern with the competitive consequences that might result when fund boards of directors come to different conclusions.²²³

²¹⁹ See proposed rule 2a–7(a)(17) (defining “institutional fund”); Proposing Release, *supra* note 2, at Section II.C.2.a-b.

²²⁰ See, e.g., BlackRock Comment Letter; Goldman Sachs Comment Letter; ICI Comment Letter; Comment Letter of TCW Investment Management Company (Sept. 4, 2009); Vanguard Comment Letter. A few commenters expressed support for the distinction. See, e.g., Dreyfus Comment Letter; Fidelity Comment Letter; USAA Comment Letter.

²²¹ See, e.g., GE Asset Mgt. Comment Letter; SIFMA Comment Letter; State Street Comment Letter. Many also argued that the nature of the financial intermediary record owner does not always correspond to the behavior of the ultimate investor. See, e.g., T. Rowe Price Comment Letter; Vanguard Comment Letter. A few commenters objected for other reasons. See Comment Letter of the Committee of Annuity Insurers (Sept. 8, 2009) (“Committee Ann. Insur. Comment Letter”) (the characterization as retail or institutional would be confusing for investors); J.P. Morgan Asset Mgt. Comment Letter (retail investors would suffer if they invested in an institutional fund through an omnibus account or a money market fund lost its retail status because of institutional investments in the fund); Comment Letter of Russell Investment Management Company (Sept. 8, 2009) (“Russell Inv. Comment Letter”) (money market funds would incur substantial costs to monitor and enforce the distinction); Waddell & Reed Comment Letter (the distinction is punitive for retail money market funds, which have a less concentrated shareholder base).

²²² See, e.g., IDC Comment Letter; Comment Letter of the New York City Bar Association (Sept. 8, 2009) (“NYC Bar Assoc. Comment Letter”).

²²³ See, e.g., Comment Letter of FAF Advisors (Sept. 9, 2009) (“FAF Advisors Comment Letter”) (in the absence of clear guidelines, boards would likely

We anticipated these concerns and requested comment on alternative approaches. One commenter suggested that we treat as institutional a fund that has any class which offers same day liquidity to shareholders.²²⁴ We are uncertain, however, whether institutional investors will be willing to migrate to funds that offer next day liquidity in order to obtain additional yield, and if they did our purpose in drawing the distinction would be defeated. We have similar concerns that institutional investors might invest in retail funds that are defined with respect to minimum initial account sizes or maximum expense ratios, as suggested by other commenters.²²⁵ The suggestion that the distinction be based on average account size raises different concerns, including the appropriate size for this measure and whether it should be based on total assets in omnibus accounts or in the accounts of the underlying shareholders.²²⁶

Taking into account the comments and after further consideration, we have not identified an effective way at this time to distinguish between types of money market funds to achieve our purpose. Therefore, we have determined to apply the same minimum liquidity standards to both institutional and retail money market funds.²²⁷ We believe the compelling need to limit the liquidity risk of money market funds before another run occurs is reason not to further distinguish retail from institutional money market funds. We intend, however, to consider revisiting our determination to apply the same minimum liquidity standards to all money market funds and reevaluate whether there is a workable objective definition that would accurately identify funds with lower liquidity needs and thus justify applying lower minimum standards to them.²²⁸

characterize funds with largely the same shareholder base differently); Goldman Sachs Comment Letter (the distinction would create an incentive to characterize a fund as retail so that the fund would be subject to the lower standard); IDC Comment Letter (a board might take a conservative approach and identify more funds as institutional at the expense of the funds’ shareholders).

²²⁴ See Fidelity Comment Letter. See also Charles Schwab Comment Letter; Waddell & Reed Comment Letter.

²²⁵ See HighMark Capital Comment Letter; T. Rowe Price Comment Letter.

²²⁶ See Waddell & Reed Comment Letter. Similar concerns would arise if we used the definition the ICI uses for its analysis of retail money market share classes, *i.e.*, those “offered primarily to individuals with moderate-sized accounts.” See http://www.ici.org/my_ici/mmf_developments/faqs_money_funds.

²²⁷ See amended rule 2a–7(c)(5)(ii)–(iii).

²²⁸ One commenter suggested that we impose different minimum liquidity standards for government and non-government money market

New Daily and Weekly Minimum Liquidity Requirements. We are adopting the higher minimum liquidity thresholds we proposed for all money market funds. Under the final rule, (i) no taxable money market fund can acquire any security other than a daily liquid asset if, immediately after the acquisition, the fund would have invested less than 10 percent of its total assets in daily liquid assets, and (ii) no money market fund can acquire any security other than a weekly liquid asset if, immediately after the acquisition, the fund would have invested less than 30 percent of its total assets in weekly liquid assets.²²⁹ We proposed these liquidity levels based on the levels of cash and overnight repurchase agreements that we believe reflect the liquidity needs of money market funds with institutional investors or other investors with similar liquidity needs.²³⁰

A few commenters supported our proposed levels for daily and weekly liquid assets, but most supported the lower levels recommended in the ICI Report of five percent of portfolios in daily liquid assets and 20 percent of portfolios in weekly liquid assets.²³¹ Commenters argued that when combined with our other proposals, these thresholds would provide sufficient protection to investors.²³² They also suggested that the lower levels strike an appropriate balance of improving funds’ liquidity while providing sufficient flexibility to allow portfolio managers to meet the challenges of different market conditions.²³³

funds. See C. Wesselkamper Comment Letter. We believe this is unnecessary, however, given that most Government money market funds have sufficient holdings of Treasury securities and Government agency discount notes to satisfy the rule’s requirements for daily and weekly liquid assets. See amended rule 2a–7(a)(8) (defining “daily liquid assets”); 2a–7(a)(32) (defining “weekly liquid assets”).

²²⁹ Amended rule 2a–7(c)(5)(ii)–(iii).

²³⁰ See Proposing Release, *supra* note 2, at n.191 and accompanying and following text.

²³¹ See, e.g., FAF Advisors Comment Letter; Invesco Aim Comment Letter. Others recommended different standards. See Crane Data Comment Letter (5% daily and 15% weekly liquidity for all money market funds); Fifth Third Comment Letter (10% daily liquidity and 25% weekly liquidity for all money market funds); J.P. Morgan Asset Mgt. Comment Letter (5% daily liquidity for taxable money market funds and 20% weekly liquidity for all money market funds); Vanguard Comment Letter (weekly liquidity requirement for institutional funds should not exceed 25%).

²³² See Dreyfus Comment Letter (\$119 billion redeemed in institutional funds during the week of September 17, 2008 represented 5% of institutional fund assets as reported by iMoneyNet on August 5, 2009); FAF Advisors Comment Letter; Goldman Sachs Comment Letter.

²³³ See Invesco Aim Comment Letter.

We are concerned that the lower minimum liquidity levels suggested by commenters would be insufficient to establish an adequate liquidity floor for money market funds in the event of a crisis such as we experienced in September 2008. The five percent daily liquidity level would have been insufficient to satisfy redemptions in one-fifth of prime institutional funds (or share classes) on each of three days during the week of September 15, and the 20 percent weekly liquidity level would have been insufficient to address outflows in more than a quarter of those funds during that week.²³⁴ We would be concerned if such a large portion of money market funds had to increase their liquidity quickly in response to sudden market turmoil at the same time the overall market experiences a flight to liquidity.²³⁵ As we noted above, one fund's inability to satisfy redemption requests may lead to a run on other money market funds.²³⁶ Accordingly, we believe that the floor we establish for minimum liquidity requirements must be sufficiently high to allow most money market funds to manage their liquidity risk in a crisis, particularly when they may experience significant redemption requests on successive days.²³⁷ For this reason, we have

²³⁴ On September 17, 2008, approximately 25% of prime institutional money market funds experienced outflows greater than 5% of total assets; on September 18, 2008, approximately 30% of prime institutional money market funds experienced outflows greater than 5%; and on September 19, 2008, approximately 22% of prime institutional money market funds experienced outflows greater than 5%. As noted in the Proposing Release, during that week, approximately 27% of prime institutional money market funds experienced redemptions of more than 20% of assets, and 22% had outflows greater than 25%. This is based on analysis of data from the iMoneyNet Money Fund Analyzer Database. Proposing Release, *supra* note 2, at n.185.

²³⁵ As of January 20, 2010, assets in taxable institutional share classes represented approximately 63% of the total assets of money market funds, and assets in prime institutional share classes represented approximately 37% of the total assets of money market assets. See ICI, *Money Market Mutual Fund Assets*, available at http://www.ici.org/research/stats/mmf/mm_01_21_10.

²³⁶ See *supra* text following note 217.

²³⁷ In support of its proposed lower liquidity levels, the ICI stated that the 5% daily and 20% weekly thresholds "would have met the demands of a large majority of the prime funds with at least one institutional share class" and noted that between September 10 through 24, 52% of these funds had outflows of less than 5 percent, and 22 percent experienced outflows of between 5% and 20% of assets, which would have been covered by the thresholds recommended by the ICI Report. Under the ICI's analysis, however, one quarter of prime money market funds would *not* have been covered by the thresholds recommended by the ICI Report, which as discussed above, we believe is too large a proportion that might have to increase liquidity quickly in response to sudden severe economic stress. We are not considering the redemption levels of the week following September 19, when the

adopted the higher liquidity thresholds, under which we estimate that approximately 90 percent of retail and institutional funds would have been able to satisfy the level of redemption demands during individual days as well as the week of greatest redemption pressure in the fall of 2008 (September 15–19).²³⁸ At the same time, we appreciate commenters' concerns that the proposed liquidity thresholds would limit funds' flexibility to meet the challenges of different market conditions. In order to address those concerns as well as our concerns regarding liquidity risk, the amendments preserve funds' ability to invest in a limited amount of illiquid securities, which is designed to permit funds some flexibility in dealing with varying market conditions.²³⁹

Tax-Exempt Money Market Funds. As proposed, the final rule excludes tax-exempt money market funds from the daily liquidity requirements.²⁴⁰ Several commenters supported the proposal, noting that these funds cannot engage in repurchase agreements and the supply of tax-exempt securities with daily demand features is extremely limited.²⁴¹ One commenter, however, argued that tax-exempt funds are subject to daily redemptions and should be subject to the required minimum.²⁴² Based on the comments we received, we continue to believe that the different nature of the markets for tax-exempt securities justifies exempting tax-exempt money

Treasury Department adopted the Guarantee Program, because we have no basis to estimate what the redemptions would have been had the Treasury not adopted the Program. We also note that another commenter that provided specific information on redemption flows, a large sponsor of money market funds, reported in its comment letter that on September 17, redemptions in its money market funds exceeded 5% and during the week of September 15, redemptions in the funds exceeded 20%. Federated Comment Letter.

²³⁸ See Proposing Release, *supra* note 2, at n.201 and accompanying text. The 9% of institutional money market funds that had redemptions exceeding 30% of assets in the week after the Reserve Fund broke the buck accounted for 10.9% of all institutional funds' total assets as of September 15, 2008. We estimate that under the minimum liquidity standards we are adopting more retail funds would have been able to satisfy the level of redemption demands than would have institutional funds. During the week ending September 19, 2008, 3% of retail funds experienced outflows greater than 30%. This is based on analysis of data from the iMoneyNet Money Fund Analyzer Database.

²³⁹ See *supra* Section II.C.2 (limitations on illiquid securities).

²⁴⁰ See Proposing Release, *supra* note 2, at nn.198–99 and accompanying text.

²⁴¹ See, e.g., Federated Comment Letter; ICI Comment Letter.

²⁴² See Fidelity Comment Letter.

market funds from the daily liquidity requirements.²⁴³

Definition of Daily and Weekly Liquid Assets. As discussed above, the new daily and weekly liquidity requirements are designed to ensure that a money market fund has the legal right to receive cash within one or five business days so that a fund may more easily satisfy redemption requests during times of market stress.²⁴⁴ Like our proposal, the final definition of "daily liquid assets" includes cash (including demand deposits), Treasury securities, and securities (including repurchase agreements) for which a money market fund has a legal right to receive cash in one business day.²⁴⁵ Our proposed definition of "weekly liquid assets" included the same assets (except that the fund would have had to have the right to receive cash in five business days rather than one).²⁴⁶ We proposed to include Treasury securities regardless of their maturity in the liquidity baskets because they have been the most liquid assets during times of market stress.²⁴⁷ Indeed, we understand that the "flight to liquidity" that happens during times of uncertainty makes it easy to sell Treasury securities in even large quantities.²⁴⁸

Commenters supported our inclusion of Treasury securities, but many argued that we should include additional securities.²⁴⁹ In particular, a number of

²⁴³ We understand that most of the portfolios consist of longer term floating and variable-rate securities with seven-day demand features from which the fund obtains much of its liquidity, and that they are unlikely to have investment alternatives that would permit them to meet a daily liquidity requirement. See Proposing Release, *supra* note 2, at n.199 and accompanying text.

²⁴⁴ See *supra* note 213 and accompanying and following text.

²⁴⁵ Amended rule 2a–7(a)(8) (defining "daily liquid asset" to mean (i) cash; (ii) direct obligations of the U.S. Government; and (iii) securities that will mature or are subject to a demand feature that is exercisable and payable within one business day).

²⁴⁶ Proposed rule 2a–7(a)(32).

²⁴⁷ U.S. Treasury securities were highly liquid during the market turmoil in 2008. See, e.g., *FRB Open Market Committee Oct. 28–29 Minutes*, *supra* note 13, at 5; *Minutes of the Federal Open Market Committee*, Federal Reserve Board, Dec. 15–16, 2008, at 4, available at <http://www.federalreserve.gov/monetarypolicy/files/fomcminutes20081216.pdf>.

²⁴⁸ See, e.g., Francis A. Longstaff, *The Flight-to-Liquidity Premium in U.S. Treasury Bond Prices*, 77 J. Bus. 511 (July 2004).

²⁴⁹ See, e.g., Comment Letter of the Federal Home Loan Banks (Sept. 8, 2009) ("FHLB Comment Letter") (include Federal Home Loan Bank discount notes); RidgeWorth Comment Letter (include fixed-rate agency discount notes with maturities of 95 days or less); Victory Cap. Mgmt. Comment Letter (include fixed-rate agency discount notes with maturities of 397 days or less). See also Dreyfus Comment Letter (include bank time deposits); Fidelity Comment Letter (include shares of other money market funds). Both shares of money market funds and bank time deposits, which some

commenters argued that we should also include agency notes (*i.e.*, direct obligations of Federal government agencies and government-sponsored enterprises) as daily or weekly liquid assets or in both liquid asset baskets.²⁵⁰ We are persuaded, based on the comments we received, that the market for very short-term agency notes is likely to be sufficiently liquid under stressful market conditions to treat them as weekly liquid assets. Therefore, amended rule 2a-7 includes agency discount notes with remaining maturities of 60 days or less in the definition of weekly liquid assets.²⁵¹

Our decision to include these securities is based on our consideration of the relative liquidity of agency discount notes during times of extreme market stress.²⁵² We compared average daily yields for the two weeks before and the two weeks after the Lehman Brothers bankruptcy on September 15, 2008. Between these periods, the yields for 30-day Treasury bills fell 75 percent while yields for 30-day and 60-day agency discount notes remained essentially the same.²⁵³ The yields for

commenters advocated we specifically include in the rule text, fall within the definitions of daily and weekly liquid assets if they satisfy the applicable maturity terms.

²⁵⁰ See, e.g., Comment Letter of the Capital Management of the Carolinas (Sept. 4, 2009) ("Cap. Mgt. Carolinas Comment Letter") (include discount notes with maturity of 397 days or less as daily liquid assets); Fidelity Comment Letter (include discount notes with maturity of 397 days or less as both daily and weekly liquid assets); ICI Comment Letter (include fixed-rate agency discount notes with maturity of 397 days or less as weekly liquid assets); C. Wesselkamper Comment Letter (include in daily and weekly liquid assets Government securities with fixed rates or fixed rate Government securities maturing in no more than 60 days). One commenter also expressed concern about the supply of assets that would qualify as daily or weekly liquid assets. See Fidelity Comment Letter.

²⁵¹ Amended rule 2a-7(a)(32) (defining "weekly liquid assets" to mean (i) cash; (ii) direct obligations of the U.S. Government; (iii) Government securities 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 are issued at a discount to the principal amount to be repaid at maturity and have a remaining maturity of 60 days or less; and (iv) securities that will mature or are subject to a demand feature that is exercisable and payable within five business days).

²⁵² Commenters who advocated including agency discount notes in the liquid asset baskets stressed the depth of liquidity in the secondary markets for these securities. See, e.g., Charles Schwab Comment Letter; ICI Comment Letter; SIFMA Comment Letter; FHLB Comment Letter (comment limited to Federal Home Loan Bank discount notes).

²⁵³ Between these periods, 30-day Treasury bill average daily yields fell from 1.53% to 0.39%; 30-day agency discount note average daily yields held constant at 2.14%; and 60-day agency discount note average daily yields increased from 2.25% to 2.27%. See Bloomberg Terminal Database, US 30-Day T-Bill USGB030Y (Index); Agency Discount Note 30 Day Yield AGDN030Y (Index); Agency Discount Note 60 Day Yield AGDN060Y (Index).

other money market assets increased over the same periods. For example, the average daily yield for 90-day agency discount notes increased four percent; while the yield for 30-day first tier financial securities increased 23 percent.²⁵⁴ Transaction volume in agency discount notes increased over this time period,²⁵⁵ which suggests to us that money market funds were able to sell their shorter maturity agency discount notes at amortized cost or higher prices.

4. Stress Testing

We are adopting amendments to rule 2a-7 to require the board of directors of each money market fund to adopt procedures providing for periodic stress testing of the money market fund's portfolio.²⁵⁶ Almost all of the commenters who addressed this matter supported requiring stress testing of fund portfolios,²⁵⁷ although several suggested changes from our proposal.²⁵⁸

Under the amended rule, a fund must adopt procedures that provide for the periodic testing of the fund's ability to maintain a stable net asset value per share based upon certain hypothetical

We note that in September 2008, the Federal Reserve's Open Market Trading Desk purchased discount notes issued by Fannie Mae, Freddie Mac, and the Federal Home Loan Banks in order to support market functioning. See Press Release, Federal Reserve Bank of New York, Statement Regarding Planned Purchases of Agency Debt (Sept. 19, 2008), available at http://www.newyorkfed.org/markets/operating_policy_080919.html. Data concerning the purchases are available at the Federal Reserve Bank of New York's Permanent Open Market Operations Historical Search webpage, available at <http://www.newyorkfed.org/markets/pomo/display/index.cfm?fuseaction=showSearchForm>.

²⁵⁴ Average daily yields on 90-day agency discount notes increased from 2.35% to 2.45%. See Bloomberg, Agency Discount Note 90 Day Yield AGDN090Y (Index). In addition, average daily yields on 30-day first tier financial securities increased from 2.40% to 2.96% and average daily yields on 30-day first tier non-financial securities increased from 2.03% to 2.16%. See Federal Reserve Commercial Paper Data, *supra* note 47 (select rates from the preformatted data package menu and follow the instructions to reformat the date range and download). Average daily yields on 60-day first tier financial securities increased from 2.57% to 2.99% and average daily yields on 60-day first tier non-financial securities increased from 2.03% to 2.19%. See *id.*

²⁵⁵ See Federal Reserve Bank of New York, Primary Dealer Statistics, available at <http://www.newyorkfed.org/markets/gds/search.cfm>.

²⁵⁶ See amended rule 2a-7(c)(10)(v).

²⁵⁷ See, e.g., J.P. Morgan Asset Mgt. Comment Letter; Tamarack Funds Comment Letter. *But see* C. Wesselkamper Comment Letter (stress testing should be an adviser's best practice).

²⁵⁸ At the suggestions of some commenters, we have made the stress testing requirement applicable to all money market funds that employ either the amortized cost method of valuing portfolio securities or the penny-rounding method of pricing fund shares. See Federated Comment Letter; TDAM Comment Letter. We believe that few, if any, money market funds will be affected by this change.

events. These include 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.²⁵⁹ Commenters differed on whether we should specify details for stress testing in addition to these hypothetical events.²⁶⁰ Because different tests may be appropriate for different market conditions and different money market funds, we believe that the funds are better positioned to design and modify their stress testing systems and have not included more specific criteria in the rule.²⁶¹

The amendment requires the testing to be done at such intervals as the fund board of directors determines appropriate and reasonable in light of current market conditions.²⁶² This is the same approach that rule 2a-7 takes with respect to the frequency of shadow pricing.²⁶³ The rule does not, however, specifically require the board to design the portfolio stress testing, as may have been suggested by our proposing

²⁵⁹ Amended rule 2a-7(c)(10)(v)(A).

²⁶⁰ See, e.g., Charles Schwab Comment Letter (opposing more specific tests in the rule); State Street Comment Letter (same); RidgeWorth Comment Letter (requesting that the Commission more clearly define feasible stress testing requirements); TDAM Comment Letter (same).

²⁶¹ See Federated Comment Letter (different types of money market funds should have different stress testing procedures); Invesco Aim Comment Letter ("each investment adviser should have the discretion to determine the appropriate assumptions and hypothetical events for which to test."). As discussed above, amended rule 2a-7's new liquidity requirements require money market funds to evaluate their liquidity needs based on their shareholder base. See *supra* note 195 and preceding and accompanying text. Money market funds should also incorporate this element in their stress testing procedures as appropriate. See Thrivent Comment Letter.

²⁶² Amended rule 2a-7(c)(10)(v)(A). Commenters differed in their views on the appropriate intervals for testing. See, e.g., J.P. Morgan Asset Mgt. Comment Letter (monthly or even more frequently); HighMark Comment Letter (quarterly under normal market conditions); Shriver Poverty Law Ctr. Comment Letter (same). We believe that a fund's board of directors is best positioned to choose the appropriate frequency under different conditions. We urge funds to adopt thresholds for testing frequency based, in part, on the amount of the deviation of the funds market-based net asset value per share from its amortized cost value per share similar to many funds' thresholds for more frequent shadow pricing. Thus, we would expect that if a fund's shadow net asset value per share decreased to less than \$0.9975, the fund would conduct stress tests at least every week, even if the fund stress tests less frequently under normal conditions. More frequent testing would likely allow the fund to better understand and manage the risks to which the fund and its shareholders are exposed.

²⁶³ Amended rule 2a-7(c)(8)(ii)(A)(1).

release.²⁶⁴ We agree with the many commenters that asserted that the board may not have sufficient expertise to construct appropriate stress tests for a fund.²⁶⁵ Each board may, of course, consider the extent to which it wishes to become involved in design of the stress tests.

The rule also requires that the board receive a report of the results of the stress testing at its next regularly scheduled meeting, as proposed, and more frequently, if appropriate, in light of the results.²⁶⁶ We have added the requirement for more frequent reporting in light of results because we believe that the board should be apprised of test results when they indicate that the magnitude of hypothetical events required to cause the fund to break a buck (such as changes in interest rates or shareholder redemptions or a combination of factors) is slight when compared with actual conditions.

As proposed, the report must include: (i) The date(s) on which the fund portfolio was tested; and (ii) the magnitude of each hypothetical event that would cause the money market fund to break the buck.²⁶⁷ The report also must include 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.²⁶⁸ Finally, as proposed,

²⁶⁴ See Proposing Release, *supra* note 2, at text following n.209.

²⁶⁵ See, e.g., ABA Comment Letter; HighMark Capital Comment Letter; IDC Comment Letter.

²⁶⁶ Amended rule 2a-7(c)(10)(v)(B). We disagree with commenters that recommended that the adviser report to the board only annually and on an exception basis. See, e.g., Stradley Ronon Comment Letter; Tamarack Funds Comment Letter; T. Rowe Price Comment Letter. We believe that regular reports will allow the board more effectively to monitor the fund's ability to withstand hypothetical events that alone or in combination would cause the fund to break the buck. In the Proposing Release, we asked whether we should impose minimum liquidity requirements based on the results of a particular stress test. See Proposing Release, *supra* note 2, at text following n.216. Commenters were divided on this issue. See Fidelity Comment Letter (against); Bankers Trust Comment Letter (in favor); Shriver Poverty Law Ctr. (same). As discussed above, we expect that money market funds take into consideration the results of their stress testing in assessing their liquidity needs under the general liquidity requirement of rule 2a-7(c)(5). See *supra* note 261.

²⁶⁷ Amended rule 2a-7(c)(10)(v)(B)(1).

²⁶⁸ Amended rule 2a-7(c)(10)(v)(B)(2). We do not agree with commenters who argued that advisers should not be required to provide an assessment of a fund's ability to withstand events that are reasonably likely to occur within the following year. See Charles Schwab Comment Letter; Federated Comment Letter; Stradley Ronon Comment Letter; Vanguard Comment Letter. The rule does not require advisers to predict the future in order to determine which hypothetical events to use in stress testing (and we recognize that advisers will not always be correct in their assessments of

funds are required to maintain records of the stress testing for six years, the first two years in an easily accessible place.²⁶⁹

D. Repurchase Agreements

Money market funds typically invest a significant portion of their assets in repurchase agreements, many of which mature the following day and provide an immediate source of liquidity. We are adopting, as proposed, two amendments to rule 2a-7 that affect fund investments in repurchase agreements for purposes of rule 2a-7's diversification provisions.²⁷⁰

First, we are limiting money market funds to investing in repurchase agreements collateralized by cash items or Government securities in order to obtain special treatment of those investments under the diversification provisions of rule 2a-7.²⁷¹ This change is designed to reduce the risk that a money market fund would experience losses upon the sale of collateral in the event of a counterparty's default.²⁷² Most commenters who addressed our proposal supported it.²⁷³ Commenters

which events are reasonably likely to occur within the following year). Instead, the provision is designed to provide to the board some context within which to evaluate the assessment on the magnitude of each hypothetical event that would cause the fund to break the buck. See Proposing Release, *supra* note 2, at text following n.211.

²⁶⁹ Amended rule 2a-7(c)(11)(vii).

²⁷⁰ Amended rule 2a-7(c)(4)(ii)(A); Proposing Release, *supra* note 2, at Section II.E.

²⁷¹ Amended rule 2a-7(a)(5) (defining the term "collateralized fully"). The special treatment allows money market funds to consider the acquisition of the repurchase agreement as an acquisition of the underlying collateral for diversification purposes. See Proposing Release, *supra* note 2, at n.228 and accompanying text. Under the new rule, securities with the highest rating, or unrated securities of comparable credit quality, will no longer be acceptable collateral. Compare amended rule 2a-7(a)(5) with current rule 2a-7(a)(5).

²⁷² See Proposing Release, *supra* note 2, at n.229 and accompanying text.

²⁷³ See Bankers Trust Comment Letter; BlackRock Comment Letter; HighMark Capital Comment Letter; RidgeWorth Comment Letter. Two commenters opposed the proposal. Wells Fargo made a number of arguments based on the premise that the change will prevent money market funds from investing in repurchase agreements collateralized by non-government securities. The rule, however, does not restrict funds from investing in repurchase agreements. Instead, it limits the circumstances under which a fund may look through the repurchase agreement to the underlying collateral for diversification purposes. A money market fund will continue to be able to invest in repurchase agreements collateralized by other types of assets, although the securities will not be eligible for special treatment under the diversification provisions. Another commenter asserted that the limitation is unnecessary if a fund evaluates the creditworthiness of the counterparty or if it adequately values the collateral in light of rule 2a-7(c)'s minimal credit risk determination. See Am. Securit. Forum Comment Letter. As discussed above and in the Proposing Release, we are adopting this provision to protect against

also confirmed our understanding that many managers of money market funds already look through only those repurchase agreements that are collateralized by Government securities or cash instruments.²⁷⁴

Second, we are reinstating the requirement that the money market fund's board of directors or its delegate evaluate the creditworthiness of the repurchase agreement's counterparty in order for the fund to take advantage of the special look-through treatment under rule 2a-7's diversification provisions.²⁷⁵ The effect of this amendment is to require a fund adviser to determine that the counterparty is a creditworthy institution, separate and apart from the value of the collateral supporting the counterparty's obligation under the repurchase agreement.²⁷⁶

We are not adopting an approach suggested by some of the commenters that the evaluation of a repurchase agreement should be limited to the credit risk determination already required by rule 2a-7(c)(3) with regard to the purchase of any security.²⁷⁷ That

circumstances in which the fund may be unable to obtain its collateral or the full value of that collateral.

²⁷⁴ See Federated Comment Letter (Federated has never relied on the diversification look-through approach for repurchase agreements collateralized by non-government securities); ICI Comment Letter (ICI members typically adopt the look-through approach only for repurchase agreements collateralized by cash items and government securities). See also *Fitch Ratings, Money Market Funds Special Report, U.S. Prime Money Market Funds: Managing Portfolio Composition to Address Credit and Liquidity Risks* (Aug. 14, 2009) ("Fitch Report"), at 6 available at http://www.fitchratings.com/creditedesk/reports/report_frame.cfm?rpt_id=462366 (reporting that after the end of 2008 "a number of advisors to Fitch-rated U.S. prime money market funds * * * significantly amended their investment policies with respect to repurchase agreements counterparties and collateral schedules"; the amendments include, among others, "[r]educed acceptance of repurchase agreement collateral other than U.S. Treasury and agency securities").

²⁷⁵ See amended rule 2a-7(c)(4)(ii)(A). We eliminated the requirement in 2001. See Proposing Release, *supra* note 2, at nn.230-33 and accompanying text. Three commenters specifically supported the change. See BlackRock Comment Letter; HighMark Capital Comment Letter; Shriver Poverty Law Ctr. Comment Letter.

²⁷⁶ A number of commenters argued that the evaluation should not be the board's responsibility. See, e.g., IDC Comment Letter; Comment Letter of the North Carolina Capital Management Trust—Independent Trustees (Sept. 8, 2009). We note that rule 2a-7(e) allows a board to delegate the creditworthiness evaluation to the fund's investment adviser or officers, under guidelines and procedures that the board establishes and reviews.

²⁷⁷ Three commenters argued that the proposed creditworthiness evaluation is unnecessary because it is already an element of the minimal credit risk determination that a fund makes pursuant to rule 2a-7(c)(3). See Federated Comment Letter; ICI Comment Letter; IDC Comment Letter. Two other commenters recommended that the applicable standard be the minimal credit risk evaluation. See

approach would not require a fund to evaluate separately the creditworthiness of the counterparty in order to take advantage of the special look-through treatment for diversification purposes. Under that approach, the fund's evaluation of a repurchase agreement could be based primarily or exclusively on the quality of the *collateral*. As we explained in the Proposing Release, in the midst of a market disruption caused by the default of a *counterparty*, a money market fund may find it difficult to protect fully its collateral without incurring losses.²⁷⁸ The amendment is designed to avoid such losses by requiring money market funds to evaluate the creditworthiness of the counterparty in order to limit exposure to less creditworthy institutions.

E. Disclosure of Portfolio Information

1. Public Web Site Posting

We are amending rule 2a-7 to require money market funds to disclose information about their portfolio holdings each month on their Web sites. The disclosure will provide greater transparency of portfolio information in a manner convenient for most investors. The amendment is designed to give investors a better understanding of the current risks to which the fund is exposed, strengthening their ability to exert influence on risk-taking by fund advisers.

Commenters generally supported requiring money market funds to post portfolio information monthly, although several urged us to revise the amendments in certain ways.²⁷⁹ The amendments we are today adopting are substantially similar to those we proposed, with modifications to (i) The information required to be disclosed, (ii) the time within which a fund must post its portfolio holdings information, and (iii) the length of time a fund must maintain the information on its Web site. We discuss each of these modifications below.

Information Required to be Disclosed. As proposed, the amendments to rule 2a-7 would have required a fund to disclose the fund's schedule of investments, as prescribed by rules 12-12 through 12-14 of Regulation S-X,²⁸⁰ identifying, among other things, the issuer, the title of the issue, the principal amount, the interest rate, the

Fidelity Comment Letter; Stradley Ronon Comment Letter.

²⁷⁸ Proposing Release, *supra* note 2, at n.233 and accompanying text.

²⁷⁹ See, e.g., Assoc. for Fin. Professionals Comment Letter; SIFMA Comment Letter; Vanguard Comment Letter.

²⁸⁰ 17 CFR 210.12-12-12-14.

maturity date, and the current amortized cost of the security.²⁸¹ Several commenters asserted that requiring the information specified in rules 12-12 through 12-14 of Regulation S-X would include information that would not be helpful to investors. They urged us instead to require information about money market fund portfolios that would better fit the needs of investors seeking information relevant to their investment decisions.²⁸² For example, some commenters noted that under the proposed amendments a fund would be required to classify and subtotal securities by industry, provide detailed restricted securities disclosures, and provide detailed information regarding repurchase agreement counterparties and collateral. One also noted that under the proposal funds may be required to provide certain notes required by generally accepted accounting principles ("GAAP"), as many funds do for filings on Form N-Q.²⁸³ Commenters asserted that these requirements would unnecessarily complicate the disclosure, be of little interest or benefit to investors, be difficult to comply with, and would impose a significant additional burden on money market funds. They suggested modifying the disclosure requirements to exclude some of the detail.²⁸⁴

We are revising the information about portfolio holdings that funds must disclose on their Web sites. Instead of referring to Regulation S-X as we proposed, we are listing in rule 2a-7(c)(12) the information that funds must disclose.²⁸⁵ These revisions more

²⁸¹ Proposed rule 2a-7(c)(12). As discussed below, all of these enumerated items are required under amended rule 2a-7(c)(12).

²⁸² See, e.g., BlackRock Comment Letter; GE Asset Mgt. Comment Letter; Invesco Aim Comment Letter.

²⁸³ See ICI Comment Letter.

²⁸⁴ See, e.g., BlackRock Comment Letter; Fidelity Comment Letter; ICI Comment Letter.

²⁸⁵ Rules 12-12 through 12-14 of Regulation S-X require, and the proposed rule amendments would have required, in addition to the information required by rule 2a-7(c)(12), the following information, which we believe is not critical to be made available to investors on money market fund Web sites: (i) The subtotals for each category of investments, subdivided by business grouping or investment type, with their percentage value compared to net assets; (ii) for repurchase agreements, showing for each, among other things, the date of the agreement, the total amount to be received upon repurchase, the repurchase date, and a description of the securities that are subject to the repurchase agreement; (iii) for restricted securities (1) as to each such issue (a) The acquisition date, (b) the carrying value per unit of investment at date of related balance sheet, and (c) the cost of such securities, (2) as to each issue acquired during the year preceding the date of the related balance sheet, the carrying value per unit of investment of unrestricted securities of the same issuer at (a) The day the purchase price was agreed to, (b) the day on which an enforceable right to acquire such securities was obtained, and (c) the aggregate value

closely tailor the required information to the needs of money market fund investors and others who seek information about fund holdings through Internet Web sites. For example, rule 12-12 of Regulation S-X requires funds to disclose the *subtotal* of each category of investments, *subdivided* by business grouping or investment type. We agree with commenters who argued that this level of detail, although appropriate for financial statements, is unnecessary in a fund's Web site disclosures to investors.²⁸⁶ For investors who may prefer to obtain the more detailed information, it will continue to be available in money market funds' quarterly Form N-CSR and Form N-Q filings.²⁸⁷ As discussed below, detailed information also will be available on a fund's filings on Form N-MFP.²⁸⁸

As amended, rule 2a-7(c)(12) will require funds to disclose monthly with respect to each security held: (i) The name of the issuer; (ii) the category of investment (e.g., Treasury debt, government agency debt, asset backed commercial paper, structured investment vehicle note); (iii) the CUSIP number (if any); (iv) the principal amount; (v) the maturity date as determined under rule 2a-7 for purposes of calculating weighted average maturity; (vi) the final maturity date, if different from the maturity date previously described; (vii) coupon or yield; and (viii) the amortized cost value.²⁸⁹ In addition, the amendments require funds to disclose their overall weighted average maturity and weighted

of all restricted securities and the percentage which the aggregate value bears to net assets; (iv) the aggregate gross unrealized appreciation for all securities in which there is an excess of value over tax cost; (v) the aggregate gross unrealized depreciation for all securities in which there is an excess of tax cost over value; (vi) the net unrealized appreciation or depreciation; (vii) the aggregate cost of securities for Federal income tax purposes; (viii) disclosure of investments in non-securities; (ix) the amount of equity in net profit and loss for the period; and (x) the dollar amount of dividends or interest in investments in affiliates.

²⁸⁶ See *supra* note 282.

²⁸⁷ Money market funds must provide a full schedule of their portfolio holdings in quarterly filings to the Commission, within 60 days after the end of the quarter. See Form N-CSR [17 CFR 274.128] (form used by registered management investment companies to file shareholder reports); Form N-Q [17 CFR 274.130] (form used by registered management investment companies to file quarterly reports of portfolio holdings after the first and third quarters).

²⁸⁸ See *infra* Section I.E.2.

²⁸⁹ Amended rule 2a-7(c)(12)(ii). We have added disclosure of the security's CUSIP number as an item of the web disclosure, which is designed to help users identify the securities in the fund's portfolio. We proposed and are adopting CUSIP number reporting on Form N-MFP, and commenters did not object to this reporting. See *infra* note 306 and accompanying text.

average life maturity of their portfolios.²⁹⁰ The information required is substantially the same as was proposed but eliminates some of the details required by Regulation S-X, to which investors will continue to have access in the fund's quarterly filings.²⁹¹

Time of Posting Information on Web site. The amended rule requires funds to post the portfolio information, current as of the last business day of the previous month, no later than the fifth business day of the month.²⁹² Under the proposed amendments, a fund would have been required to post the portfolio information on its Web site no later than the second business day of the month.²⁹³ We have extended the time in response to commenters that asserted that the second business day deadline would not provide funds with enough time to compile, review, and post the required portfolio information accurately.²⁹⁴

Maintenance of Information on the Web site. Portfolio information must be maintained on the fund's Web site for no less than six months after posting.²⁹⁵

²⁹⁰ Amended rule 2a-7(c)(12)(i). We proposed to require that funds disclose this information on Form N-MFP, which we indicated we intended to make public. Some commenters also recommended we include these disclosure items in funds' Web site disclosures. See Assoc. Fin. Professionals Comment Letter; BlackRock Comment Letter; Fidelity Comment Letter.

²⁹¹ As discussed above, the proposed amendments to rule 2a-7 would have required money market funds to disclose on their Web sites their monthly schedule of investments in accordance with rules 12-12 to 12-14 of Regulation S-X. To avoid unnecessarily duplicative disclosure obligations, we also proposed to amend rule 30b1-5 to exempt money market funds from Item 1 of Form N-Q, which similarly requires funds to disclose their schedule of investments in accordance with rules 12-12 to 12-14 of Regulation S-X in quarterly filings with the Commission. Because we have revised the Web site disclosure requirement not to include certain items in rules 12-12 to 12-14 of Regulation S-X, the disclosure requirements of rule 2a-7 and Item 1 of Form N-Q are no longer duplicative. As a result, we are not adopting the proposed amendments to rule 30b1-5.

²⁹² Amended rule 2a-7(c)(12).

²⁹³ Proposed rule 2a-7(c)(12).

²⁹⁴ See, e.g., BlackRock Comment Letter; Charles Schwab Comment Letter; T. Rowe Price Comment Letter; Vanguard Comment Letter. One commenter estimated that compliance with the proposed second business day deadline would cost \$1.5 million initially and \$220,000 annually. See Fidelity Comment Letter. The recommended deadlines submitted by commenters ranged from 5 business days to 15 or 30 business days after the end of each month. In light of the modifications we are making to the information that must be posted on the fund's Web site, as discussed above, we believe that lengthening the deadline to five business days should provide funds sufficient time to compile, review, and post the portfolio holding information accurately. We also note that a five business day deadline will typically mean seven calendar days and, when holidays intervene, eight calendar days.

²⁹⁵ Amended rule 2a-7(c)(12). The amended rule also requires funds to provide a link to a Securities

We have reduced the maintenance period from the proposed twelve months in response to commenters.²⁹⁶ Many commenters stated that the proposed twelve-month maintenance period was too long.²⁹⁷ Half of these commenters recommended a six-month period, asserting that historical portfolio holdings information could be obtained from publicly available semi-annual filings with the Commission.²⁹⁸ Other commenters recommended that no historical data be maintained on a fund's Web site at all.²⁹⁹ We believe that it is important for investors to be able to compare current holdings information with previous holdings information from which they (or others analyzing the data) may discern trends. However, because historical portfolio holdings information is available to investors in semi-annual filings to the Commission, we have determined to reduce the maintenance period to six months.³⁰⁰

2. Reporting to the Commission

We are adopting a new rule requiring money market funds to provide the Commission a monthly electronic filing of more detailed portfolio holdings information. The information will permit us to create a central database of money market fund portfolio holdings, which will enhance our oversight of money market funds and our ability to respond to market events.³⁰¹ As discussed further below, the information will also be made public on a delayed basis.

and Exchange Commission Web page where a user may obtain access to the fund's most recent 12 months of publicly available filings on Form N-MFP. Amended rule 2a-7(c)(12)(iii).

²⁹⁶ Proposed rule 2a-7(c)(12).

²⁹⁷ See Comment Letter of Clearwater Analytics, LLC (Sept. 7, 2009) ("Clearwater Comment Letter"); Comment Letter of Data Communiqué (Sept. 8, 2009) ("Data Communiqué Comment Letter"); Dreyfus Comment Letter; Fidelity Comment Letter; Fifth Third Comment Letter; GE Asset Mgt. Comment Letter; SIFMA Comment Letter; T. Rowe Price Comment Letter.

²⁹⁸ See Dreyfus Comment Letter; Fifth Third Comment Letter; SIFMA Comment Letter; T. Rowe Price Comment Letter.

²⁹⁹ See Clearwater Comment Letter; Data Communiqué Comment Letter (investors "only interested in the most recent data"); Fidelity Comment Letter; GE Asset Mgt. Comment Letter.

³⁰⁰ Two commenters stated that retaining portfolio holdings information on a fund's Web site for no more than six months would be consistent with the current requirements for portfolio holdings of open-end management investment companies. See Fifth Third Comment Letter; T. Rowe Price Comment Letter.

³⁰¹ As we explained in the Proposing Release, our current information on money market portfolio holdings is limited to quarterly reports filed with us which, due to the high turnover rate of portfolio securities, quickly become stale. See Proposing Release, *supra* note 2, at Section II.F.2.

New rule 30b1-7 requires money market funds to report portfolio information on new Form N-MFP. We received 49 comment letters on the proposed rule and form, most of which supported enhancing our oversight capabilities. Many of these commenters suggested technical modifications, a number of which we are adopting, as discussed below.³⁰² The rule and form that we are adopting today are substantially similar to what we proposed.³⁰³

Information. Money market funds must report on Form N-MFP, with respect to each portfolio security held on the last business day of the prior month, the following items:³⁰⁴ (i) The name of the issuer; (ii) the title of the issue, including the coupon or yield;³⁰⁵ (iii) the CUSIP number;³⁰⁶ (iv) the category of investment (e.g., Treasury debt, government agency debt, asset backed commercial paper, structured investment vehicle note, repurchase agreement³⁰⁷); (v) the NRSROs

³⁰² See, e.g., Charles Schwab Comment Letter; Stradley Ronon Comment Letter; Tamarack Funds Comment Letter.

³⁰³ In September 2009, we adopted interim final temporary rule 30b1-6T. Disclosure of Certain Money Market Fund Portfolio Holdings, Investment Company Act Release No. 28903 (Sept. 18, 2009) [74 FR 48376 (Sept. 23, 2009)] ("Rule 30b1-6T Release"). We therefore have adopted proposed rule 30b1-6 as rule 30b1-7. The portfolio securities information that money market funds currently must report each quarter (pursuant to rule 30b1-5) is less timely and more limited in scope, and includes information about the issuer, the title of the issue, the balance held at the close of the period, and the value of each item at the close of the period. See Item 1 of Form N-Q [17 CFR 274.130] and Item 6 of Form N-CSR [17 CFR 274.128] (requiring funds to include a schedule of investments as set forth in rule 12-12 through 12-14 of Regulation S-X [17 CFR 210.12-12—12-14]).

³⁰⁴ We have revised the form's general instructions to clarify that a filer may amend the form at any time. See Form N-MFP at General Instruction A.

³⁰⁵ We understand that the title of an issue typically includes the coupon or yield of the instrument, and we have revised Item 27 to require this information, if applicable.

³⁰⁶ Item 20 of proposed Form N-MFP would have required a fund to disclose the CIK of the issuer. Several commenters suggested that the form not require the issuer's CIK because the CIK is not a widely used identifier for money market instruments and is not generally maintained by money market funds. See, e.g., Dreyfus Comment Letter; Federated Comment Letter; SIFMA Comment Letter. Form N-MFP, as adopted, only requires the issuer's CIK number if the security does not have a CUSIP number and the issuer has a CIK. Item 28 and Item 30 of Form N-MFP. If the security does not have a CUSIP number, the fund must provide a unique identifier for the security if there is one. Item 29 of Form N-MFP.

³⁰⁷ For repurchase agreements we are also requiring funds to provide additional information regarding the underlying collateral. Item 32 of Form N-MFP. This information would have been required under our proposed amendments to rule 2a-7 regarding the Web site disclosure of portfolio holdings. Although we continue to believe that the

designated by the fund, the credit ratings given by each NRSRO, and whether each security is first tier, second tier, unrated, or no longer eligible; (vi) the maturity date as determined under rule 2a-7, taking into account the maturity shortening provisions of rule 2a-7(d); (vii) the final legal maturity date, taking into account any maturity date extensions that may be effected at the option of the issuer; (viii) whether the instrument has certain enhancement features;³⁰⁸ (ix) the principal amount; (x) the current amortized cost value;³⁰⁹ (xi) the percentage of the money market fund's assets invested in the security;³¹⁰ (xii) whether the security is an illiquid security (as defined in amended rule 2a-7(a)(19));³¹¹ and (xiii) "Explanatory

information is important to understanding the risks associated with a repurchase agreement and should be readily available to investors who seek it, we agree with commenters who asserted that that level of detail may not be necessary on the Web site disclosure. Fidelity Comment Letter ("detailed information regarding repurchase agreement counterparties and collateral" is contained across multiple systems); ICI Comment Letter. Accordingly, we have added the disclosure requirement to Form N-MFP.

³⁰⁸ At the suggestion of one commenter, we are incorporating defined terms from amended rule 2a-7 into Form N-MFP. See Federated Comment Letter. The form requires a fund to report: (i) Whether the instrument has a "demand feature" (as defined in amended rule 2a-7(a)(9)); (ii) the identity of the issuer of the demand feature; (iii) the designated NRSRO(s) for the demand feature or its provider; (iv) the credit rating provided by each designated NRSRO, if any; (v) whether the instrument has a "guarantee" (as defined in amended rule 2a-7(a)(17)); (vi) the identity of the guarantor; (vii) the designated NRSRO(s) for the guarantee or guarantor; (viii) the credit rating provided by each designated NRSRO, if any; (ix) whether the instrument has any other enhancements (*i.e.*, other than a demand feature or guarantee); (x) the type of enhancement; (xi) the identity of the enhancement provider; (xii) the designated NRSRO(s) for the enhancement or enhancement provider; and (xiii) the credit rating provided by each designated NRSRO, if any. See Items 37-39 of Form N-MFP.

³⁰⁹ Under Item 37 of proposed Form N-MFP, a fund would have had to provide the amortized cost of a security to the nearest hundredth of a cent. Commenters pointed out that fund accounting systems carry costs of securities in whole cents, and recommended that funds therefore be required to report the amortized cost to the nearest cent. See, *e.g.*, Dreyfus Comment Letter; ICI Comment Letter; State Street Comment Letter. We therefore have revised the form to require the amortized cost of each portfolio security to the nearest cent. Item 41 of Form N-MFP.

³¹⁰ Under Item 39 of proposed Form N-MFP, a fund would have had to disclose the percentage of gross assets invested in the security. We have revised the form to require that funds disclose the percentage of net assets invested in the security (Item 42 of Form N-MFP) to conform to existing disclosure requirements. See rule 12-12 of Regulation S-X.

³¹¹ See Item 44 of Form N-MFP. We have added this disclosure requirement at the suggestion of one commenter who believed that it would be useful for us to know if different funds have taken different positions regarding the liquidity of a commonly

notes."³¹² Form N-MFP also requires funds to report to us information about the fund,³¹³ including information about the fund's risk characteristics such as the dollar weighted average maturity of the fund's portfolio and its seven-day gross yield.³¹⁴

held security. See Federated Comment Letter. Conversely, we are not adopting proposed Item 38, which would have required funds to disclose whether the inputs used in determining the value of the securities are Level 1, Level 2, or Level 3, if applicable. See Financial Accounting Standards Board, *Statement of Financial Accounting Standards No. 157, "Fair Value Measurement,"* available at <http://www.fasb.org/cs/BlobServer?blobcol=urldata&blobtable=MungoBlobs&blobkey=id&blobwhere=1175818754924&blobheader=application%2Fpdf>. Commenters explained that industry practice is to categorize all securities valued through reference to amortized cost as Level 2. See, *e.g.*, Dreyfus Comment Letter; ICI Comment Letter. We understand that industry practice is to determine the value of an illiquid security using Level 3 inputs. Requiring funds to disclose whether a security is illiquid will provide comparable information regarding the classification of the security.

³¹² See Item 43 of Form N-MFP. This item permits funds to add miscellaneous information that may be material to other disclosure in the form.

³¹³ As proposed, many of the items would have been disclosed with regard to each *series* of the fund. As adopted, however, we are requiring that funds provide some of this information with regard to each *class* of the fund, where relevant (*e.g.*, minimum initial investment and flow activity). We believe that class-specific information about these items will be more useful for analysis. We also understand that funds typically maintain this information with regard to each class of the fund. For example, funds are required to disclose class-specific information about net assets and flow activities in financial statements. See Rules 6-04 and 6-09 of Regulation S-X. Therefore we do not believe that requiring certain information on a class basis will be any more burdensome than what we proposed. See also Clearwater Comment Letter (suggesting that total net asset value should be disclosed on a class-level basis).

³¹⁴ We also have revised or augmented some of the disclosure items of Form N-MFP. In addition to the seven-day gross yield, the form as adopted requires the fund's seven-day net yield for each class as calculated under Item 26(a)(1) of Form N-1A. Item 24 of Form N-MFP. Item 15 of proposed Form N-MFP would have required that a fund provide its net shareholder flow activity for the month ended. As adopted, Form N-MFP requires the net shareholder flow information for each class and also requires the fund to provide the gross subscriptions and redemptions for the month from which the net shareholder flow is calculated. Item 23 of Form N-MFP. Item 9 of proposed Form N-MFP would have required a fund to indicate if the fund was primarily used to invest cash collateral. One commenter stated that the term "cash collateral" is ambiguous (it could include corporate trust accounts and escrows as well as collateral for securities loans or over-the-counter derivatives) and that it would be difficult for a fund to know when it is being used "primarily" for these investments. See Federated Comment Letter. As adopted, Form N-MFP does not require this information. Items 12-14 of proposed Form N-MFP would have required certain assets and liabilities information to the nearest hundredth of a cent. We have slightly revised these items to conform to accounting conventions and added an item for the net assets of the class. Items 13-16 and 21-22 of Form N-MFP. In addition, in response to commenters'

Money market funds also must report on Form N-MFP the market-based values of each portfolio security³¹⁵ and the fund's market-based net asset value per share, with separate entries for values that do and do not take into account any capital support agreements into which the fund may have entered.³¹⁶ When we proposed Form N-MFP, we solicited comment on requiring funds to report market-based values, including the value of any capital support agreement, on the form.³¹⁷ Two commenters supported requiring money market funds to report market-based values to the Commission.³¹⁸ Other commenters objected to the *public disclosure* of market-based values.³¹⁹ We have decided to require market-based information in the monthly reports, because it will assist us in our understanding of fund portfolio valuation practices as well as the potential risks associated with a fund, *e.g.*, a fund that has a market-based net asset value that suggests that it may be at risk of breaking the buck. The information regarding capital support agreements will help show the extent to which the funds' valuations depend on external support agreements.

Public availability. Under rule 30b1-7, the information contained in the portfolio reports that money market funds file with the Commission on Form N-MFP will be available to the public 60 days after the end of the month to which the information pertains.³²⁰ Although the portfolio information and other information reported to the Commission on Form N-MFP is not

assertion that fund accounting systems only carry costs in whole cents, Form N-MFP as adopted requires this information to the nearest cent. *Id.*

³¹⁵ See Items 45-46 of Form N-MFP. It should be noted that Form N-MFP requires the total market-based value of each portfolio security, not the per-unit price of the security.

³¹⁶ See Item 18 (shadow NAV of the series) and Item 25 of Form N-MFP (shadow NAV of each class).

³¹⁷ See Proposing Release, *supra* note 2, at paragraph accompanying n.253.

³¹⁸ See Fund Democracy/CFA Comment Letter ("We strongly support the SEC's proposal to require that additional information be filed with the Commission on a temporarily confidential basis. It is critical that the Commission be able to gauge the stability of the MMF industry on an ongoing basis. * * * We believe strongly that the values at which MMFs are carrying portfolio securities is the most important piece of information for monitoring potential liquidity problems."); Tamarack Funds Comment Letter.

³¹⁹ See, *e.g.*, ABA Comment Letter; Dreyfus Comment Letter; Goldman Sachs Comment Letter; Tamarack Funds Comment Letter.

³²⁰ Rule 30b1-7(b). As discussed above, money market fund portfolio information will be required to be posted on fund Web sites within five business days after the end of the month. See *supra* notes 292-294 and accompanying text.

primarily designed for individual investors, we anticipate that many investors, as well as academic researchers, financial analysts, and economic research firms, will use this information to study money market fund holdings and evaluate their risk. Their analyses may help other investors and regulators better understand risks in money market fund portfolios.³²¹ Therefore we believe that it is important to make this information publicly available.

In the Proposing Release, we stated that we expected to make the information filed on Form N-MFP available to the public on a delayed basis, and we also requested comment on whether the rule should require funds to report, and therefore disclose to the public, the market-based valuations of the portfolio securities and of the net asset value of the fund.³²² As discussed further below, commenters' objections to public availability of the information collected on Form N-MFP generally fell into two categories—the competitive effects of portfolio information and the potentially de-stabilizing effects of market-based value information. We address each objection in turn.

First, some commenters objected to the disclosure of information filed on Form N-MFP because of its competitive effects on funds or fund managers. Three commenters argued that the information to be provided on the form is proprietary, sensitive, or confidential in nature.³²³ Others expressed concern that making the information public could result in “investor confusion.”³²⁴ Two other commenters, however, supported making Form N-MFP information available to the public on a delayed basis.³²⁵ One of them emphasized the positive effect that public disclosure can have on portfolio management practices.³²⁶

³²¹ See Proposing Release, *supra* note 2, at paragraph accompanying n.245. See also Clearwater Comment Letter (“[R]egular disclosure will also allow third-party analytics and reporting providers to make meaningful comparisons of money funds and highlight certain characteristics that are of interest to investors and the market generally.”).

³²² We stated that we intended to make Form N-MFP information public two weeks after the filing of the form. See Proposing Release, *supra* note 2, at paragraph accompanying n.245.

³²³ See BlackRock Comment Letter; Federated Comment Letter; T. Rowe Price Comment Letter.

³²⁴ See, e.g., Fidelity Comment Letter; GE Asset Mgt. Comment Letter; Vanguard Comment Letter. Some commenters stated that the monthly fund Web site postings would provide sufficient transparency for investors. See, e.g., Fifth Third Comment Letter; ICI Comment Letter; Vanguard Comment Letter.

³²⁵ See Fund Democracy/CFA Comment Letter; Comment Letter of J.P. Morgan Investor Services Co. (Sept. 4, 2009).

³²⁶ See Fund Democracy/CFA Comment Letter.

We believe commenters overstated the *competitive* risks for money market funds of public access to the fund's information. As we discussed in the Proposing Release, the risks of trading ahead of funds are severely curtailed in the context of money market funds, because of the short-term nature of money market fund investments and the restricted universe of eligible portfolio securities.³²⁷ For similar reasons, we believe that the potential for “free riding” on a money market fund's investment strategies, *i.e.*, obtaining for free the benefits of fund research and investment strategies, is minimal. Because shares of money market funds are ordinarily purchased and redeemed at the stable price per share, we believe that there would be relatively few opportunities for profitable arbitrage by investors. Moreover, most funds currently disclose their *current* portfolios on their Web sites, and much of the information contained in Form N-MFP is already available through other publicly available filings with the Commission, albeit on a less frequent basis.³²⁸

Second, many commenters objected to the disclosure of the *market-based* values of portfolio securities and of fund net asset value per share, because of the possible destabilizing effects on money market funds. These commenters stated that disclosure of market-based values would result in investor confusion and alarm that could result in redemption requests that exacerbate pricing deviations.³²⁹ One commenter supported the disclosure of market-based net asset values, stating that the disclosure could provide discipline to managers operating their funds near the level of breaking the buck, and would level the informational playing field for

³²⁷ See Proposing Release, *supra* note 2, at n.379 and accompanying and following text; ICI Report, *supra* note 14, at 93 (“Because of the specific characteristics of money market funds and their holdings * * * the frontrunning concerns are far less significant for this type of fund. For example, money market funds' holdings are by definition very short-term in nature and therefore would not lend themselves to frontrunning by those who may want to profit by trading in a money market fund's particular holdings. Rule 2a-7 also restricts the universe of Eligible Securities to such an extent that frontrunning, to the extent it exists at all, tends to be immaterial to money market fund performance.”).

³²⁸ As noted above, money market funds must provide a full schedule of their portfolio holdings in quarterly filings to the Commission. See *supra* note 287.

³²⁹ See, e.g., ABA Comment Letter; T. Rowe Price Comment Letter; USAA Comment Letter (redemptions might lead to greater volatility in cash flows and increase the instability of the fund). In addition, one commenter stated that the investor confusion might result in additional costs for funds due to the need to answer investor inquiries. See Dreyfus Comment Letter.

less sophisticated investors.³³⁰ Another commenter supported only the public disclosure of market-based *portfolio securities* values.³³¹

We appreciate the risks that are involved with the real-time public disclosure of a fund's market-based portfolio and net asset values. Money market funds normally pay redeeming shareholders \$1.00 per share even if their market-based net asset value is less than \$1.00. These redemptions can hurt the fund's remaining shareholders because the realized and unrealized losses are spread across fewer shares, further depressing the fund's market-based net asset value. If enough shareholders redeem shares under these conditions, the fund, absent a capital contribution by its investment adviser or another person, can break the buck, causing remaining shareholders to receive less than \$1.00 per share. We believe that many institutional investors are currently well aware of this dynamic. If more shareholders understand the mechanical relationship between shareholder redemptions and market-based net asset value, the disclosure of a market-based net asset value below \$1.00 might precipitate a run on the fund. If one fund were to fail for this reason, runs might develop in other money market funds, even those with relatively high market-based net asset values.

Notwithstanding these risks, we believe that shareholders will benefit from knowing the monthly market-based net asset values of money market funds.³³² We anticipate that the public availability of these values will help investors make better informed decisions about whether to invest, or maintain their investments, in money market funds. This disclosure will indicate the extent to which the fund is managing its portfolio to achieve its fundamental objective of maintaining a stable net asset value. In addition, if market-based prices indicate significant risks in a fund's portfolio, investors, advisers and others can have a more meaningful dialogue with the fund's manager about such risks and any plans the fund manager may have to address any discounts between the market-based net asset value and the stable net asset value. This type of dialogue already

³³⁰ See Shadow FRC Comment Letter.

³³¹ See Clearwater Comment Letter.

³³² Adequate disclosure to investors is a fundamental principle of the Commission's regulatory mandate. See, e.g., section 1(b), 1(b)(1) of the Investment Company Act (“[N]ational public interest and the interests of investors are adversely affected * * * when investors purchase, pay for, exchange, * * * sell, or surrender securities issued by investment companies without adequate, accurate, and explicit information * * *.”).

takes place between sophisticated investors and funds that disclose portfolio information on a current basis. These sophisticated, often institutional, investors have the resources to estimate current market values and make purchase and redemption decisions on the basis of information that, in the past, has been beyond the reach of most retail investors.

As a collateral effect, we expect that the public disclosure of monthly market-based net asset values may have the effect of discouraging a fund's portfolio manager from taking risks that might reduce the fund's market-based net asset value.³³³ We also anticipate that such disclosure may lead to greater cash flows into funds that have a smaller discount from the \$1.00 NAV (or less historical volatility in that discount). This disclosure, which will provide values that include and exclude the effect of any capital support agreements, might also have the effect of encouraging funds that have affiliates to request financial support or other appropriate measures as soon as problems develop. Such support or other measures could provide greater stability to money market funds.

Nevertheless, we understand commenters' concerns that the disclosure of certain fund information, including market-based values, might result in investor confusion and alarm, at least in the short term, that could result in redemption requests that exacerbate pricing deviations.³³⁴ In response to these and other concerns discussed above, we are delaying the public availability of the information filed on Form N-MFP for 60 days after the end of the reporting period.³³⁵ This 60-day delay in public availability mirrors the current 60-day lag under other rules between the end of a fund's reporting period and the public filing of portfolio information with the Commission.³³⁶ In addition, funds currently are required to file twice a year a public report that includes the fund's market-based net asset value, within 60 days after the end of the reporting period.³³⁷

³³³ See Fund Democracy/CFA Comment Letter ("[G]reater transparency should provide a strong incentive for funds to avoid the excessively risky practices that lead to instability and encourage redemption.").

³³⁴ See *supra* note 329 and accompanying text.

³³⁵ Rule 30b1-7(b).

³³⁶ Funds are required to file each quarter with the Commission portfolio holdings reports, which are available to the public, within 60 days after the end of the quarter. See *supra* note 287.

³³⁷ Money market funds currently must disclose their mark-to-market net asset value per share, to four decimals, twice a year in their Form N-SAR filings [17 CFR 274.101]. See Sub-Item 74W of Form

We anticipate that, during the 60 days between the end of the reporting period and public availability of the information, funds will take steps to resolve issues that may raise concerns with investors and analysts. In addition, because money market fund portfolios have a limited maturity, many of the portfolio securities will have matured by the time the information is released to the public. Thus we expect that the 60-day delay will ameliorate many of the risks associated with public disclosure. We also expect that, over time, investors and analysts will become more accustomed to the information disclosed about fund portfolios, and thus there may be less need in the future to require a 60-day delay between the end of the reporting period and the public availability of the information. We therefore may revisit in a subsequent release whether to retain the same (or any) delay in public availability of this information.

Timing. Each money market fund must submit Form N-MFP electronically to the Commission within five business days after the end of each month.³³⁸ Under the proposed rule, a fund would have been required to file Form N-MFP with the Commission no later than two business days after the end of each month. Commenters asserted that the second business day deadline would not have provided funds enough time to compile, review, and file the requested portfolio information accurately.³³⁹

In response to commenters, we are delaying the mandatory filing date for several months after the effective date of the amendments, to permit money market funds to develop systems necessary to collect and submit the portfolio information on Form N-MFP.³⁴⁰ Thus, the first mandatory filing

N-SAR. Form N-SAR must be filed with the Commission no later than the 60th day after the end of the fiscal period for which the report is being prepared. See General Instruction C to Form N-SAR. Information supplied on Form N-SAR is publicly available on EDGAR and in the public files of the Commission. See General Instruction A to Form N-SAR.

³³⁸ See rule 30b1-7.

³³⁹ See, e.g., BlackRock Comment Letter; Dreyfus Comment Letter; Vanguard Comment Letter. The recommended deadlines submitted by commenters ranged from five business days to 15 to 30 business days. We are providing for an extended implementation period before compliance with rule 30b1-7 is required, as discussed below, during which time funds will be able to build or update systems to compile the data and file the new form, test those systems, and possibly participate in the voluntary compliance program. Therefore, we believe that lengthening the deadline to five business days should provide funds sufficient time to compile, review, and file Form N-MFP accurately.

³⁴⁰ Several commenters requested that the Commission allow funds at least six months before

will be due on December 7, 2010, for holdings as of the end of November 2010. For approximately two months before the first mandatory filing, our staff will accept the submission of trial data so that money market funds may voluntarily make (non-public) electronic submissions with us. We anticipate that these submissions will help money market funds gain experience collecting and submitting the information, and we will use these submissions and the experiences of the funds to make technical adjustments to our systems and provide any guidance. Because of the possibility of errors or mistakes in the information submitted, we do not intend to make the trial data public.

Method of filing. As proposed, Form N-MFP must be filed electronically through the Commission's EDGAR system in an eXtensible Markup Language ("XML") tagged data format.³⁴¹ We understand that money market funds already maintain most of the information that will be filed on the form, and therefore the main requirement for funds will be the tagging of the data and filing of the reports with the Commission.³⁴² Some commenters recommended that the Commission require that Form N-MFP be filed in an eXtensible Business Reporting Language ("XBRL") format.³⁴³ Although XBRL may allow for more comparative analysis or more opportunities for manipulation of data than XML allows, we believe that the data required by Form N-MFP will be clearly defined and often repetitive from one month to the next, and therefore the XML format will provide us with the necessary information in the most timely and cost-effective manner.³⁴⁴

mandatory compliance with the new reporting requirement on Form N-MFP. See, e.g., FAF Advisors Comment Letter; ICI Comment Letter; J.P. Morgan Asset Mgt. Comment Letter.

³⁴¹ We anticipate that the XML interactive data file will be compatible with a wide range of open source and proprietary information management software applications. Continued advances in interactive data software, search engines, and other Web-based tools may further enhance the accessibility and usability of the data.

³⁴² We understand that many funds often provide this type of information in different formats to various information services and third-parties, including NRSROs. Standardizing the data format in Form N-MFP may encourage standardization across the industry, resulting in cost savings for money market funds.

³⁴³ See, e.g., Comment Letter of the American Institute of Certified Public Accountants (Sept. 8, 2009); Comment Letter of EDGAR Online, Inc. (July 23, 2009); Comment Letter of XBRL US (Sept. 8, 2009). Most commenters were neutral on the submission format for Form N-MFP. See, e.g., Clearwater Comment Letter; Fund Democracy/CFA Comment Letter; ICI Comment Letter.

³⁴⁴ The XBRL format would require a longer period for implementation by the Commission and

Over time we expect these filings will become highly automated and involve minimal costs.

3. Phase-Out of Weekly Reporting by Certain Funds

We are adopting as final rule 30b1-6T, the temporary rule that requires the weekly filing of portfolio information by money market funds in certain circumstances. As adopted, the only change to the rule is the expiration date. Rule 30b1-6T will expire on December 1, 2010, which corresponds with the first filing of portfolio information required by new rule 30b1-7.

In September 2009, we adopted rule 30b1-6T.³⁴⁵ The rule requires any money market fund that has a market-based net asset value per share below \$0.9975 to provide the Commission with weekly portfolio and valuation information. The information required by the rule is similar to the information money market funds participating in the Treasury Department's Guarantee Program were required to provide under similar circumstances.³⁴⁶ We requested comments on the rule when we adopted it, but received none.³⁴⁷

Rule 30b1-6T originally would have expired one year after we adopted it, *i.e.*, on September 17, 2010.³⁴⁸ The information that rule 30b1-7, which we are adopting today, will require *all* money market funds to file on a monthly basis subsumes the information that funds with lower market-based NAVs were required to file under rule 30b1-6T. Therefore we are phasing out the latter rule, but are extending its expiration date so that we will continue to receive weekly reports until the monthly reporting requirements of rule 30b1-7 are mandatory. After that time, our monitoring of information filed by money market funds on Form N-MFP, as well as notifications of purchases of certain assets from funds in reliance on rule 17a-9 should enable our staff to

funds, and would entail additional costs. However, the XBRL format derives from and is compatible with the XML format. Moreover, to the extent possible, we intend to follow the naming convention for the XBRL-tagging of the Schedule of Investments in the voluntary filer program. See Interactive Data for Mutual Fund Risk/Return Summary, Investment Company Act Release No. 28617 (Feb. 11, 2009) [74 FR 7748 (Feb. 19, 2009)]. If the Commission determines at a future date to require the filing of Form N-MFP in an XBRL format, the Commission and funds might benefit from their experience with their existing XML technology.

³⁴⁵ See Rule 30b1-6T Release, *supra* note 303. We adopted the rule on an interim final basis. See *id.* at Section II.C.

³⁴⁶ See rule 30b1-6T(b)(3). See also *supra* note 16.

³⁴⁷ See Rule 30b1-6T Release, *supra* note 303, at Section III.

³⁴⁸ Rule 30b1-6T(d).

identify, and analyze information from, money market funds that exhibit signs of distress and the need for further monitoring.³⁴⁹

Because the compliance date for filing monthly portfolio information on Form N-MFP is December 7, 2010, we are amending rule 30b1-6T so that it expires on December 1, 2010. The last date that funds will be required to file information under rule 30b1-6T therefore will be on November 30, 2010.

F. Processing of Transactions

We are amending rule 2a-7, substantially as proposed, to require that a fund (or its transfer agent) have the capacity to redeem and sell its securities at a price based on the fund's current net asset value per share, including the capacity to sell and redeem shares at prices that do not correspond to the stable net asset value or price per share.³⁵⁰ This amendment will require that shareholder transactions be processed in an orderly manner, even under circumstances that require a fund to "break a dollar."³⁵¹ Other types of mutual funds already have this ability to process transactions at varying prices.

Several commenters supported the proposed amendment, noting that it is important that funds be able to redeem shareholders at prices based on the current net asset value of the fund.³⁵² Some commenters expressed concerns about the costs for funds to modify their systems under the amendment.³⁵³ We noted when we proposed the amendment that, because funds are already obligated to redeem at a price other than the stable net asset value per share, there should be no new cost associated with the requirement that funds (or their transfer agents) have systems that can meet these requirements.³⁵⁴ It is the responsibility

³⁴⁹ See *infra* Section II.G.2 (notification provision under amended rule 2a-7 concerning purchases undertaken in reliance on rule 17a-9).

³⁵⁰ Amended rule 2a-7(c)(13).

³⁵¹ Once a fund has broken a dollar, the fund could no longer use penny-rounding method of pricing or the amortized cost method of valuing portfolio securities, and therefore would have to compute share price by reference to the market values of the portfolio with the accuracy of at least a tenth of a cent. See 1983 Adopting Release, *supra* note 6, at n.6 and accompanying text. Thus, a fund whose market-based net asset value was determined to be \$0.994 would, upon ceasing to use the amortized cost method of valuation, begin to redeem shares at \$0.994 (rather than at \$0.990). See *generally id.*

³⁵² See, e.g., Dreyfus Comment Letter; Fund Democracy/CFA Comment Letter; MFDF Comment Letter.

³⁵³ See, e.g., Federated Comment Letter; RidgeWorth Comment Letter.

³⁵⁴ See Proposing Release, *supra* note 2, at Section V.A.6 (cost benefit analysis).

of money market funds, as issuers of redeemable securities, to be able to satisfy redemption requests within seven days after tender of the securities, even if a fund has re-priced its net asset value at a price other than its stable net asset value per share.³⁵⁵ Based on our recent experience, we believe it is unlikely that a fund that breaks the dollar would be able to satisfy redemption requests within seven days if it did not already have the capacity to process redemptions at prices other than the stable net asset value.³⁵⁶ To the extent that funds incur costs in meeting the new requirement, we believe the benefits to shareholders justify those costs, which we discuss in detail in the cost benefit section below.³⁵⁷

When we proposed the amendment, we proposed to require that the fund's board of directors determine that the fund has the capacity to sell and redeem securities at the current net asset value.³⁵⁸ We asked for comments on the board's role, and specifically whether the rule should require that the fund simply *have* the ability to process transactions at the fund's current net asset value without a specific board determination.³⁵⁹ Some commenters preferred that the board not be required to make such a determination, arguing that the determination is operational in nature and more appropriate for the fund's investment adviser or chief compliance officer to make.³⁶⁰ We agree that the focus of the rule should be on the fund's ability to process transactions, rather than on the board's determination regarding that ability, because the issue is operational in nature and need not directly involve the board. We have therefore revised the rule accordingly.³⁶¹

Some commenters raised the issue of whether the rule applies to third-party intermediaries, *i.e.*, whether it requires third parties to have the capacity to

³⁵⁵ See section 22(e) of the Act.

³⁵⁶ As we noted in the Proposing Release, the inability of one money market fund in 2008 to be able to process securities at prices other than \$1.00 per share impeded its ability to distribute assets during its liquidation. See Proposing Release, *supra* note 2, at n.262 and accompanying text. Even if a fund were to break a dollar, decide to liquidate, and suspend redemptions in reliance on new rule 22e-3 that we are adopting today, see *infra* Section II.H, the fund's ability to process redemptions at prices other than the stable net asset value is necessary to facilitate the orderly liquidation of the fund.

³⁵⁷ See *infra* Section V.

³⁵⁸ Proposed rule 2a-7(c)(1) (last two sentences).

³⁵⁹ See Proposing Release, *supra* note 2, at text following n.263.

³⁶⁰ See, e.g., Federated Comment Letter; MFDF Comment Letter; NYC Bar Assoc. Comment Letter.

³⁶¹ As adopted, the new requirement is paragraph (c)(13) of amended rule 2a-7, titled "Processing of Transactions."

process transactions in a money market fund at prices other than the fund's stable net asset value.³⁶² The rule by its terms applies only to money market funds and their transfer agents. We note, however, that intermediaries themselves 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 those investors.³⁶³

Several commenters requested that, if the Commission adopted the rule amendment, it provide ample time for money market funds to change their systems to accommodate purchases and redemptions at the current net asset value.³⁶⁴ We have established a compliance date of October 31, 2011, which is approximately 18 months after the effective date of the rule amendments, and more than 20 months after adoption of the amendments. This compliance period is designed to enable funds and those who act on their behalf sufficient time to come into full compliance with the amended rule.

G. Exemption for Affiliate Purchases

The Commission is adopting an amendment to rule 17a-9 under the Investment Company Act to expand the circumstances under which certain affiliated persons can purchase portfolio securities from a money market fund.³⁶⁵

³⁶² See, e.g., Tamarack Funds Comment Letter (requesting that the Commission clarify that funds "are not responsible for ensuring that intermediaries have the capacity to effect share transactions at other than \$1.00"); Russell Inv. Comment Letter (stating that the proposed rule amendment would not apply to intermediaries); see also ICI Comment Letter ("proposed amendments are silent with respect to * * * similar systems changes for broker-dealers, banks, insurance companies, trusts, 401(k) recordkeepers, and others that process such amendments"). Some commenters raised concerns about the costs that third parties might bear to revise their computer systems to have the capacity to accommodate purchases and redemptions of money market fund shares at prices other than the fund's stable net asset value. See, e.g., ICI Comment Letter.

³⁶³ Cf. rule 15c3-3(e)(3) under the Securities Exchange Act [17 CFR 240.15c3-3(e)(3)] (requiring broker-dealers to periodically re-compute the value of bank accounts held on behalf of broker-dealer customers); rule 15c3-2 under the Securities Exchange Act [17 CFR 240.15c3-2] (prohibiting a broker-dealer from using proceeds from free credit balances unless the proceeds are payable on demand of the customer). See also *Gilman v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 404 N.Y.S.2d 258, 262 (N.Y. Sup. Ct. 1978) (holding that after an investment is sold and proceeds belonging to the customer come into the broker's possession, the broker becomes a fiduciary with respect to those proceeds and may not consciously use them to the detriment of his customer and for his own benefit).

³⁶⁴ See, e.g., Federated Comment Letter (requesting at least one year); ICI Comment Letter (requesting at least two and a half years); SIFMA Comment Letter (requesting an "adequate period of time").

³⁶⁵ Rule 17a-9 provides an exemption from section 17(a) of the Act to permit affiliated persons

The amendment permits money market funds to dispose of distressed securities (e.g., securities depressed in value as a result of market conditions) quickly during times of market stress. The Commission is also adopting a related amendment to rule 2a-7, which requires funds to report all such transactions to the Commission.

1. Expanded Exemptive Relief

We are adopting the amendment to rule 17a-9, as proposed. The amendment expands the exemption provided by the rule from the Act's prohibition on affiliated transactions to permit affiliated persons to purchase from a money market fund a portfolio security that has defaulted,³⁶⁶ but that continues to be an eligible security, as long as the conditions of the rule governing the purchase price are satisfied.³⁶⁷ These conditions require that the purchase price is paid in cash and is equal to the greater of the security's amortized cost or its market value, including accrued interest.³⁶⁸

We are adding a new provision to the rule that will more broadly permit affiliated persons, under the same conditions as discussed above, to purchase other portfolio securities from an affiliated money market fund, for any reason, provided that such person promptly remits to the fund any profit

of a money market fund to purchase distressed portfolio securities from the fund. Absent a Commission exemption, section 17(a)(2) 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. Rule 17a-9 exempts certain purchases of securities from a money market fund from section 17(a), if the purchase price is equal to the greater of the security's amortized cost or market value (in each case, including accrued interest). 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.

³⁶⁶ The rule excludes an immaterial default unrelated to the financial condition of the issuer, which would make the rule unavailable in the case of defaults that are technical in nature, such as where the obligor has failed to provide a required notice or information on a timely basis. See Proposing Release, *supra* note 2, at n.272. Other provisions of rule 2a-7 currently except immaterial defaults unrelated to the financial condition of the issuer. See amended rule 2a-7(c)(7)(ii)(A).

³⁶⁷ See amended rule 17a-9(a). Previously, the exemption was available only for the purchase of a portfolio security that was no longer an "eligible security." This could occur, for example, when a security's ratings are downgraded. As we explained in the Proposing Release, this limitation served as a proxy indicating that the market value of the security was likely less than its amortized cost value, and thus the resulting transaction was fair to the fund and did not involve overreaching. See Proposing Release, *supra* note 2, at n.269 and accompanying text.

³⁶⁸ See amended rule 17a-9(a)(1)-(2).

it realizes from the later sale of the security.³⁶⁹ In these circumstances there may not be an objective indication that the security is distressed and thus that the transaction is clearly in the interest of the fund. Therefore, as proposed, we have added the "claw back" requirement to eliminate incentives for fund advisers and other affiliated persons to buy securities for reasons other than protecting fund shareholders from potential future losses.

Commenters supported the proposed amendment, agreeing that it would provide money market fund advisers with important flexibility to manage fund assets for the benefit of all shareholders during volatile periods.³⁷⁰ One commenter opposed the proposed amendment out of concern that the expansion of the rule may exacerbate the unwarranted expectation of some shareholders that advisers will take whatever steps are necessary to financially support the \$1.00 share price of their money market funds.³⁷¹ While we appreciate the commenter's concern, we do not believe that today's action will materially change shareholders' perceptions about money market funds or the likelihood of sponsor support during times of market turmoil. The amendment simply extends the existing rule to types of transactions that historically have been permitted through no-action assurances obtained from the Commission's staff because the staff believed they were in the best interest of the fund's shareholders.³⁷²

The amendment to rule 17a-9 that we are adopting today is intended to enable advisers to address acute credit or liquidity problems in a money market fund portfolio by purchasing securities from the fund that would be difficult or impossible to sell on the open market at or near their amortized cost. We have crafted the conditions of the rule, including the pricing conditions and the new claw back provision, to protect shareholders' interests and prevent overreaching by advisers. Our staff's experience is that, under such circumstances, these transactions appear to be fair and reasonable and in the best interests of fund shareholders.³⁷³ Moreover, we believe that the alternative of funds obtaining no-action assurances from the Commission staff for these transactions,

³⁶⁹ See amended rule 17a-9(b)(1)-(2).

³⁷⁰ See, e.g., Dreyfus Comment Letter; Vanguard Comment Letter.

³⁷¹ See Federated Comment Letter.

³⁷² See Proposing Release, *supra* note 2, at nn.270-71 and preceding, accompanying, and following text.

³⁷³ See Proposing Release, *supra* note 2, at text following n.271.

particularly during times of market stress, is time consuming and inefficient.

2. New Reporting Requirement

We also are adopting an amendment to rule 2a-7 to require a money market fund whose securities have been purchased by an affiliated person in reliance on rule 17a-9 to provide us with prompt notice by electronic mail of the transaction and the reasons for the purchase.³⁷⁴ Such reasons might include, for example, that the fund's adviser expected that the security would be downgraded, that due to the decreased market value of the security the fund was at risk of breaking the buck, or that the fund was experiencing significant redemption requests and wished to avoid a "fire sale" of assets to satisfy such requests. The amendment is intended to provide us with more complete information about these transactions and to alert us to potential problems the fund may be experiencing.

All commenters who addressed the proposed reporting requirement agreed with the need to provide the Commission with this information.³⁷⁵ At the suggestion of one,³⁷⁶ we have modified the requirement to provide that the notification must include the price at which the transaction was conducted and the amortized cost value of the security (which will be different if the market value is higher than the amortized cost), which will help us monitor whether the pricing conditions of rule 17a-9 have been satisfied.³⁷⁷

H. Fund Liquidation

The Commission is adopting new rule 22e-3, which 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. The rule permits a fund to suspend redemptions and payment of redemption proceeds if (i) The fund's board, including a majority of disinterested directors, determines 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, (ii) the board, including a majority of disinterested directors, irrevocably has approved the liquidation of the fund, and (iii) the fund, prior to suspending redemptions, notifies the Commission of its decision to liquidate and suspend redemptions.³⁷⁸ The new rule replaces rule 22e-3T, a temporary rule that provided a similar exemption for money market funds that participated in the Treasury Department's Guarantee Program.³⁷⁹

Rule 22e-3 is intended to reduce the vulnerability of investors to the harmful effects of a run on the fund, and minimize the potential for disruption to the securities markets. Because the suspension of redemptions may impose hardships on investors who rely on their ability to redeem shares, the conditions of the rule 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. The rule is designed only to facilitate the permanent termination of a fund in an orderly manner. We are revising one of the conditions of the rule, which requires that the board approve the liquidation of the fund, to provide that the fund board must have *irrevocably* approved the liquidation of the fund.³⁸⁰

Commenters generally supported the rule, which we are adopting largely as

proposed.³⁸¹ We have revised one of the rule's conditions in response to commenters' concerns. The proposed rule conditioned its relief on a fund breaking a dollar and re-pricing its shares.³⁸² Some commenters argued that the rule should allow a fund to suspend redemptions before it breaks a dollar.³⁸³ We are concerned that, without appropriate limits, fund sponsors might use the rule in the course of routine liquidations. We also recognize, however, that requiring a money market fund to actually re-price its securities may not be necessary in order to warrant the suspension of redemptions. Therefore, we have revised the rule's condition to require that the fund's board of directors, including a majority of disinterested directors, determine pursuant to rule 2a-7(c)(8)(ii)(C)³⁸⁴ that the extent of the deviation between the fund's amortized cost price per share and its shadow price may result in material dilution or other unfair results to investors or existing shareholders.³⁸⁵ In order to invoke the exemption, therefore, the fund's board must make the same determination that it would make if it were deciding to break a dollar. We believe the revised condition provides fund directors with the appropriate amount of discretion to act in the interest of shareholders.³⁸⁶

Paragraph (b) of rule 22e-3 allows a conduit fund (*i.e.*, a fund that invests in a money market fund) to rely on the rule if the money market fund in which it invests has suspended redemptions under the rule.³⁸⁷ We anticipated when

³⁸¹ Commenters generally agreed that the rule would facilitate fair and orderly liquidations to the benefit of all fund shareholders. *See, e.g.*, IDC Comment Letter; MFDF Comment Letter.

³⁸² Proposed rule 22e-3(a)(1).

³⁸³ *See, e.g.*, ABA Comment Letter; ICI Comment Letter; IMMFA Comment Letter.

³⁸⁴ Amended rule 2a-7(c)(8)(ii)(C) provides that, if a money market fund's board of directors believes that the deviation between the fund's amortized cost price per share and its shadow price may result in material dilution or other unfair results to investors or existing shareholders, it shall cause the fund to take such action as it deems appropriate to eliminate or reduce to the extent practicable such dilution or unfair results.

³⁸⁵ Rule 22e-3(a)(1).

³⁸⁶ Under the final rule, the exemption applies to securities tendered for redemption but not yet priced at the time the fund begins to rely on the rule. Therefore, for example, if a shareholder submits a redemption order at noon and the fund decides to liquidate and suspend redemptions pursuant to rule 22e-3 at 2:00 pm, the shareholder would be entitled to receive only his or her *pro rata* share of the fund's liquidation proceeds. This is also the case for shareholders who submitted redemption orders after the last time as of which the fund computed its net asset value and shareholders who submitted redemption orders after 2:00 pm.

³⁸⁷ Rule 22e-3(b) also requires that the conduit fund promptly notify the Commission that it has suspended redemptions in reliance on the rule.

³⁷⁴ Amended rule 2a-7(c)(7)(iii)(B). We have clarified that not only purchases by affiliated persons, but also purchases by promoters and principal underwriters of a fund, and any affiliated person of such persons, which are exempt under rule 17a-9, must be reported to the Commission under the provision. *Compare* amended rule 2a-7(c)(7)(iii)(B) with proposed rule 2a-7(c)(7)(iii)(B).

³⁷⁵ *See, e.g.*, BlackRock Comment Letter, Dreyfus Comment Letter. One suggested that sales prices of any securities purchased by the adviser pursuant to rule 17a-9 be promptly reported to the fund's board of directors as well as to the Commission. Comment Letter of the Independent Trustees of Fidelity Fixed Income Funds (Sept. 8, 2009) ("Fidelity Fixed Income Indep. Trustees Comment Letter"). We are not extending the reporting provision to include notification to fund boards because the provision is intended to enable the Commission to monitor how rule 17a-9 is being used. Nevertheless, we expect that fund boards will want to know this information and will request it.

³⁷⁶ *See* Fidelity Fixed Income Indep. Trustees Comment Letter.

³⁷⁷ *See* amended rule 2a-7(c)(iii)(B).

³⁷⁸ Rule 22e-3(a). A fund that intends to be able to rely on rule 22e-3 may also need to update its prospectus to disclose the circumstances under which it may suspend redemptions. *See, e.g.*, Item 6 of Form N-1A ("Purchase and Sale of Fund Shares").

³⁷⁹ *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)]. The Treasury Department's Guarantee Program guaranteed that shareholders of a participating money market fund would receive the fund's stable share price for each share owned as of September 19, 2008, if the fund were to liquidate under the terms of the Program. *See supra* note 16 and accompanying text. The Program expired on September 19, 2009, and rule 22e-3T expired on October 18, 2009.

³⁸⁰ Rule 22e-3(a)(2). This revision is designed to limit the availability of the rule to extraordinary circumstances, by preventing a fund from invoking the rule if the board determines to liquidate the fund but subsequently revokes its determination, which might, in effect, enable the fund to temporarily suspend redemptions.

we proposed this provision that it would be used principally by insurance company separate accounts issuing variable insurance contracts and by funds participating in master-feeder arrangements.³⁸⁸ At the suggestion of one commenter who pointed out that most insurance company separate accounts are organized as unit investment trusts rather than management companies,³⁸⁹ we have expanded the rule to include unit investment trusts.³⁹⁰

Paragraph (c) of the rule provides that the Commission may take certain steps to protect shareholders. It permits the Commission to rescind or modify the relief provided by the rule (and thus require the fund to resume honoring redemptions) if, for example, a liquidating fund has not devised, or is not properly executing, a plan of liquidation that protects fund shareholders. Under this provision, the Commission may modify the relief after appropriate notice and opportunity for hearing in accordance with section 40 of the Act.³⁹¹ Commenters did not address this provision, and we are adopting it as proposed.

One commenter recommended that the rule not require prior notice to the Commission.³⁹² In light of the seriousness of the consequences to shareholders, we believe it is important that the Commission receive prior notice of a suspension of redemptions, particularly when the burden of providing such notice is minimal.³⁹³ Another commenter suggested that the Commission require funds to disclose their plan of liquidation as a condition for suspending redemptions.³⁹⁴ We are reluctant to impose such a requirement because the time needed to formulate such a plan may prevent fund boards from acting in a timely fashion in the case of an emergency, but we expect that funds would promptly communicate their plan of liquidation to shareholders. Another commenter recommended that the suspension period be limited to 60 days.³⁹⁵ We have not modified the final rule in response

to these comments because liquidations will proceed differently depending on a fund's particular circumstances, and we believe that fund management, under the supervision of the board, is best able to devise and execute a plan of liquidation that is in the best interest of fund shareholders. Furthermore, as discussed above, the Commission will retain authority under the rule to rescind or modify the relief (after appropriate notice and opportunity for hearing) if we conclude, for example, that a liquidating fund has not devised, or is not properly carrying out, a plan of liquidation that protects fund shareholders.³⁹⁶

III. Compliance Dates

The amendments to rules 2a-7, 17a-9 and 30b1-6T, and new rules 22e-3 and 30b1-7, and new Form N-MFP become effective May 5, 2010. Unless otherwise discussed below or in this Release, the compliance date is the date of effectiveness.

Some money market funds may have policies that can be changed only if authorized by a shareholder vote. For example, a money market fund may have a disclosed policy of maintaining a WAM (*i.e.*, weighted average maturity) no greater than 90 days, which is less restrictive than the amendment the Commission is adopting today requiring a money market fund to maintain a WAM no greater than 60 days.³⁹⁷ The Commission believes that, in those circumstances where the existing policy is less restrictive than the amendments we are today adopting and does not conflict with those amendments, a money market fund would not need to hold a shareholder vote under sections 8(b) or 13(a) of the Act merely to comply with the amendments.³⁹⁸ Moreover, we would not object if a fund were to amend its registration statement to reflect the fund's compliance with the amended rule pursuant to rule 485(b) under the Securities Act of 1933, if other changes in the fund's post-effective amendment meet the conditions for immediate effectiveness under that rule.³⁹⁹

A. Portfolio Requirements

Except as indicated below, the compliance date for amendments to rule 2a-7 related to portfolio quality, maturity, liquidity, and repurchase agreements, is May 28, 2010. Funds are not required to dispose of portfolio

securities owned, or terminate repurchase agreements entered into, as of the time of adoption of the amendments to comply with the requirements of the rule as amended. Fund portfolios must meet the new maximum WAM and WAL limits by June 30, 2010.

B. Designation of NRSROs

Each fund must disclose the designated NRSROs in its Statement of Additional Information pursuant to amended rule 2a-7(a)(11)(iii) no later than December 31, 2010. This additional time should permit fund boards of directors to evaluate and designate NRSROs without the need to call a special board meeting. Fund boards are free to take advantage of the rule amendments any time after the effective date.

C. Disclosure and Reporting of Portfolio Information

Web site disclosure. The compliance date for public Web site disclosure is October 7, 2010. This should provide each fund sufficient time to revise its information and other systems to ensure that required information is accurately posted and maintained on its Web site.

Reporting to the Commission. All money market funds must begin filing information on Form N-MFP pursuant to rule 30b1-7 no later than December 7, 2010. This compliance date is designed to permit money market funds to develop systems necessary to collect and submit the portfolio information on Form N-MFP. Funds filing information with the Commission pursuant to rule 30b1-6T will no longer be required to file this information after December 1, 2010.

Beginning October 7, 2010, our staff will be able to receive trial data from funds, on a voluntary basis, pursuant to the requirements of rule 30b1-7. We will use these voluntary submissions and the experiences of funds during this period to make adjustments to our filing system and provide guidance to funds. We do not intend to make these submissions public.⁴⁰⁰

D. Processing of Transactions

Funds must comply with the new requirement to be able to process transactions at prices other than stable net asset value no later than October 31, 2011, which is more than 20 months

³⁸⁸ See Proposing Release, *supra* note 2, at text accompanying n.289.

³⁸⁹ See Committee Ann. Insur. Comment Letter.

³⁹⁰ Rule 22e-3(b) (providing relief to a "registered investment company" rather than to a "fund," or "registered open-end management investment company," as proposed).

³⁹¹ Rule 22e-3(c).

³⁹² See ABA Comment Letter.

³⁹³ In addition, these prior notices will, among other things, help us to ascertain whether a fund has erroneously invoked the rule in circumstances for which it was not intended to be used (*e.g.*, a routine liquidation).

³⁹⁴ See Federated Comment Letter.

³⁹⁵ See Bankers Trust Comment Letter.

³⁹⁶ See *supra* note 391 and accompanying paragraph.

³⁹⁷ See *supra* Section II.B.1.

³⁹⁸ 15 U.S.C. 80a-8(b), 80a-13(a).

³⁹⁹ 17 CFR 230.485(b).

⁴⁰⁰ We do not intend to make public the information submitted to us on Form N-MFP as trial data before the mandatory compliance date because of the possibility of errors in the information submitted. See *supra* text following note 339.

after adoption of the amendments.⁴⁰¹ This compliance period is designed to enable funds and those who act on their behalf sufficient time to come into full compliance with the amended rule.

IV. Paperwork Reduction Act Analysis

Certain provisions of the amendments to rules 2a-7 and 30b1-6T, new rules 22e-3 and 30b1-7, and Form N-MFP under the Investment Company Act contain “collections of information” within the meaning of the Paperwork Reduction Act of 1995 (“PRA”).⁴⁰² The titles for the existing collections of information that are affected by the rule amendments are: “Rule 2a-7 under the Investment Company Act of 1940, Money market funds” (OMB Control No. 3235-0268), “Rule 30b1-6T under the Investment Company Act of 1940, Weekly portfolio report for certain money market funds” (OMB Control No. 3235-0652), and “Rule 38a-1 under the Investment Company Act of 1940, Compliance procedures and practices of registered investment companies” (OMB Control No. 3235-0586). The titles for the new collections of information are: “Rule 22e-3 under the Investment Company Act of 1940, Exemption for liquidation of money market funds,” “Rule 30b1-7 under the Investment Company Act of 1940, Monthly report for money market funds,” and “Form N-MFP under the Investment Company Act of 1940, Portfolio Holdings of Money Market Funds.” We published notice soliciting comments on the collection of information requirements in the Proposing Release and submitted the proposed collections of information to the Office of Management and Budget (“OMB”) for review in accordance with 44 U.S.C. 3507(d) and 5 CFR 1320.11 under the control numbers 3235-0268 (rule 2a-7), 3235-0654 (rule 22e-3), and 3235-0653 (rule 30b1-6 and Form N-MFP). OMB has approved the collection of information pursuant to rule 30b1-6T under the control number 3235-0652.

Our amendments and new rules are designed to make money market funds more resilient to risks in the short-term debt markets, and to provide greater protections for investors in a money market fund that is unable to maintain a stable net asset value. 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.

⁴⁰¹ See *supra* text accompanying and following note 364.

⁴⁰² 44 U.S.C. 3501-3521.

A. Rule 2a-7

Rule 2a-7 under the Investment Company Act exempts money market funds from the Act’s valuation requirements, permitting money market funds to maintain stable share pricing, subject to certain risk-limiting conditions. As discussed above, we are amending rule 2a-7 in several respects. Our amendments revise portfolio quality and maturity requirements; introduce liquidity requirements; require money market fund boards to adopt procedures providing for periodic stress testing of the fund’s portfolio; require funds to disclose monthly on their Web sites information on portfolio securities; and finally, require money market funds to have the capability to redeem and issue their securities at prices other than the fund’s stable net asset value per share.⁴⁰³ Several of the amendments create new collection of information requirements. The respondents to these collections of information will be money market funds or their advisers, as noted below.

1. Designation of NRSROs

Under the amendments to rule 2a-7, money market funds will be required to disclose designated NRSROs (including any limitation in the use of the designated NRSRO) in their SAI,⁴⁰⁴ which constitutes a collection of information. Compliance with this disclosure requirement will be mandatory for any fund that holds itself out as a money market fund in reliance on rule 2a-7. This information will not be kept confidential. The disclosures are intended to provide investors and third party analysts with information on NRSROs that money market funds will look to when they have to consider credit ratings under rule 2a-7, which may be relevant to investors in choosing among funds. Many money market funds currently discuss credit rating agencies in their registration statements describing threshold credit ratings for portfolio investments, and often specify NRSROs that rate instruments of the type the fund purchases. We anticipate that adding one or two sentences to the discussion identifying designated NRSROs (and any limitations on the use of a designated NRSRO) will not result in additional hourly burdens or printing costs beyond those currently approved in the existing collection of information titled “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).

2. Portfolio Liquidity

As discussed above, the amended rule includes a general liquidity requirement, under which each money market fund must hold securities that are sufficiently liquid to meet foreseeable shareholder redemptions in light of its obligations under section 22(e) of the Act and any commitments the fund has made to shareholders. We also noted that in order to comply with this provision in amended rule 2a-7 under the compliance rule, we expect that money market funds will adopt policies and procedures designed to assure that appropriate efforts are undertaken to identify risk characteristics of the fund’s shareholders.⁴⁰⁵ We anticipate that these policies and procedures may add additional burdens to those currently approved in the existing collection of information under rule 38a-1 under the Investment Company Act. Based on commenters’ views, we assume that money market funds currently monitor and manage daily net flows in and out of the funds,⁴⁰⁶ and in doing so, monitor the risk characteristics and likely redemptions of certain shareholders, which is a factor we would expect funds to consider under the general liquidity requirement in the amended rule. We believe, however, that many, if not most, funds may have to document the procedures they adopt for the compliance rule. For purposes of this PRA analysis, we estimate that funds would incur a one-time average burden of 8 hours to document policies and procedures to identify risk characteristics of the fund’s investors. In addition, staff estimates that the board of directors (as a whole) would take 1 hour to review and adopt these policies and procedures. Amortized over a 3 year period, this would be an annual burden per fund complex of 3 hours. We believe that these characteristics would be applicable to and documented on behalf of all money market funds in a fund complex, and we estimate that 163 fund complexes with money market funds are subject to rule 2a-7. Accordingly, we estimate that the total additional burden to document these policies would be 1467 hours.⁴⁰⁷ Amortized over a 3-year period, the estimated annual hourly burden would be 489 hours for all

⁴⁰⁵ See *supra* note 198 and accompanying text.

⁴⁰⁶ See Dreyfus Comment Letter; RidgeWorth Comment Letter.

⁴⁰⁷ This estimate is based on the following calculation: (8 + 1) hours × 163 fund complexes = 1467 hours.

⁴⁰³ See *supra* Section II.A-F.

⁴⁰⁴ Amended rule 2a-7(a)(11)(iii).

money market fund complexes.⁴⁰⁸ We believe that any ongoing burdens to reevaluate the need for changes in the policies and procedures would be incorporated in the current estimated burdens for rule 38a-1.

3. Stress Testing

We are requiring, substantially as proposed, that a money market fund's board of directors adopt written procedures that provide for the periodic testing of the fund's ability to maintain a stable net asset value per share based on certain hypothetical events.⁴⁰⁹ The rule requires the board to determine the frequency of testing. The procedures must provide for a report of the testing results to be submitted to the board of directors at its next regularly scheduled meeting, or sooner if appropriate based on the results. The report must include 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.⁴¹⁰ Compliance with the new reporting requirement is mandatory for any fund that holds itself out as a money market fund and uses either the amortized cost method of valuing portfolio securities or the penny-rounding method of pricing fund shares. When provided to the Commission in connection with staff examinations or investigations, the information will be kept confidential to the extent permitted by law.

We anticipate that stress testing will give fund advisers a better understanding of the effect of potential market events and shareholder redemptions on their funds' ability to maintain a stable net asset value, the fund's exposure to the risk of not maintaining a stable net asset value, and actions the adviser may need to take to

⁴⁰⁸ PRA submissions for approval are made every three years. To estimate an annual burden for a collection of information that occurs one time, the total burden is amortized over the three-year period.

⁴⁰⁹ See *supra* Section II.C.4. These events include, without limitation, 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 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 amended rule 2a-7(c)(10)(v)(A).

⁴¹⁰ Amended rule 2a-7(c)(10)(v)(B). The report to the board must include the dates on which the testing was performed and the magnitude of each hypothetical event that would cause the deviation of the money market fund's net asset value calculated using available market quotations (or appropriate substitutes that reflect current market conditions) from its net asset value per share calculated using amortized cost to exceed 1/2 of 1%.

mitigate the possibility of the fund breaking the buck.⁴¹¹

Commission staff believes that in light of the events of the fall of 2008, most, if not all, money market funds currently conduct some stress testing of their portfolios as a matter of routine fund management and business practice.⁴¹² These procedures likely vary depending on the fund's investments. For example, a prime money market fund that is offered to institutional investors may test for hypothetical events such as potential downgrades or defaults in portfolio securities while a U.S. Treasury money market fund might not.⁴¹³ Some funds that currently conduct testing may be required to include additional hypothetical events under the amended rule. These funds likely provide regular reports of the test results to senior management. We assumed, however, that currently most funds do not have written procedures documenting the stress testing, do not report the results of testing to their boards of directors, and do not provide an assessment from the fund's adviser regarding the fund's ability to withstand the hypothetical events reasonably likely to occur in the next year.

Commission staff believes that stress testing procedures will be developed for all the money market funds in a fund complex by the fund adviser, and will address appropriate variations for individual money market funds within the complex.⁴¹⁴ Staff estimates that it will take a portfolio risk analyst an average of 22 hours initially to draft procedures documenting the complex's stress testing, and 3 hours for the board of directors (as a whole) to consider and adopt the written procedures.⁴¹⁵ We

⁴¹¹ See Proposing Release, *supra* note 2, at text following n.212.

⁴¹² Commenters corroborated our staff's belief. See, e.g., State Street Comment Letter; T. Rowe Price Comment Letter. The estimates of hour burdens and costs provided in the PRA and cost benefit analyses in the Proposing Release were based on staff discussions with representatives of money market funds and on the experience of Commission staff. We did not receive any comment on the estimates and assumptions with respect to stress testing included in the analysis in our proposal. Accordingly, we have not modified any of those assumptions and estimates other than as necessary in light of the new requirement included in the amended rule.

⁴¹³ See TDAM Comment Letter (noting that testing Treasury funds for downgrades or defaults would be unnecessary).

⁴¹⁴ We expect that the board of directors would be the same for all the money market funds in a complex, and thus could adopt the stress test procedures for all money market funds in the complex at the same meeting.

⁴¹⁵ We have added 1 hour to the estimate of 21 hours in the Proposing Release to account for drafting procedures on when additional reports must be provided to the board based on the results of stress testing.

therefore estimate that the total burden to draft these procedures initially will be 4075 hours.⁴¹⁶ Amortized over a three-year period, this will result in an average annual burden of 8.33 hours for an individual fund complex and a total of 1358 hours for all fund complexes.⁴¹⁷ Staff estimates that a risk analyst will also spend an average of 6 hours per year revising the written procedures to reflect changes in the type or nature of hypothetical events appropriate to stress tests and the board will spend 1 hour to consider and adopt the revisions, for a total annual burden of 1141 hours.⁴¹⁸

As noted above, each report to the board of directors will include an assessment by the fund's adviser of the fund's ability to withstand reasonably likely hypothetical events in the coming year. Staff estimates that it will take on average: (i) 10 hours of portfolio management time to draft each report to the board and 2 hours of an administrative assistant's time to compile and copy the report (for a total of 12 hours), and (ii) 15 hours for the fund adviser to provide its assessment. Under normal circumstances, the report must be provided at the next scheduled board meeting, and we estimate that the report and the adviser's assessment will cover all money market funds in a complex. We assume that funds will conduct stress tests no less than monthly. With an average of 6 board meetings each year, we estimate that the annual burden for regularly scheduled reports would be 162 hours for an individual fund complex.⁴¹⁹ Under the final rule, a report must be provided earlier if appropriate in light of the results of the test. Staff estimates that as a result of unanticipated changes in market conditions or other events, stress testing results are likely to prompt additional reports on average four times each year.⁴²⁰ Thus, we estimate these

⁴¹⁶ This estimate is based on the following calculation: (22 hours + 3 hours) × 163 fund complexes = 4075 hours.

⁴¹⁷ These estimates are based on the following calculations: (22 + 3) × 3 = 8.33 hours; 8.33 × 163 fund complexes = 1357.79 hours. PRA submissions for approval are made every three years. To estimate an annual burden for a collection of information that occurs one time, the total burden is amortized over the three-year period.

⁴¹⁸ This estimate is based on the following calculation: (6 hours (analyst) + 1 hour (board)) × 163 fund complexes = 1141 hours.

⁴¹⁹ This estimate is based on the following calculation: (10 hours + 2 hours + 15 hours) × 6 meetings = 162 hours.

⁴²⁰ We anticipate that in many years there will be no need for special reports, but that in a year in which there is severe market stress, a fund may report to the board weekly for a period of 3 to 6 months. Such reporting would generate 9 to 18 reports in addition to the regular monthly reports. Assuming that this type of event may occur once

reports would result in an additional 108 hours for an individual fund complex each year.⁴²¹ We estimate the total annual burden for all fund complexes would be 44,010 hours.⁴²²

The amended rule requires a money market fund to retain records of the reports on stress tests for at least 6 years (the first two in an easily accessible place).⁴²³ The retention of these records is necessary to allow the staff during examinations of funds to determine whether a fund is in compliance with the stress test requirements. We estimate that the burden will be 10 minutes per fund complex per report to retain these records for a total annual burden of 272 hours for all fund complexes.⁴²⁴

Thus, we estimate that for the three years following adoption, the average annual burden resulting from the stress testing requirements will be 287 hours for each fund complex with a total of 46,781 hours for all fund complexes.⁴²⁵

4. Repurchase Agreements

We are adopting, as proposed, amendments affecting a money market fund's ability to "look through" a repurchase agreement for purposes of rule 2a-7's diversification provisions.⁴²⁶ One of these amendments is that a money market fund will be able to look through a repurchase agreement only if the fund's board of directors or its delegate evaluates the counterparty's creditworthiness.⁴²⁷

Several commenters stated that money market fund boards already evaluate the credit quality of counterparties in the course of making an overall credit risk determination under rule 2a-7(c)(3)(i).⁴²⁸ Because we are adding a separate creditworthiness evaluation in rule 2a-7(c)(4)(ii)(A), funds will need to keep records of such evaluations pursuant to rule 2a-7(c)(11)(ii), which requires a money

every five years, and additional reports would be generated for 6 months, a fund would produce an average of four additional reports per year (18 additional reports ÷ 5 = 3.6 reports).

⁴²¹ This estimate is based on the following calculation: (10 hours + 2 hours + 15 hours) × 4 = 108 hours.

⁴²² This estimate is based on the following calculation: (162 hours + 108 hours) × 163 fund complexes = 44,010 hours.

⁴²³ Amended rule 2a-7(c)(11)(vii).

⁴²⁴ This estimate is based on the following calculation: 0.1667 hours × 10 reports × 163 fund complexes = 271.7 hours.

⁴²⁵ These estimates are based on the following calculations: 8.33 hours (draft procedures) + 7 hours (revise procedures) + 120 hours (10 reports) + 150 hours (10 assessments) + 1.67 hours (record retention) = 287 hours; 287 hours × 163 complexes = 46,781 hours.

⁴²⁶ See *supra* Section II.D; Proposing Release, *supra* note 2, at Section II.E.

⁴²⁷ Amended rule 2a-7(c)(4)(ii)(A).

⁴²⁸ See *supra* note 277.

market fund to retain a record of considerations and actions under the rule for at least 6 years (the first two in an easily accessible place).⁴²⁹

Compliance with this recordkeeping requirement is mandatory for all funds that take advantage of the special look-through treatment for diversification purposes. We estimate that the burden to keep those records will be 2 hours per fund complex, for a total annual burden of 326 hours for all fund complexes.⁴³⁰

5. Public Web site Posting

The amendments require money market funds to post monthly portfolio information on their Web sites.⁴³¹ We believe that greater transparency of fund portfolios will provide investors with a better understanding of the fund's investment risks, and may allow investors to exert influence on risk-taking by fund advisers and thus reduce the likelihood that a fund will break the buck. Information will be posted on a public Web site, and compliance with this requirement is mandatory for any fund that holds itself out as a money market fund in reliance on rule 2a-7. In the Proposing Release, Commission staff estimated that there are approximately 750 money market funds that would be affected by the amendments. In addition, our staff noted that based on interviews with industry representatives, most money market funds already post portfolio information on their webpages at least quarterly.⁴³² Commission staff also estimated that 20 percent of money market funds, or 150 funds, do not currently post this information at least quarterly, and therefore would need to develop a webpage to comply with the amendments. Staff estimated that a money market fund would spend approximately 24 hours of internal money market fund staff time initially to develop the Web page. Staff further estimated that a money market fund would spend approximately 4 hours of professional time to maintain and update the relevant webpage with the required information on a monthly basis.

⁴²⁹ Amended rule 2a-7(c)(11)(ii).

⁴³⁰ This estimate is based on the following calculation: 2 hours × 163 fund complexes = 326 hours.

⁴³¹ Amended rule 2a-7(c)(12).

⁴³² Certain of the required information is currently maintained by money market funds for regulatory reasons, such as in connection with accounting, tax, and disclosure requirements. We understand that the remaining information is retained by funds in the ordinary course of business. Accordingly, for the purposes of our analysis, we do not ascribe any time to producing the required information.

No commenters addressed the number of money market funds that would be affected by the proposal or the estimated burden hours for developing, maintaining and updating the webpage. Although, as described above, we have revised the proposed disclosure which should result in less information being required on a fund's Web site, Commission staff believes that the number of money market funds is currently 719 and that the hour burden per fund remains the same as previously estimated. Although it is possible that the reduced information required might result in a minimal decrease in the amount of time required to develop, maintain and update the webpage, Commission staff believes that the decrease would be negligible.

One commenter stated that the funds that currently post portfolio holdings information at least quarterly on their Web sites would need, under the rule amendments, to develop the capability to retain previous months' portfolio holdings information on their Web sites, resulting in an additional one-time burden that Commission staff did not include in its estimate in the Proposing Release.⁴³³ Based on a review of some of the current portfolio Web site disclosure by some commenters and follow-up discussions with some commenters, Commission staff estimates that 500 of the 575 funds that currently post portfolio information on their webpages at least quarterly will need to develop this capability. Commission staff further estimates that each of these 500 funds will spend 12 hours to develop this capability, resulting in an additional one-time burden for all such funds of 6000 hours.⁴³⁴

Based on an estimate of 719 money market funds posting their portfolio holdings on their webpages, including 144 funds incurring start-up costs to develop a webpage and 500 funds incurring a one-time cost to develop the capability to retain previous months' portfolio holdings information on their Web sites, we estimate that, in the aggregate, the amendment will result in a total of 37,664 average burden hours for all money market funds for each of the first three years.⁴³⁵

⁴³³ See Data Communiqué Comment Letter. Under our proposal, funds would have been required to maintain the portfolio holdings information on their Web sites for at least 12 months. We are adopting a 6-month maintenance period for portfolio holding information.

⁴³⁴ The estimated 12 hours is one-half the time that we estimated that a fund would need to set up a new webpage (24 hours).

⁴³⁵ The estimate is based on the following calculations. The staff estimates that 144 funds will require a total of 3456 hours initially to develop a webpage (144 funds × 24 hours per fund = 3456

6. Reporting of Rule 17a-9 Transactions

We are amending rule 2a-7 to require a money market fund to promptly notify the Commission by electronic mail of the purchase of a money market fund's portfolio security by certain affiliated persons in reliance on rule 17a-9 and to explain the reasons for, and the transaction price of, such purchase.⁴³⁶ The reporting requirement is designed to assist Commission staff in monitoring money market funds' affiliated transactions that otherwise would be prohibited. The new collection of information will be mandatory for money market funds that rely on rule 2a-7 and that rely on rule 17a-9 for an affiliated person to purchase a money market fund's portfolio security. Information submitted to the Commission related to a rule 17a-9 transaction will not be kept confidential.

We estimate that fund complexes will provide one notice for all money market funds in a particular fund complex holding a distressed security purchased in a transaction under rule 17a-9. As noted above, Commission staff estimates that there are 163 fund complexes with money market funds subject to rule 2a-7. Of these fund complexes, Commission staff estimates that an average of 25 per year will be required to provide notice to the Commission of a rule 17a-9 transaction, with the total annual response per fund complex, on average, requiring 1 hour of an in-house attorney's time. We received no comments on this estimate and have not modified it. Given these estimates, the total annual burden of this amendment to rule 2a-7 for all money market funds would be approximately 25 hours.⁴³⁷

7. Total Burden

The currently approved burden for rule 2a-7 is 310,983 hours. The additional burden hours associated with the proposed amendments to rule 2a-7 will increase the renewal estimate to 395,779 hours annually.⁴³⁸

hours) and 500 funds will require a total of 6000 hours initially to develop the capability to maintain historical portfolio holding information (500 funds × 12 hours per fund = 6000 hours). In addition, each of the 719 funds would require 48 hours per year to update and maintain the webpage, for a total of 34,512 hours per year (4 hours per month × 12 months = 48 hours per year; 48 hours per year × 719 funds = 34,512). The average annual hour burden for each of the first three years would thus equal 37,664 hours (3456 + 6000 + (34,512 × 3) + 3).

⁴³⁶ See amended rule 2a-7(c)(7)(iii)(B).

⁴³⁷ The estimate is based on the following calculation: (25 fund complexes × 1 hour) = 25 hours.

⁴³⁸ This estimate is based on the following calculation: 310,983 hours (current burden) + 46,781 hours (stress testing) + 326 hours

B. Rule 22e-3

Rule 22e-3 permits a money market fund that has broken the buck, or is at imminent risk of breaking the buck, to suspend redemptions and postpone the payment of proceeds pending board-approved liquidation proceedings. The rule also requires a money market fund to provide prior notification to the Commission of its decision to suspend redemption and liquidate. Rule 22e-3 is intended to facilitate an orderly liquidation, reduce the vulnerability of shareholders to the harmful effects of a run on a fund, and minimize the potential for market disruption. The notification 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 redemption. The respondents to this information collection would be money market funds that break the buck, or are at imminent risk of breaking the buck, and elect to rely on the exemption afforded by the rule. Respondents also will include certain conduit funds that have invested in money market funds that suspended redemptions in reliance on the rule. Compliance with the notification requirement is mandatory for funds and conduit funds that rely on rule 22e-3, and the information will not be kept confidential.

In the Proposing Release, Commission staff estimated for purposes of the Paperwork Reduction Act that, on average, one money market fund would break the buck and liquidate every six years.⁴³⁹ The staff further estimated that a fund would spend approximately one hour of an in-house attorney's time to prepare and submit the notice. No commenter addressed the estimated number of money market funds that would rely on the rule or the estimated burden hours associated with complying with the rule's notification requirement. 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.⁴⁴⁰ The proposed rule would have applied only to conduit funds that are registered open-end management investment companies, and in response to one comment we have expanded the provision to also permit conduit funds

(repurchase agreements) + 37,664 hours (Web site posting) + 25 hours (reporting 17a-9 transactions) = 395,779 hours.

⁴³⁹ As noted above, only two money market funds have broken the buck since the adoption of rule 2a-7 in 1983.

⁴⁴⁰ See rule 22e-3(b).

that are organized as unit investment trusts to rely on the rule.⁴⁴¹ The staff estimates that there are a total of 780 conduit funds that may invest in money market funds that suspend redemptions in reliance on the rule, and that an average of 10 conduit funds may invest in any money market fund.⁴⁴² Given these estimates, the total annual burden of proposed rule 22e-3 for all money market funds and conduit funds would be approximately 110 minutes.⁴⁴³

C. Monthly Reporting of Portfolio Holdings

Rule 30b1-7 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 rule is intended to improve transparency of information about money market funds' portfolio holdings and facilitate oversight of money market funds. The information required by the form will be data-tagged in XML format and filed through EDGAR. The respondents to rule 30b1-7 will be investment companies that are regulated as money market funds under rule 2a-7. Compliance with rule 30b1-7 is mandatory for any fund that holds itself out as a money market fund in reliance on rule 2a-7. Responses to the disclosure requirements will not be kept confidential.

In the Proposing Release, Commission staff estimated that 750 money market funds would be required by proposed rule 30b1-6 to file, on a monthly basis, a complete Form N-MFP disclosing certain information regarding the fund and its portfolio holdings.⁴⁴⁴ No commenters addressed this estimate. For purposes of this PRA analysis, the burden associated with the requirements of rule 30b1-7 has been included in the collection of information requirements of Form N-MFP.

Based on our experience with other interactive data filings, we estimated in the Proposing Release that money market funds would require an average of approximately 40 burden hours to compile, tag, and electronically file the required portfolio holdings information

⁴⁴¹ See *supra* note 390 and accompanying text.

⁴⁴² These estimates are based on a review of filings with the Commission.

⁴⁴³ 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 × 11 (combined number of affected funds and conduit funds) = 110 minutes.

⁴⁴⁴ As noted above, in September 2009 we adopted interim final temporary rule 30b1-6T. In order to minimize confusion over rule numbering, we are adopting proposed rule 30b1-6 as rule 30b1-7.

for the first time and an average of approximately 8 burden hours in subsequent filings.⁴⁴⁵ Two commenters asserted that the Commission's estimates did not include time to review the information required in Form N-MFP.⁴⁴⁶ While the estimate did include time for the review of the information, we nevertheless have increased our estimate to include an additional 2 hours per filing for review of the information to account for a full and careful review of the information to be filed. We now estimate that there are 719 money market funds and that they will require an average of approximately 42 burden hours to compile (including review of the information), tag and electronically file the required portfolio holdings information for the first time and an average of approximately 10 burden hours in subsequent filings. Based on these estimates, we estimate the average annual burden over a three-year period would be 131 hours per money market fund.⁴⁴⁷ Based on an estimate of 719 money market funds submitting Form N-MFP in interactive data format, each incurring 131 hours per year on average, we estimate that, in the aggregate, Form N-MFP would result in 94,189 burden hours, on

⁴⁴⁵ See Proposing Release, *supra* note 2, at n.334 and accompanying text. We understand that the required information is currently maintained by money market funds pursuant to other regulatory requirements or in the ordinary course of business. Accordingly, for the purposes of our analysis, we do not ascribe any time to producing the required information.

⁴⁴⁶ See Data Communiqué Comment Letter; Comment Letter of Bowne & Co. Inc. (Oct. 29, 2009) ("Bowne Comment Letter"). In addition, one commenter asserted that the Commission's estimate of 128 burden hours per money market fund for the first year (1 filing × 40 hours + 11 filings × 8 hours) is far too low for subadvised funds. See Committee Ann. Insur. Comment Letter. The commenter, however, did not provide an estimate of the first year burden hour for subadvised funds. As explained below in our discussion of the effect the rule and form will have on competition, we do not believe that the one-time burden for subadvised funds will be much different than the burden on non-subadvised money market funds because the information already should be readily available to the subadviser and the lengthened time for filing Form N-MFP (from the proposed two business days to five business days after the end of each month) should provide subadvisers with sufficient time to send the information to the principal adviser without having to invest in new infrastructure to provide the information on a real-time basis. See *also infra* Section VI.D.

⁴⁴⁷ The staff estimates that a fund will make 36 filings in three years. The first filing will require 42 hours and subsequent filings would require 10 hours each, for an average annual burden of 131 hours (1 filing × 42 hours = 42 hours; 35 filings × 10 hours = 350 hours; 42 hours + 350 hours = 392 hours; 392 hours ÷ 3 years = 130.66 hours). Thereafter, filers generally would not incur the start-up burdens applicable to the first filing.

average, for all money market funds for each of the first three years.⁴⁴⁸

D. Weekly Reporting of Portfolio Holdings

Rule 30b1-6T requires a money market fund whose market-based net asset value is less than \$0.9975 to electronically (i) notify the Commission promptly and submit a portfolio schedule within one business day, and (ii) submit a portfolio schedule within two business days after the end of each week until such time as the fund's market-based net asset value equals or exceeds \$0.9975. The rule is intended to facilitate our oversight of money market funds. We are adopting as final rule 30b1-6T. As adopted, the only change to the rule is the expiration date. Rule 30b1-6T will expire on December 1, 2010. The respondents to rule 30b1-6T are investment companies that are regulated as money market funds under rule 2a-7. Compliance with the rule is mandatory for any money market fund whose market-based NAV is less than \$0.9975. Responses to the disclosure requirements will be kept confidential.

We previously estimated, based on past experience under the Guarantee Program, that at any given time 10 money market funds will be required by rule 30b1-6T to provide weekly reports disclosing certain information regarding the fund's portfolio holdings.⁴⁴⁹ We received no comments on our estimates. We estimate that money market funds will require an average of approximately 6 burden hours to compile and electronically submit the initial required portfolio holdings information, and an average of approximately 4 burden hours in subsequent reports.⁴⁵⁰ Based on these estimates, we estimate the annual burden will be 210 hours per money market fund that is required to provide the information.⁴⁵¹ Based on an estimate of 10 money market funds submitting information under the rule, we estimate that, in the aggregate, rule

⁴⁴⁸ This estimate is based on the following calculation: 719 portfolios × 131 hours = 94,189 hours.

⁴⁴⁹ See Rule 30b1-6T Release, *supra* note 303, at Section V.

⁴⁵⁰ We understand that the required information is currently maintained by money market funds pursuant to other regulatory requirements or in the ordinary course of business. Accordingly, for the purposes of our analysis, we do not ascribe any time to producing the required information.

⁴⁵¹ Because one report is required each week, a fund would submit 52 reports in one year. The first report would require 6 hours and subsequent reports would require 4 hours each. The difference between the hours is due to the fact that funds generally would not incur the additional start-up time applicable to the first report. The burden of the reporting requirement would be 210 hours (1 report × 6 hours = 6 hours, 51 reports × 4 hours = 204 hours, and 6 hours + 204 hours = 210 hours).

30b1-6T will result in 2100 burden hours for all money market funds required to submit portfolio schedules.

V. Cost Benefit Analysis

The Commission is sensitive to the costs and benefits imposed by its rules. We have identified certain costs and benefits of the amendments and new rules. We received comments on the Commission's cost benefit analysis of our proposed amendments to rule 2a-7 and on new rule 30b1-7 and Form N-MFP, which are discussed below. The Commission notes that no comments addressed the Commission's analysis of the costs and benefits associated with the proposed amendments to rule 17a-9 and new rule 22e-3 contained in the Proposing Release. We also received no comments on the cost benefit analysis of rule 30b1-6T. As discussed throughout the release, although there are costs associated with the rules, we think the rules we are adopting will provide significant benefits to the investing public and money market funds. We believe these benefits justify the costs.

A. Rule 2a-7

1. Second Tier Securities, Portfolio Maturity, and Liquidity Requirements

We are adopting several changes to the risk-limiting conditions of rule 2a-7. While we believe that these changes will impart substantial benefits to money market funds, we recognize that they also may also impose certain costs.

First, we are amending rule 2a-7 to further restrict money market funds' exposure to the risks presented by second tier securities. Under the amendments, money market funds will not be permitted to acquire second tier securities unless immediately after their acquisition the money market fund would not have invested (i) more than three percent of its total assets in second tier securities and (ii) more than 0.5 percent of its total assets in second tier securities of any particular issuer.⁴⁵² In addition, money market funds will not be permitted to acquire any second tier security with a remaining maturity in excess of 45 days.⁴⁵³

Second, we are changing rule 2a-7's portfolio maturity limits. We are

⁴⁵² See amended rule 2a-7(c)(3)(ii) (portfolio quality—second tier securities); amended rule 2a-7(a)(27) (defining "total assets"); amended rule 2a-7(c)(4)(i)(C) (portfolio diversification—issuer diversification—second tier securities). We also are proportionately reducing by half the ability of a money market fund to acquire "demand features" or "guarantees" of a single issuer that are second tier securities from 5% to 2.5% of the money market fund's total assets. See amended rule 2a-7(c)(4)(iii)(B) and discussion of our rationale for making this change in note 59 *supra*.

⁴⁵³ See amended rule 2a-7(c)(3)(ii).

reducing the maximum weighted average maturity of a money market fund permitted by rule 2a-7 from 90 days to 60 days.⁴⁵⁴ We also are adopting a new 120-day maturity limitation on the “weighted average life” of fund portfolio securities that will limit the portion of a fund’s portfolio that can be held in longer term floating- or variable-rate securities.⁴⁵⁵ This restriction will require a fund to calculate the weighted average maturity of its portfolio without regard to interest rate reset dates. Finally, we are deleting a provision in rule 2a-7 that permitted money market funds not relying on the amortized cost method of valuation to acquire Government securities with a remaining maturity of up to 762 calendar days.⁴⁵⁶ Under the amended rule, money market funds cannot acquire any security with a remaining maturity of more than 397 days, subject to the maturity shortening provisions for floating- and variable-rate securities and securities with a demand feature.⁴⁵⁷

Third, we are adopting new liquidity requirements for money market funds. In particular, we are amending rule 2a-7 to (i) Require that each money market fund hold securities that are sufficiently liquid to meet reasonably foreseeable shareholder redemptions in light of its obligations under section 22(e) of the Act and any commitments the fund has made to shareholders;⁴⁵⁸ (ii) further limit a money market fund’s investments in illiquid securities (i.e. securities that cannot be sold or disposed of in the ordinary course of business within seven days at approximately the value ascribed to them by the money market fund);⁴⁵⁹ and (iii) require a taxable money market fund to hold at least 10 percent of its total assets in “daily liquid assets” and any money market fund to hold at least 30 percent of its total assets in “weekly liquid assets.”⁴⁶⁰

⁴⁵⁴ See amended rule 2a-7(c)(2)(ii).

⁴⁵⁵ See amended rule 2a-7(c)(2)(iii).

⁴⁵⁶ Compare amended rule 2a-7(c)(2)(i) with current rule 2a-7(c)(2)(ii). In a conforming change, we also are amending the maturity-shortening provision of the rule for variable-rate Government securities to require that the variable rate of interest is readjusted no less frequently than every 397 days, instead of 762 days as previously permitted. See amended rule 2a-7(d)(1).

⁴⁵⁷ See amended rule 2a-7(c)(2)(i); amended rule 2a-7(d)(1)-(5).

⁴⁵⁸ See amended rule 2a-7(c)(5).

⁴⁵⁹ See amended rule 2a-7(c)(5)(i). Under the amended rule, a money market fund cannot acquire illiquid securities if immediately after the acquisition, the fund would have invested more than five percent of its total assets in illiquid securities.

⁴⁶⁰ See amended rule 2a-7(c)(5)(ii)-(iii). See also amended rule 2a-7(a)(8) (defining “daily liquid assets”) and 2a-7(a)(32) (defining “weekly liquid assets”).

a. Benefits

We believe that the amendments to rule 2a-7’s risk-limiting conditions are likely to produce broad benefits for money market fund investors. As discussed in Sections II.A-C above, commenters agreed that the proposed rule 2a-7 amendments concerning second tier securities, maturity, and liquidity would benefit money market funds and their investors.⁴⁶¹ The amendments should reduce money market funds’ exposure to certain credit, interest rate, spread, and liquidity risks. For example, limiting money market funds’ ability to acquire second tier securities will decrease money market funds’ exposure to credit, spread, and liquidity risks. Reducing the maximum weighted average maturity of money market funds’ portfolios will further decrease their interest rate sensitivity. It also will increase their ability to maintain a stable net asset value in the face of multiple shocks to a money market fund, such as a simultaneous widening of spreads and increase in redemptions, such as occurred during the fall of 2008.⁴⁶² Introducing the weighted average life limitation on money market funds’ portfolios will limit credit spread risk and interest rate spread risk to funds from longer term floating- or variable-rate securities. In addition, fund portfolios with a lower WAM and a 120-day maximum WAL will turn over more quickly, and the fund will be better able to increase its holdings of highly liquid securities in the face of illiquid markets than funds operating under a maximum 90-day WAM limitation.

We believe that the new liquidity requirements will decrease liquidity risk. As discussed above, they are designed to increase a money market fund’s ability to withstand illiquid markets by ensuring that the fund further limits its acquisitions of illiquid securities and that a certain percentage of its assets are held in daily and weekly liquid assets.⁴⁶³ Under the general liquidity requirement, moreover, each money market fund must assess its liquidity needs on an ongoing basis and take additional actions as appropriate in order to manage its liquidity. Together, these requirements should decrease the likelihood that a fund would have to realize losses from selling portfolio

⁴⁶¹ See *supra* notes 36-40 and accompanying text; notes 137-139 and accompanying text; notes 159-161 and accompanying text; and notes 184-185 and accompanying text.

⁴⁶² See discussion in Section II.B.1 of this Release for an example of the size of simultaneous shocks that a money market fund could withstand with a WAM of 90 days as opposed to a WAM of 60 days.

⁴⁶³ See *supra* Section II.C.

securities into an illiquid market to satisfy redemption requests, which could put pressure on the fund’s ability to maintain a stable net asset value.⁴⁶⁴ The minimum daily and weekly liquidity standards require a money market fund to hold cash or securities that can be readily converted to cash. In certain circumstances, funds would be required to increase the level of these assets under the general liquidity standard.⁴⁶⁵ We believe that these requirements, rather than our traditional notion of liquidity, which was based on a fund’s ability to find a buyer of a security, are more likely to enable money market fund advisers to meet their funds’ liquidity needs and adjust the funds’ portfolios to increase liquidity when needed.⁴⁶⁶

We believe that a reduction of these credit, interest rate, spread, and liquidity risks will better enable money market funds to weather market turbulence and maintain a stable net asset value per share. The amendments are designed to reduce the risk that a money market fund will break the buck, and thereby prevent losses to fund investors. To the extent that money market funds are more stable, they also will reduce systemic risk to the capital markets and provide a more stable source of financing for issuers of short-term credit instruments, thus promoting capital formation. If money market funds become more stable investments as a result of the rule amendments, they may attract further investment, increasing their role as a source of capital.

b. Costs

We recognize that our amendments regarding second tier securities, portfolio maturity, and liquidity will impose costs on some money market funds. For example, yields might decrease in funds depending on their current positions in second tier securities, less liquid securities, and longer term instruments because those instruments typically offer above average yields. We note that the yield offered by a security is tied to its risk. It is important to consider our rule amendments’ impact on money market fund yields in this context.

Second Tier Securities. We received several comments on the estimated costs of eliminating money market funds’ ability to acquire second tier securities. One commenter stated that such an elimination would cost a money market fund 2 basis points in yield, assuming

⁴⁶⁴ See *id.*

⁴⁶⁵ See *supra* Section II.C.1.

⁴⁶⁶ See *supra* Section II.C.

that this money market fund held 5 percent of its assets in second tier securities.⁴⁶⁷ This commenter stated that it believed that this cost would be appropriate to strengthen the stability of money market funds to weather potential future liquidity and credit crises and to promote investor confidence. Several commenters agreed, stating that they did not expect elimination to lead to market disruption.⁴⁶⁸ One commenter added that given the small size of the second tier securities market, the benefits of elimination would far outweigh any disadvantages.⁴⁶⁹

Another commenter stated that the benefits of money market funds being able to invest in second tier securities, in terms of reducing portfolio concentration in financial institution securities and providing affordable financing for second tier security issuers, outweigh any potential increased credit risk.⁴⁷⁰ This commenter estimated that elimination of a money market fund's ability to acquire second tier securities would cost it 3 basis points in yield, again assuming that the money market fund held a full 5 percent of its assets in second tier securities. Finally, a third commenter estimated that elimination of money market funds' ability to acquire second tier securities would cost a retail money market fund 4–8 basis points in yield, a non-rated institutional money market fund 2–4 basis points in yield, and a rated institutional fund 1–3 basis points in yield.⁴⁷¹ This commenter assumed that

⁴⁶⁷ This number was obtained in discussions with a commenter clarifying certain aspects of its comment letter. See J.P. Morgan Asset Mgt. Comment Letter.

⁴⁶⁸ ICI Comment Letter; TDAM Comment Letter; Thrivent Comment Letter.

⁴⁶⁹ TDAM Comment Letter.

⁴⁷⁰ See Federated Comment Letter. As discussed in Section II.A.1 of this Release, other commenters also asserted that a complete ban on acquisition of second tier securities would not be justified on a cost-benefit basis, would have a material adverse impact on second tier security issuers, would have unintended effects on the capital markets, and would increase borrowing costs for second tier security issuers. We discuss these comments, and provide our response, *supra* notes 41–53 and accompanying and following text.

⁴⁷¹ Fidelity Comment Letter. According to the iMoneyNet Money Market Fund Analyzer Database, as of November 17, 2009, 61% of money market fund assets were held in funds that were top rated by at least one NRSRO and 34% of money market funds had a top rating from at least one NRSRO. In order to retain a top rating, money market funds must only hold first tier securities. According to analysis of the iMoneyNet analyzer database, as of December 1, 2009, approximately 48% of money market funds were retail funds and 52% were institutional funds. Accordingly, Fidelity's estimates result in a blended impact on money market funds of (6 basis points × 48% retail funds) + (3 basis points × 34% non-rated institutional

these money market funds held 5 percent of their assets in second tier securities and 5 percent of their assets in lower quality first tier assets, and that all of these assets would not be held if funds' ability to acquire second tier securities was eliminated.

As discussed above, we have determined not to eliminate money market funds' ability to acquire second tier securities, but instead are further restricting this ability. This change from our proposal should result in costs that are less than estimated in the proposal and less than commenters estimated for full-scale elimination. We believe that the 3 percent limitation on money market funds' ability to acquire second tier securities will have a small impact on money market funds.⁴⁷² Based on commenters' estimates described above, a reduction in a money market fund's investment in second tier securities from 5 percent to 3 percent of its total assets would reduce its yield on average by approximately 1.2 basis points.⁴⁷³ However, very few money market funds hold more than 3 percent of their total assets in second tier securities, and even fewer hold a full 5 percent. Our staff's review of money market fund portfolios in September 2008 found that only 4 percent of money market funds held more than 3 percent of their assets in second tier securities. Accordingly, we estimate that each of only 29 money market funds⁴⁷⁴ would face a reduction of yield of 1.2 basis points as a result of our amendments.

We also are further reducing the ability of money market funds to acquire second tier securities of any particular issuer from the greater of 1 percent of assets or \$1 million to 0.5 percent of assets. Based on our staff's review of money market fund portfolios in September 2008, 8 percent of money market funds held second tier securities of any particular issuer in excess of 0.5 percent of the money market fund's assets. We expect that these money market funds, however, will simply reinvest this excess in the securities of other second tier issuers and, therefore,

funds) + (2 basis points × 18% rated institutional funds) = 4.3 basis points per fund.

⁴⁷² As discussed above, we do not believe that further limitations on money market funds' ability to acquire second tier securities will prevent their ability to achieve diversification benefits. See *supra* note 47 and accompanying text.

⁴⁷³ This estimate is based on averaging the 2 basis point, 3 basis point, and 4.3 basis point estimates from commenters for a reduction in second tier securities investment from 5% to 0%, proportionately adjusted to reflect a reduction in investment from 5% to 3%.

⁴⁷⁴ This estimate is based on the following calculation: 719 money market funds × 4% = 29 money market funds.

that there will be no loss in fund yield as a result of this restriction.⁴⁷⁵ Several commenters argued that there are many second tier security issuers worthy of investment.⁴⁷⁶ If any of these money market funds did not perform credit analysis of a large enough group of second tier security issuers, these funds may incur some administrative costs in tracking additional issuers.⁴⁷⁷

Finally, we are limiting money market funds to only acquiring second tier securities with a remaining maturity of less than 45 days. According to Federal Reserve data, in 2009, only 4 percent of A2/P2 non-financial commercial paper had a maturity of greater than 40 days on issuance, and thus we do not expect that the 45-day maturity limit will have more than a negligible cost impact on taxable money market funds.⁴⁷⁸ In addition, based on our staff's review of tax-free money market fund portfolios in September 2008, we estimate that very few money market funds held second tier municipal securities with a maturity of greater than 45 days that were second tier securities at the time of acquisition. As a result, we do not expect that the 45-day maturity limit will have more than a negligible cost impact on money market funds.

WAM and WAL. Three commenters provided cost estimates for a reduction in the maximum weighted average maturity for money market funds. One commenter estimated that if all money market funds had a WAM of 75 days and reduced their WAM to 60 days, it would cost each money market fund 2.5 to 3 basis points in yield.⁴⁷⁹ Similarly, another commenter estimated that this same reduction would cost each money market fund 3 basis points in yield, and a reduction in WAM from 90 days to 75

⁴⁷⁵ Commenters (for example, the Federated Comment Letter and the Fidelity Comment Letter) asserted that there are numerous quality second tier security issuers. Because this limitation, when combined with the 3% aggregate limitation on acquisition of second tier securities, only limits money market funds to holding a minimum of 6 second tier issuers if it were to maximize the limitations (rather than 5 second tier issuers under the current rule), we do not expect that money market funds would have difficulty finding six appropriate second tier security issuers in which to invest.

⁴⁷⁶ See, e.g., Chamber/Tier 2 Issuers Comment Letter; Federated Comment Letter; Fidelity Comment Letter; USAA Comment Letter.

⁴⁷⁷ Based on discussions we had with certain commenters clarifying certain aspects of their comment letters, we understand that all of these larger managers track sufficient second tier security issuers that the 0.5% limitation per second tier security issuer should not create additional costs related to tracking additional issuers.

⁴⁷⁸ See Federal Reserve, *Volume Statistics for Commercial Paper, A2/P2 Nonfinancial*, available at <http://www.federalreserve.gov/releases/cp/volumestats.htm>.

⁴⁷⁹ J.P. Morgan Asset Mgt. Comment Letter.

days would also cost a money market fund 3 basis points in yield.⁴⁸⁰ Finally, a third commenter estimated that if all money market funds had a WAM of 90 days and reduced their WAM to 60 days, it would cost each money market fund 5 to 10 basis points in yield.⁴⁸¹ According to these estimates, it would cost a money market fund 5 to 10 basis points in yield to reduce its WAM from 90 days to 60 days.

However, historically most money market funds have not maintained a WAM of more than 60 days. According to data provided by the ICI, from January 1998 through April 2009, even the 75th percentile of prime money market funds has maintained an average WAM of 53 days and the 90th percentile of prime money market funds has maintained an average WAM of 65 days.⁴⁸² As of November 17, 2009, despite the historically low interest rate environment in which money market funds have tended to extend WAM closer to the maximum limits to gain additional yield, only 1.5 percent of taxable money market funds reported a WAM of more than 75 days (with most of those having a WAM of only slightly over 75 days) and only 15.5 percent reported a WAM of 61–75 days (with these funds having an average WAM of 68 days).⁴⁸³ We understand that most money market funds like to have some cushion by maintaining a WAM below the permitted maximum, but we do not believe that money market funds believe that such a large cushion must always be maintained. Rather, we believe that many money market funds have maintained lower WAMs than required because they believed that it is prudent management of their portfolio to do so.⁴⁸⁴

Based on this data, on the WAMs of taxable and prime money market funds and on commenters' estimates of the impact of a reduction in WAM, we estimate that 10 money market funds will have to reduce their WAM from 78 days to 55 days at a cost of 6 basis points per fund. We further estimate that 70 money market funds will have

to reduce their WAM from 68 days to 55 days at a cost of 2 basis points per fund.

Three commenters provided cost estimates for a reduction in the maximum weighted average life for money market funds. One commenter estimated that if all money market funds had a WAL of 180 days and reduced their WAL to 120 days, it would cost each money market fund 2 to 4 basis points in yield.⁴⁸⁵ Another commenter estimated that a WAL reduction of 150 to 120 days would cost each money market fund 1 to 3 basis points in yield.⁴⁸⁶ Finally, a third commenter estimated that if all money market funds reduced their WAL to 120 days, it would cost each money market fund 3 basis points in yield.⁴⁸⁷ According to these estimates, it would cost a money market fund 1 to 3 basis points in yield to reduce its WAL from 150 days to 120 days.⁴⁸⁸ We estimate that two-thirds of taxable money market funds and all tax-free money market funds already maintain a WAL of 120 days or less and thus will incur no cost in transitioning to this amendment to rule 2a–7.⁴⁸⁹ We

⁴⁸⁵ J.P. Morgan Asset Mgt. Comment Letter and subsequent Commission staff conversation with J.P. Morgan staff breaking down the cost estimate in the J.P. Morgan Asset Mgt. Comment Letter by each proposed amendment to rule 2a–7.

⁴⁸⁶ Fidelity Comment Letter (focusing on government money market funds).

⁴⁸⁷ Federated Comment Letter. The Federated Comment Letter did not specify a WAL starting point for its assumed reduction to a 120-day WAL. Rather, it evaluated instruments that it believed would likely be subject to greater demand or a shorter maturity with a 120-day maximum WAL requirement and estimated the increased cost to money market funds from those securities becoming more expensive as a result.

⁴⁸⁸ Based on discussions we had with certain commenters clarifying certain aspects of their comment letters, we do not believe that more than a negligible number of money market funds are maintaining a WAL of 180 days.

⁴⁸⁹ We are not aware of any data provider that tracks the WAL of all money market funds (likely because money market funds are not limited currently in the weighted average life that they must maintain). An analysis of the 16 largest, top-rated, prime institutional money market funds (representing 53% of all prime institutional money market fund assets as of June 30, 2009) found that of the 14 funds providing information on the final maturities of their portfolio securities, all had a WAL of under 120 days. See Capital Advisors Group, *How Safe are Prime Money Market Funds?* (Nov. 1, 2009), available at <http://web.capitaladvisors.com/whitepapers/How%20Safe%20Are%20MMFs.pdf> (“CAG Report”). This information, combined with discussions we had with certain commenters clarifying certain aspects of their comment letters, leads us to estimate that two thirds of money market funds currently are maintaining a WAL of no greater than 120 days and that the other third currently are maintaining a WAL of no greater than 150 days. We also understand that the majority of money market funds currently are in compliance with the maximum 120-day WAL because of their voluntary compliance with the recommendations contained in the ICI Report. Because most securities held by tax-free money market funds have a demand feature

estimate that the other third of taxable money market funds, or 163 funds, maintain a maximum WAL of no greater than 150 days and will incur on average a cost of 2 basis points per fund to reduce their WAL to 120 days.

Several commenters stated that the new WAM limitation would reduce the range of securities available for money market fund investment and increase demand for shorter term securities.⁴⁹⁰ No commenters provided any cost estimate for this potential impact. If this did occur, and if the increased demand was not met with increased supply of such securities, the new maturity limitations could result in additional incremental costs to money market funds.

A few commenters also believed that the amended maturity limitations would increase security issuer costs because they would have to issue shorter maturity securities and assume greater risk from having to roll over their securities more frequently.⁴⁹¹ No commenters provided any cost estimate for this potential impact. If security issuer costs do increase as a result of the amended maturity limitations and these issuers as a consequence are unable to obtain the same amount of financing, it may have a negative impact on capital formation.

General Liquidity Requirement. As discussed above, the amended rule includes a general liquidity requirement, under which a fund's management and its board must evaluate the funds' liquidity needs and protect shareholders from the harm that can occur from the failure to properly anticipate and provide for those needs. We also noted that in order to comply with this provision in amended rule 2a–7 under the compliance rule, we expect that money market funds would adopt policies and procedures designed to assure that appropriate efforts are undertaken to identify risk characteristics of the fund's shareholders.⁴⁹² For purposes of the PRA analysis, we estimated that each fund complex would incur, on average, 9 hours to document, review, and adopt policies and procedures for monitoring the risk characteristics of money market

reducing the security's maturity under the WAL calculation to a very short duration, we understand that tax-free money market funds do not have a WAL greater than 120 days.

⁴⁹⁰ See, e.g., Charles Schwab Comment Letter; J.P. Morgan Asset Mgt. Comment Letter; State Street Comment Letter.

⁴⁹¹ See, e.g., Fannie Mae Comment Letter; State Street Comment Letter; Wells Fargo Comment Letter.

⁴⁹² See *supra* note 198 and accompanying text.

⁴⁸⁰ Federated Comment Letter.

⁴⁸¹ Fidelity Comment Letter.

⁴⁸² Investment Company Institute, *Average Maturity of Taxable Prime Money Market Funds, 1998–2009*, available at <http://www.sec.gov/comments/s7-11-09/s71109-14.htm>.

⁴⁸³ Based on data from the iMoneyNet Money Market Fund Analyzer Database as of November 17, 2009. The WAMs of the funds with WAMs over 75 days were: 2 at 76 days, 1 at 77 days, and 3 at 78 days. Tax-free money market funds have WAMs considerably lower (30% of money market funds were tax-free as of December 8, 2009 according to data from the iMoneyNet Money Market Fund Analyzer Database).

⁴⁸⁴ See, e.g., *supra* notes 137–139 and accompanying text.

fund investors.⁴⁹³ Based on this estimate, we estimate that it would cost a fund complex \$6976 to document, review, and adopt these policies and procedures, for a total cost of \$1,137,000.⁴⁹⁴

Illiquid Securities. Two commenters provided estimates with respect to the proposed ban on purchases of illiquid securities. One commenter estimated that the proposed ban would decrease

money market funds' yields from 2 to 6 basis points, assuming that the fund holds 10 percent of its total assets in illiquid securities.⁴⁹⁵ Another commenter submitted that the ban on illiquid securities would decrease yields by 3 basis points.⁴⁹⁶ Based on commenters' estimates, a money market fund that reduces its investments in illiquid securities from 10 percent to 5

percent would reduce its yield on average by 2 basis points.⁴⁹⁷

Our staff's review of money market funds' portfolios in September 2008 found that 24 percent of funds reported held any illiquid securities.⁴⁹⁸ Based on the staff's review as applied to the current number of money market funds (719),⁴⁹⁹ we estimate current money market fund holdings of illiquid securities as follows:

Percentage of total assets represented by illiquid securities	Percentage of funds	Number of funds
10 percent	0.6	4
9 percent	0.4	3
8 percent	0.4	3
7 percent	0.4	3
6 percent	1.0	7
5 percent or less	97.2	698

Based on these estimated holdings, staff makes the following estimates: 4 funds with 10 percent of assets invested in illiquid securities will experience a reduction in holdings of 5 percent and a yield impact of 2 basis points;⁵⁰⁰ 3 funds with 9 percent of assets invested in illiquid securities holdings will experience a reduction in holdings of 4 percent and a yield impact of 1.6 basis points;⁵⁰¹ 3 funds with 8 percent of assets invested in illiquid securities holdings will experience a reduction in holdings of 3 percent and a yield impact of 1.2 basis points;⁵⁰² 3 funds with 7 percent of assets invested in illiquid securities holdings will experience a reduction in holdings of 2 percent and a yield impact of 0.8 basis points;⁵⁰³ 7 funds with 6 percent of assets invested in illiquid securities holdings will experience a reduction in holdings of 1

percent and a yield impact of 0.4 basis points.⁵⁰⁴

Daily Liquidity Requirements. Two commenters specifically addressed the proposed daily liquidity requirements. Both commenters estimated that there would be no yield impact as a result of the proposed 10 percent threshold.⁵⁰⁵ Based on these comments, we assume that the 10 percent daily minimum liquidity standard we are adopting will have no impact on money market funds' yield.⁵⁰⁶

Weekly Liquidity Requirements. A few commenters provided estimates on the costs of the proposed weekly liquidity requirements. One commenter estimated that the yield impact of the proposed 30 percent weekly liquidity standard for institutional funds would range from 15 to 20 basis points,⁵⁰⁷ while another commenter estimated that the yield impact would be 10 basis points.⁵⁰⁸ A

third commenter submitted that the proposed 30 percent weekly liquidity requirement would have a yield impact of 9 basis points, but would have no impact if the threshold was 20 percent and included agency discount notes with remaining maturities of 95 days or less.⁵⁰⁹ None of these commenters explained the baseline (*i.e.*, the percentage of weekly liquid assets institutional funds currently hold) on which their estimated impacts on yield are based. A fourth commenter estimated that if money market funds had to increase their weekly liquid assets by 10 percent, the yield impact would be between 3 and 6 basis points.⁵¹⁰ Thus, commenters' estimates of the yield impact to institutional funds of maintaining 30 percent of their portfolio in weekly liquid assets ranged

⁴⁹³ See *supra* note 407 and accompanying and preceding text.

⁴⁹⁴ These estimates are based on the following calculations: 8 hours × \$372/hour (for a senior portfolio manager) = \$2976; 1 hour × \$4000 (for a board of directors) = \$4000; (\$2976 + \$4000) × 163 complexes = \$1,137,088. The hourly wage used for senior portfolio managers is from the SIFMA *Report on Management & Professional Salaries Data* (Sept. 2008), modified to account for an 1800-hour work-year and multiplied by 5.35 to account for bonuses, firm size, employee benefits, and overhead.

⁴⁹⁵ See Fidelity Comment Letter.

⁴⁹⁶ See Federated Comment Letter (without specifying the assumed holdings of illiquid securities).

⁴⁹⁷ The individual reduction in basis points is calculated by taking the average of the estimated range of 2 to 6 basis points ((2+6) ÷ 2 = 4 basis points; 4 basis points ÷ 10% = 0.4 basis points per 1% reduction), proportionally adjusted to reflect an adjustment in investment in illiquid securities from 10% to 5% (5 × 0.4 = 2).

⁴⁹⁸ We note that these holdings are likely to include some securities that were not illiquid at acquisition. Thus, our estimates on the impact of reducing holdings of illiquid securities may be

higher than the impact that would be experienced by some money market funds.

⁴⁹⁹ The number of money market funds is based on Investment Company Institute, *Trends in Mutual Fund Investing*, Oct. 2009, available at http://www.ici.org/research/stats/trends/trends_10_09.

⁵⁰⁰ (10% - 5% (allowable amount remaining) = 5%). 5 × 0.4 basis points (basis point impact per 1%) = 2 basis points.

⁵⁰¹ (9% - 5% (allowable amount remaining) = 4%). 4 × 0.4 basis points = 1.6 basis points.

⁵⁰² (8% - 5% (allowable amount remaining) = 3%). 3 × 0.4 basis points = 1.2 basis points.

⁵⁰³ (7% - 5% (allowable amount remaining) = 2%). 2 × 0.4 basis points = 0.8 basis points.

⁵⁰⁴ (6% - 5% (allowable amount remaining) = 1%). 1 × 0.4 basis points = 0.4 basis points.

⁵⁰⁵ See Federated Comment Letter; Fidelity Comment Letter.

⁵⁰⁶ Our understanding is that money market funds' current practice is to maintain approximately 10% of their portfolio in daily liquid assets. See CAG Report, *supra* note 489; Fitch Report, *supra* note 274, at 6 (Fitch-rated prime money market funds' aggregate exposure to sources of overnight liquidity, including repurchase agreements, time

deposits and shares of other money market funds, was approximately 15% of total assets for the six-month period ended on May 15, 2009).

⁵⁰⁷ See Fidelity Comment Letter (noting that including agency discount notes with remaining maturities of 397 days or less in weekly liquid assets would have reduced this estimate by about 3 basis points for institutional money market funds).

⁵⁰⁸ GE Asset Mgt. Comment Letter (arguing that the requirement could cause a more pronounced yield widening effect as a result of supply/demand dynamics, *i.e.*, there would be an increase in demand for securities with 7-day maturities or less, which would result in a corresponding decrease in yield for such instruments; consequently, there could also be a reduced demand for longer-dated instruments, which would adversely impact the short-term financing for issuers of such instruments).

⁵⁰⁹ Federated Comment Letter.

⁵¹⁰ J.P. Morgan Asset Mgt. Comment Letter and subsequent Commission staff conversation with J.P. Morgan staff breaking down the cost estimate in the J.P. Morgan Asset Mgt. Comment Letter by each proposed amendment to rule 2a-7.

from 3 to 20 basis points.⁵¹¹ We have averaged these estimates to determine our estimated yield impact on institutional funds of 1.025 basis points per percentage increase in existing assets that would have to be converted to weekly liquid assets.⁵¹²

We estimate that half of institutional money market funds currently maintain 30 percent or more of their total assets in weekly liquid assets and thus would experience no reduction in yield as a result of the weekly liquidity requirement. We further estimate that 38 percent of institutional funds maintain 25 percent of their assets in weekly liquid assets; 6 percent of institutional funds maintain 20 percent of their assets in weekly liquid assets and 6 percent of institutional funds maintain 15 percent of their assets in weekly liquid assets.⁵¹³ Based on these estimates, we estimate that 187 funds may experience no impact, 142 funds may experience a 5.125 basis point impact on yield, 22 funds may experience a 10.25 basis points, and 22 funds may experience a 15.375 basis point impact on yield.⁵¹⁴

One commenter provided specific estimates for the impact of the proposed 15 percent weekly liquid asset requirement on retail money market funds of between two and four basis points.⁵¹⁵ Assuming that the starting point for these estimates was 10 percent of investments in weekly liquid assets, we estimate that the yield impact per percentage increase to satisfy the weekly

liquid asset requirement would be 0.6 basis points.⁵¹⁶ We estimate that all retail money market funds maintain 15 percent of their total assets in weekly liquid assets.⁵¹⁷ Based on this estimate, we estimate that the average yield impact for each retail money market fund would be 9 basis points.⁵¹⁸

Investors. The decreased yield that some money market funds may offer as a result of the amendments we are adopting today may limit the range of choices that individual money market fund investors have to select their desired level of investment risk. This might cause some investors to shift their assets to, among other places, bank deposits or offshore or other enhanced cash funds unregulated by rule 2a–7 that are able to offer a higher yield.⁵¹⁹ Investors that choose to move to unregulated products may have fewer protections than they had in money market funds regulated under rule 2a–7. When markets come under stress, investors may be more likely to withdraw their money from these offshore or private funds due to their perceived higher risk⁵²⁰ and substantial redemptions from those funds and accompanying sales of their portfolio securities could increase systemic risk to short-term credit markets, which would impact money market funds. In addition, the stricter portfolio quality, maturity, and liquidity requirements may result in some money market funds having fewer issuers from which to select securities if some issuers only offer second tier securities, less liquid

securities, or a larger percentage of longer term securities.

Issuers. Our new portfolio quality, maturity, and liquidity restrictions also may impact issuers. Issuers may experience increased financing costs to the extent that they are unable to find alternative purchasers at previous market rates of second tier securities, less liquid securities, longer term securities, or adjustable-rate securities that money market funds determine to no longer acquire because of the new restrictions. Several commenters stated that elimination of money market funds' ability to acquire second tier securities would increase issuers' borrowing costs and thus could increase the cost of capital formation.⁵²¹ No commenters provided estimates of such costs.

As noted earlier in this section, we do not believe that money market funds currently hold a significant amount of second tier securities or securities that are illiquid at acquisition in excess of the newly adopted limitations for these securities. Thus, we expect that the amendments' impact on issuers of these securities will be minimal. We also know that few money market funds maintain a WAM in excess of 60 days, and we therefore believe that our new WAM restriction will not have a significant impact on issuers of longer term securities.⁵²² To the extent that the new WAM limitation results in companies or governments issuing shorter maturity securities, those issuers may be exposed to an increased risk of insufficient demand for their securities and adverse credit market conditions because they must roll over their short-term financing more frequently. We note that this impact could be mitigated if money market funds sufficiently staggered or "laddered" the maturity of the securities in their portfolios.

Finally, we estimate that one third of taxable money market funds will have to reduce the WAL of their portfolio,⁵²³ and thus it is possible that some adjustable-rate security issuers will need to shorten the maturities of some of the securities they offer, which may result in increased borrowing costs.⁵²⁴ In addition, the markets for longer term securities may become less liquid if the

⁵¹¹ We note that the range of these estimates is likely to be lower if agency discount notes with remaining maturities of less than 60 days are included. We have not adjusted for that, however, to maintain a conservative estimate.

⁵¹² Our estimate is based on an average of the commenters' estimated (or the midpoint of commenters' estimated) impacts of 17.5, 10, 9, and 4.5 basis points per 10% increase in weekly liquid assets as proportionally adjusted: $1.75 + 1.0 + 0.9 + 0.45 = 4.1$; $4.1 \text{ basis points} \div 4 = 1.025 \text{ basis point increase}$. See notes 507–510 and accompanying text.

⁵¹³ While we are not aware of any data provider that tracks the actual maturities of securities (as opposed to WAM, which estimates the maturity of floating rate notes based on the interest reset date rather than actual maturity), we are able to provide estimates based on the analysis of the Capital Advisors Group that found that on or near September 30, 2009, the 16 funds providing information on their portfolio securities averaged 30% of assets in securities convertible to cash in 1 to 7 days. In addition, 8 (50%) had 7-day liquidity of 30% or greater; 6 (38%) had 7-day liquidity of 25%–30%; 1 (6%) had liquidity of 20%–25%, and 1 (6%) had 7-day liquidity of 15%–20%. See CAG Report, *supra* note 489. For purposes of our estimates, we are assuming the funds in each category held the lowest level of weekly liquid assets in the category.

⁵¹⁴ As noted above, there are currently 719 money market funds, of which we estimate that 52% (374) are institutional funds. See *supra* notes 471 and 499.

⁵¹⁵ See Fidelity Comment Letter.

⁵¹⁶ This assumes an average of 3 basis points proportionally adjusted for an increase of 5%. We assume that the commenter based its estimate on an increase from 10% holdings because as noted above, we assume that all money market funds have on average daily liquidity of at least 10% and the commenter based its estimates on the proposed weekly liquid asset requirement of 15% for retail funds. See *supra* note 506 and accompanying text.

⁵¹⁷ We believe that most retail money market funds currently are in voluntary compliance with the 20% weekly liquidity standard recommended by the ICI Report, which would include agency discount notes with original issue maturity of 95 days or less. The final rule permits agency discount notes with remaining maturities of 60 days or less, and we are conservatively estimating that retail funds maintain an average of 15% of assets in weekly liquid assets.

⁵¹⁸ $0.6 \text{ basis points} \times 15\% = 9 \text{ basis points}$. This estimate may be overstated because, as noted above, we believe that most retail funds hold 20% of their assets in weekly liquid assets, and thus would have to convert a smaller percentage of assets to weekly liquid assets.

⁵¹⁹ Some commenters suggested this possibility. See, e.g., Goldman Sachs Comment Letter; State Street Comment Letter (making this comment with respect to reducing the maximum permissible WAM).

⁵²⁰ During the market events of 2007–2008, investors redeemed substantial amounts of assets from certain bond funds and offshore money market funds. See ICI Report, *supra* note 14, at 106–07.

⁵²¹ See, e.g., Am. Elec. P. Comment Letter; Chamber/Tier 2 Issuers Comment Letter. But see ICI Comment Letter (stating their belief that elimination would have a manageable impact on second tier security issuers).

⁵²² See *supra* notes 482–483 and accompanying text.

⁵²³ See *supra* note 489 and accompanying and following text.

⁵²⁴ See *supra* note 491 and accompanying text for comments asserting this possible negative impact.

rule amendments cause issuance of these instruments to decline.⁵²⁵

Government Securities. We do not believe that eliminating the provision in rule 2a-7 that allowed money market funds relying solely on the penny-rounding method of pricing to hold Government securities with remaining maturities of up to 762 days will have a material impact on money market funds, investors, or issuers of longer term Government securities because we believe that substantially all money market funds rely on the amortized cost method of valuation, and not exclusively on the penny-rounding method of pricing, and thus are not eligible to rely on this exception. We received one comment on this proposal, which stated that they were not aware of any money market funds that relied on the penny rounding method of pricing.⁵²⁶

2. Designation of NRSROs

The amendments to rule 2a-7 require a money market fund's board of directors to designate at least four NRSROs whose credit ratings the fund will use in determining the eligibility of portfolio securities under the rule and that the board determines annually issue credit ratings that are sufficiently reliable for this use.⁵²⁷ In addition, money market funds are required to disclose designated NRSROs in their registration statements.⁵²⁸

We anticipate that the requirement to designate at least four NRSROs could foster competition among NRSROs to produce the most accurate ratings in order to obtain designation by money market fund boards. Several commenters agreed that designating at least three NRSROs could encourage competition among NRSROs to achieve designation by money market fund boards.⁵²⁹ To the extent that competition increases the reliability of the credit ratings of designated NRSROs, this could increase the efficiency of fund managers in determining eligibility of portfolio securities. Some commenters expressed concern, however, that a requirement to designate at least three NRSROs could result in fund boards designating only the three largest NRSROs that issue

most of the ratings,⁵³⁰ which could result in decreased competition among NRSROs. To address this concern, in light of the Commission's goal of increasing competition among NRSROs, we are requiring each fund to designate at least four NRSROs. In addition, requiring designation of four NRSROs may encourage new NRSROs that issue ratings specifically for money market fund instruments to enter the market.

We recognize that the requirement to designate and annually evaluate at least four NRSROs will result in costs to the fund.⁵³¹ For the purposes of the PRA, we estimate that the requirement that money market funds disclose this designation, including any limitations on the use of the designations, in their SAIs will not result in additional costs for funds.⁵³² We expect that boards will designate NRSROs based on recommendations from the fund's adviser and its credit analysts. Similarly, we believe the board's annual determination regarding designated NRSROs will be based on recommendations from the adviser and its credit analysts. Staff estimates that it will take each fund's board of directors approximately 6 hours each year to designate NRSROs and determine whether the NRSROs ratings are sufficiently reliable for such use. Based on an hourly rate for the board of \$4000, we estimate that each money market fund will incur \$24,000 and all fund complexes will incur \$3.9 million annually for the boards of directors to initially designate and determine the reliability and sufficiency of the designated NRSROs' credit ratings for use in determining eligibility of portfolio securities.⁵³³

We expect that fund advisers currently evaluate the reliability of NRSRO ratings and ratings criteria as part of the credit analysis they perform (under delegated authority from the board) in determining the eligibility of

⁵³⁰ See DBRS Comment Letter; C. Wesselkamper Comment Letter. We note that of the 10 registered NRSROs, three issued over 97% of the ratings across categories that NRSROs reported to the Commission. See SEC, *Annual Report on Nationally Recognized Statistical Rating Organizations* at 9 (Sept. 2009).

⁵³¹ While we received comments regarding the designation of NRSROs, none of the comments discussed the costs of designation to funds or their advisers.

⁵³² See *supra* Section IV.A.1.

⁵³³ This estimate is based on the following calculation: \$24,000 × 163 (fund complexes) = \$3,912,000. We have estimated total costs for fund complexes because we assume that boards of directors will undertake to designate and determine for all funds in the complex at the same time (although boards may designate and make annual determinations with respect to different NRSROs for different money market funds).

portfolio securities. We also assume that this evaluation includes consideration and internal documentation of whether an NRSRO's rating is sufficient for that use. Accordingly, while we do not anticipate that fund advisers will incur additional time to prepare their recommendations, we expect that fund advisers will incur costs to draft those recommendations in a presentation or report for board review regarding designation of NRSROs and the sufficiency of designated NRSROs' ratings. Staff estimates that the investment adviser for each complex will spend 6 hours annually to prepare a report based on the adviser's internal review and documentation that summarizes its recommendation with respect to each NRSRO that may be considered for designation and any limits on the use of that NRSRO under the rule at a cost per fund complex of \$1770 and a total cost of \$288,510.⁵³⁴

As noted above, we understand that money market fund advisers currently evaluate NRSROs that rate securities in which the fund invests. We also understand that fund advisers monitor NRSROs for potential downgrades of portfolio securities. Prior to today's amendments, if the fund invested in unrated or second tier securities, the adviser had to monitor all NRSROs in case there was a downgrade of a second tier security or an unrated security received a rating below one of the top two categories.⁵³⁵ Thus, we do not expect that limiting the number of NRSROs that a fund must monitor to four (or more, if the fund chooses) will result in increased costs to fund advisers to monitor NRSROs.

3. Stress Testing

As proposed, we are amending rule 2a-7 to require that a money market fund's board of directors adopt written procedures that provide for the periodic stress testing of each money market fund's portfolio.⁵³⁶ A fund's board of directors determines the frequency of stress testing. The procedures must require testing of the fund's ability to

⁵³⁴ These estimates are based on the following calculations: (\$202/hour (intermediate portfolio manager) × 3 hours) + (\$388/hour (senior portfolio manager) × 3 hours) = \$1770; \$1770 × 163 fund complexes = \$288,510. Hourly wages used for purposes of the estimate of portfolio manager salaries are from the SIFMA *Report on Management & Professional Salaries Data* (Sept. 2008), modified to account for an 1800-hour work-year and multiplied by 2.93 to account for bonuses, firm size, employee benefits and overhead.

⁵³⁵ See current rule 2a-7(c)(6)(i)(A)(2).

⁵³⁶ See *supra* Section II.C.4. We did not receive any comment on the estimates and assumptions included in our proposal. Accordingly, we have not modified any of those estimates except to reflect the new requirement included in the amended rule.

⁵²⁵ No commenters addressed this possibility.

⁵²⁶ BlackRock Comment Letter.

⁵²⁷ Amended rule 2a-7(a)(11) (defining the term "designated NRSRO").

⁵²⁸ Amended rule 2a-7(a)(11)(iii). The fund would be required to make the disclosure in its SAI under Part B of Form N-1A [17 CFR 239.15A].

⁵²⁹ See, e.g., HighMark Capital Comment Letter; Invesco Aim Comment Letter.

maintain a stable net asset value per share based upon certain hypothetical events.⁵³⁷ The procedures also must provide for a report to be delivered to the fund's board of directors at its next regularly scheduled meeting on the results of the testing, or more often as appropriate in light of the results.⁵³⁸ The report must include 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.⁵³⁹

We anticipate that stress testing will give fund advisers a better understanding of the effect of potential market events and shareholder redemptions on their funds' ability to maintain a stable net asset value, the funds' exposure to the risk that they would break the buck, and actions the advisers may need to take to mitigate the possibility of the funds breaking the buck.⁵⁴⁰ We believe that many funds currently conduct stress testing as a matter of routine fund management and business practice.⁵⁴¹ We anticipate, however, that funds that do not currently perform stress testing and funds that may revise their procedures in light of the amended rule will give their managers a tool to better manage those risks. For fund boards of directors that do not currently receive stress test results, we believe that the regular reports of the testing and assessments will provide money market fund boards a better understanding of the risks to which the fund is exposed.

We understand that today rigorous stress testing is a best practice followed by many money market funds.⁵⁴² We understand that the fund complexes that conduct stress tests include smaller complexes that offer money market funds externally managed by advisers experienced in this area of

management.⁵⁴³ Accordingly, staff estimates that as a result of the new requirement to adopt stress testing procedures: (i) Funds that currently conduct rigorous stress testing, including tests for hypothetical events listed in the amended rule (and concurrent occurrences of those events), will incur some costs to evaluate whether their current test procedures comply with the new requirement, but will be likely to incur relatively few costs to revise those procedures or continue the stress testing they currently perform; (ii) funds that conduct less rigorous stress testing, or that do not test for all the hypothetical events listed in the amended rule, will incur somewhat greater expenses to revise those procedures in light of the new requirement and maintain the revised testing; and (iii) funds that do not conduct stress testing will incur costs to develop and adopt stress test procedures and conduct stress tests.

As noted above, we believe that there is a range in the extent and rigor of stress testing currently performed by money market funds. We also expect that stress test procedures are being or will be developed by the adviser to a fund complex for all money market funds in the complex, while specific stress tests are performed for each individual money market fund. We estimate that a fund complex that currently does not conduct stress testing will require approximately 1 month for 2 risk management specialists and 2 systems analysts to develop stress test procedures at a cost of approximately \$155,000, 22 hours for a risk management specialist to draft the procedures, and 3 hours of board of directors' time to adopt the procedures for a total of approximately \$173,000.⁵⁴⁴ Costs for fund complexes that will have to revise or fine-tune their stress test procedures would be less. For purposes of this cost benefit analysis, we estimate that these funds will incur half the costs of development, for a total of approximately \$96,000.⁵⁴⁵ Funds that will not have to change their test

procedures will incur approximately \$20,000 to determine compliance with the new requirement and to draft and adopt the procedures.⁵⁴⁶ We also anticipate that in light of the new demand to develop stress testing procedures, third parties will develop programs that funds will be able to purchase for less than our estimated cost to develop the programs themselves.

As with the development of stress test procedures, the costs funds will incur each year as a result of the proposed amendments to update test procedures, conduct stress tests, and provide reports on the tests and assessments to the board of directors will vary. Funds that currently conduct stress tests already incur costs to perform the tests. In addition, some of those funds may currently provide reports to senior management (if not the board) of their test results. We assume, however, that few, if any, fund advisers provide a regular assessment to the board of the fund's ability to withstand the events reasonably likely to occur in the following year. For that reason, we estimate that for routine reports, each fund complex will incur costs of \$3000 to provide a written report on the test results to the board, \$4000 to provide the assessment in the report, and \$10 to retain records of the reports for a total annual cost to a fund complex of \$42,000.⁵⁴⁷ As noted above, however, the procedures must provide for additional reports to the board as appropriate based on testing results, and we estimate that each fund complex will incur costs of \$28,000 for an average of four of these reports each year.⁵⁴⁸ We estimate that a portion of funds will incur additional costs to perform stress tests and update their procedures each

⁵³⁷ As proposed, the hypothetical events described in the final rule include a change in short-term interest rates, an increase in shareholder redemptions, a downgrade of or default on a portfolio security, and widening or narrowing of spreads between yields on a benchmark selected by the fund and securities held by the fund. See amended rule 2a-7(c)(10)(v)(A).

⁵³⁸ Amended rule 2a-7(c)(10)(v)(B). The report must include dates on which the testing was performed and the magnitude of each hypothetical event that would cause the deviation of the money market fund's net asset value, calculated using available market quotations (or appropriate substitutes that reflect current market conditions), from its net asset value per share, calculated using amortized cost, to exceed ½ of 1%. Amended rule 2a-7(c)(10)(v)(B)(1).

⁵³⁹ Amended rule 2a-7(c)(10)(v)(B)(2).

⁵⁴⁰ See *supra* note 411 and accompanying and preceding text.

⁵⁴¹ See Proposing Release, *supra* note 2, at paragraph following n.358.

⁵⁴² See *id.* at n.359 and accompanying text.

⁵⁴³ These complexes do not, however, meet the definition of "small entities" under the Investment Company Act for purposes of the Regulatory Flexibility Act of 1980. 17 CFR 270.0-10. See *infra* note 636.

⁵⁴⁴ This estimate is based on the following calculations: \$275/hour × 280 hours (collectively, 2 senior risk management specialists) + \$244/hour × 320 hours (collectively, 2 senior systems analysts) = \$155,080; \$275/hour (senior risk management specialist) × 22 hours = \$6050; \$4000/hour × 3 hours = \$12,000; \$155,080 + \$6050 + \$12,000 = \$173,130.

⁵⁴⁵ This estimate is based on the following calculation: (\$155,080 × 0.5) (revise procedures) + \$6050 (draft procedures) + \$12,000 (board approval) = \$95,590.

⁵⁴⁶ This estimate is based on the following calculation: \$275/hour (senior risk management specialist) × 8 hours = \$2200; \$2200 + \$6050 + \$12,000 = \$20,250.

⁵⁴⁷ See *supra* note 419 and preceding, accompanying, and following text. This estimate is based on the following calculation: Report: \$275/hour × 10 hours (senior risk management specialist) + \$62 × 2 hours (administrative assistant) = \$2874; Assessment: \$275/hour × 15 hours (senior risk management specialist) = \$4125; Record retention: \$62/hour × 0.1667 hours (administrative assistant) = \$10.33; (\$2874 + \$4125 + \$10) × 6 (board meetings per year) = \$42,054. Hourly wages used for purposes of the estimate of administrative assistant salaries are from the SIFMA Report on Management & Professional Salaries Data (Sept. 2008), modified to account for an 1800-hour work-year and multiplied by 2.93 to account for bonuses, firm size, employee benefits and overhead.

⁵⁴⁸ See *supra* note 420 and accompanying text. This estimate is based on the following calculation: (\$2874 (reports) + (\$4125 (assessment) + \$10 (recordkeeping)) × 4 = \$28,036.

year, up to a maximum of approximately \$149,000.⁵⁴⁹

For purposes of this cost benefit analysis, Commission staff has estimated that 25 percent of fund complexes (or 41 complexes) will have to develop stress test procedures, 50 percent (or 81) would have stress test procedures, but have to revise those procedures, and 25 percent of complexes (or 41 complexes) will review the procedures without having to change them. Based on these estimates, staff further estimates that the total one-time costs for fund complexes to develop or refine existing stress test procedures will be approximately \$16 million.⁵⁵⁰ In addition, staff estimates that the annual costs to all funds to conduct stress tests, update test procedures, provide reports to fund boards, and retain records of the reports will be approximately \$24 million.⁵⁵¹

4. Repurchase Agreements

We are adopting, as proposed, changes affecting a money market fund's ability to "look through" a repurchase agreement for purposes of rule 2a-7's diversification provisions.⁵⁵² Under the amended rule, a money market fund will be able to look through a repurchase agreement only if it is collateralized by cash items or Government securities, and if the fund's board of directors or its delegate evaluates the counterparty's creditworthiness.

The changes are designed to reduce money market funds' risks related to repurchase agreement investments so that funds will be better positioned to weather market turbulence and maintain a stable net asset value per share. A money market fund that invests in a repurchase agreement collateralized by cash items or Government securities is less likely to experience losses upon the sale of collateral in the event of a counterparty's default.⁵⁵³ The creditworthiness evaluation, moreover, will diminish the risk that a money

market fund in the first place enters into a repurchase agreement with a counterparty that subsequently defaults.

We believe that the costs associated with these changes will be minimal. As confirmed by commenters, most money market funds typically do not look through repurchase agreements collateralized with securities other than Government securities.⁵⁵⁴ Under the amended rule, money market funds will be able, as they have in the past, to invest in such repurchase agreements, although the funds will not be able to look through the repurchase agreements for purposes of rule 2a-7's diversification provisions.⁵⁵⁵

With regard to the new creditworthiness evaluation, several commenters stated that money market funds already evaluate the credit quality of counterparties under rule 2a-7(c)(3).⁵⁵⁶ We estimate, therefore, that investment advisers to only approximately 20 percent of all 163 fund complexes are not currently making such determinations. To the extent that boards or their delegates, in response to the amended rule, will make determinations that they would not otherwise make, those parties will expend time and/or resources in making those determinations. We estimate that, if an investment adviser were to spend 10 hours a year making creditworthiness determinations that it would not otherwise make concerning repurchase agreement counterparties, it would spend approximately \$2750 per year.⁵⁵⁷ Therefore the total cost to all money market funds would be approximately \$90,750 per year.⁵⁵⁸ In addition to these costs, we also estimated above, for purposes of the Paperwork Reduction Act, that funds might spend 2 hours per year maintaining records concerning the determinations made under the amended rule.⁵⁵⁹ We estimate the aggregate total costs associated with this recordkeeping to be \$20,212 per year.⁵⁶⁰

⁵⁵⁴ See *supra* note 274 and accompanying text.

⁵⁵⁵ No commenter has expressed the view that the new diversification requirement will increase money market funds' cost of investing in repurchase agreements.

⁵⁵⁶ As discussed above, three commenters argued that the proposed creditworthiness evaluation is unnecessary because it is already an element of the minimal credit risk determination that a fund makes pursuant to rule 2a-7(c)(3). See *supra* note 277.

⁵⁵⁷ This estimate is based on the following calculation: \$275/hour (senior risk management specialist) × 10 hours = \$2750.

⁵⁵⁸ This estimate is based on the following calculation: \$275/hour (senior risk management specialist) × 10 hours × 33 fund complexes = \$90,750.

⁵⁵⁹ See *supra* Section IV.A.4.

⁵⁶⁰ This estimate is based on the following calculation: \$62/hour (administrative assistant) × 2 hours × 163 fund complexes = \$20,212.

5. Public Web site Posting

The amendments to rule 2a-7 require money market funds to post monthly portfolio information on their Web sites.⁵⁶¹ The rule amendments are intended to provide shareholders with timely information about the securities held by the money market fund.

We anticipate that requiring funds to post monthly portfolio information on their Web sites will benefit investors by providing them a better understanding of their own risk exposure enabling them to make better informed investment decisions. The rule amendments may thus instill more discipline into portfolio management and reduce the likelihood of a money market fund breaking the buck.

The Web site posting requirement will impose certain costs on funds. We estimated in the Proposing Release that money market funds would be required to spend 24 hours of internal money market fund staff time initially to develop a webpage, at a cost of \$4944 per fund.⁵⁶² We also estimated that all money market funds would be required to spend 4 hours of professional time to maintain and update the Webpage each month, at a total annual cost of \$9888 per fund.⁵⁶³ We also stated that we believe, however, that our estimates may overstate the actual costs that would be incurred to comply with the Web site posting requirement because many funds currently post their portfolio holdings on a monthly, or more frequent, basis.⁵⁶⁴ For purposes of the cost benefit analysis in the Proposing Release, Commission staff estimated that 20 percent of money market portfolios (150 portfolios) did not post portfolio holdings information on their Web sites.⁵⁶⁵ We requested comment on these estimated costs in the Proposing Release.⁵⁶⁶ One commenter suggested that we may have underestimated the costs associated with the initial development of the Web page, but also may have overestimated the costs associated with the ongoing

⁵⁶¹ Amended rule 2a-7(c)(12).

⁵⁶² See Proposing Release, *supra* note 2, at n.374 and accompanying text. The staff estimated that a webmaster at a money market fund would require 24 hours (at \$206 per hour) to develop and review the webpage (24 hours × \$206 = \$4944).

⁵⁶³ See Proposing Release, *supra* note 2, at n.375 and accompanying text. The staff estimated that a webmaster would require 4 hours (at \$206 per hour) to maintain and update the relevant webpages on a monthly basis (4 hours × \$206 × 12 months = \$9888).

⁵⁶⁴ See Proposing Release, *supra* note 2, at n.376 and accompanying text.

⁵⁶⁵ See Proposing Release, *supra* note 2, at text preceding n.377.

⁵⁶⁶ See Proposing Release, *supra* note 2, at Section V.A.5.

⁵⁴⁹ This estimate is based on the following calculations: Tests: \$275/hour × 15 hours (senior risk management specialist) + \$244/hour × 20 hours (senior systems analyst) = \$9005; \$9005 × 12 (monthly testing) + (\$9005 × 4 additional "appropriate" testing) = \$144,080; Update procedures: \$275/hour × 5 hours (senior risk management specialist) + \$4000/hour × 1 hour = \$5375; \$144,080 + \$5375 = \$149,455.

⁵⁵⁰ This estimate is based on the following calculation: (41 × \$173,000) + (81 × \$95,000) + (41 × \$20,000) = \$15,608,000.

⁵⁵¹ This estimate is based on the following calculation: (41 × \$149,455) + (81 × \$149,455 × 0.5) + (163 × \$70,090 (reports, including assessments)) = \$23,605,252.5.

⁵⁵² See *supra* Section II.D; Proposing Release, *supra* note 2, at Section II.E.

⁵⁵³ See *supra* note 272 and accompanying text.

maintenance of Web site reporting.⁵⁶⁷ The commenter did not provide any cost estimates. Commission staff continues to believe that these cost estimates are appropriate. In addition, as discussed above, we have decided not to require some of the information required by Regulation S–X, which we proposed that funds post on their Web sites.⁵⁶⁸ We expect that eliminating the mandatory posting of this information, which we believe is not critical to be made available to investors, will reduce costs for funds and their advisers.⁵⁶⁹

One commenter, however, stated that the cost estimates did not include the cost for the 80 percent of money market portfolios that currently post portfolio holdings information at least quarterly on their Web sites to develop the capability to retain previous months' portfolio holdings information on their Web sites.⁵⁷⁰ Based on a review of some of the commenters' current portfolio Web site disclosure and follow-up discussions with some commenters, Commission staff estimates that 500 funds will need to develop this capability. Commission staff estimates that each of these 500 funds will spend approximately 12 hours, at a one-time cost of \$2472 per fund, to develop this capability.⁵⁷¹

Based on these estimates, we estimate that the total initial costs for the Web site disclosure will be \$1,947,936.⁵⁷² In addition, we estimate that the annual costs for all money market funds to maintain and update their webpages will be \$7.1 million.⁵⁷³

In addition, monthly Web site disclosure may impose other costs on funds and their shareholders. For example, more frequent disclosure of portfolio holdings may arguably expand the opportunities for professional traders to exploit this information by engaging in predatory trading practices, such as front-running. However, given

the short-term nature of money market fund investments and the restricted universe of eligible portfolio securities, we believe that the risk of trading ahead is severely curtailed in the context of money market funds.⁵⁷⁴ For similar reasons, we believe that the potential for "free riding" on a money market fund's investment strategies, *i.e.*, obtaining for free the benefits of fund research and investment strategies, is minimal. Given that shares of money market funds are ordinarily purchased and redeemed at the stable price per share, we believe that there would be relatively few opportunities for profitable arbitrage. Thus, we estimate that the costs of predatory trading practices under the amended rule will be minimal. Furthermore, as previously noted, most money market fund portfolios (80 percent) already are posted on fund Web sites at least quarterly.

6. Processing of Transactions

The amendments to rule 2a–7 require a money market fund to have the capacity to redeem and sell its securities at a price based on the fund's current net asset value per share, including the capacity to sell and redeem shares at prices that do not correspond to the stable net asset value or price per share.⁵⁷⁵ As discussed above, the events of fall 2008 revealed that some funds had not implemented automated systems to process redemptions at prices other than the funds' stable net asset value per share. As a result, transactions were processed manually, which extended the time that investors had to wait for the proceeds from their redeemed shares. This experience showed that funds that cannot electronically process redemptions at prices other than the funds' stable net asset value per share risk being unable to meet their obligations to redeem shares and pay redemption proceeds within seven days, as required under the Act.

The amendments to rule 2a–7 mitigate the risk that money market funds would not be able to meet these obligations in the event the fund breaks a buck. These amendments benefit shareholders because they increase the likelihood that shareholders will timely receive the proceeds of their investments when a fund breaks the buck.

Because funds have an existing obligation to redeem at other than their stable net asset value per share, we do not believe that this amendment to rule 2a–7 imposes any additional costs on

funds or their transfer agents.⁵⁷⁶ Nonetheless, to the extent that funds and transfer agents have to change their systems, we estimated in the Proposing Release that the total cost for a fund complex would be \$39,040.⁵⁷⁷ We further estimated that one-third of the fund complexes are not currently able to redeem at prices other than stable net asset value, and thus the total cost to all money market funds would be \$2,225,280.⁵⁷⁸

Several commenters claimed that the costs of changing the systems would exceed our estimates.⁵⁷⁹ One commenter estimated that the costs of making the required changes to the core transfer agent and ancillary systems would total approximately \$24 million for ten fund complexes, representing 63 percent of money market fund assets, and two of the three largest transfer agent service providers.⁵⁸⁰ Based on those figures, we have revised our estimate to reflect that the total cost of making the required systems changes for all money market funds would be approximately \$38.1 million.⁵⁸¹

B. Rule 17a–9

The Commission is amending rule 17a–9 to expand the circumstances under which affiliated persons can purchase money market fund portfolio securities. Under the amendment, a money market fund generally will be able to sell a portfolio security that has defaulted to an affiliated person for cash equal to the greater of the security's amortized cost value or market value (including accrued interest), even though the security continues to be an eligible security.⁵⁸²

⁵⁷⁶ See *supra* Section II.F.

⁵⁷⁷ This estimate is based on the following calculation: \$244/hour × 160 hours (senior systems analyst) = \$39,040.

⁵⁷⁸ This estimate was based on the following calculation: (171 fund complexes + 3) × \$39,040 = \$2,225,280.

⁵⁷⁹ See, *e.g.*, HighMark Capital Comment Letter; ICI Comment Letter.

⁵⁸⁰ See ICI Comment Letter. The ICI conducted a survey of its members and gathered data from 10 fund complexes and 2 transfer agent service providers. Six of the 12 respondents indicated that their transfer agent system already had the capability to process money market fund trades at other than a \$1.00 stable net asset value.

⁵⁸¹ We believe that the systems changes costs are correlated to the size of the fund complex. Accordingly, this estimate is based on the following calculations: \$24 million ÷ 63% = \$38.1 million. The ICI Comment Letter also provided additional cost estimates for changes to the systems of intermediaries who perform sub-transfer agency or similar recordkeeping functions. We do not discuss those additional costs here because, as discussed above, the rule does not impose any requirements on those intermediaries. See *supra* text preceding note 363.

⁵⁸² See amended rule 17a–9(a).

⁵⁶⁷ See Clearwater Comment Letter.

⁵⁶⁸ See *supra* note 285 and accompanying text.

⁵⁶⁹ *Id.*

⁵⁷⁰ See Data Communiqué Comment Letter. Under our proposal, funds would have been required to maintain the portfolio holdings information on their Web sites for at least twelve months. We are adopting a six-month maintenance period for portfolio holding information.

⁵⁷¹ The staff estimates that a Webmaster at a money market fund would require 12 hours (at \$206 per hour) to develop the capability to retain previous months' portfolio holdings information on their Web sites as required by the rule (12 hours × \$206 = \$2472).

⁵⁷² This calculation was based on the following estimate: (\$4944 × 144 portfolios) (cost to develop webpage) + (\$2472 × 500 portfolios) (cost to develop capability to retain previous months' portfolio holdings information on existing Web sites) = \$1,947,936.

⁵⁷³ This calculation was based on the following estimate: (\$9888 × 719 portfolios) = \$7,109,472.

⁵⁷⁴ See *ICI Report, supra* note 14, at 93.

⁵⁷⁵ Amended rule 2a–7(c)(13).

The amendment essentially codifies past Commission staff no-action letters⁵⁸³ and should benefit investors by enabling money market funds to dispose of distressed securities (e.g., securities depressed in value as a result of market conditions) from their portfolios quickly without any loss to fund shareholders. It also benefits money market funds by eliminating the cost and delay of requesting no-action assurances in these scenarios and the uncertainty whether such assurances will be granted.⁵⁸⁴ We do not believe that there are any costs associated with this amendment, and we received no comments on this analysis.

In addition, the amendment permits affiliated persons to purchase other portfolio securities from an affiliated money market fund, for any reason, as long as the security's purchase price meets the rules' other conditions and such person promptly remits to the fund any profit it realizes from the later sale of the security.⁵⁸⁵ Our staff provided temporary no-action assurances during the fall of 2008 to certain funds facing extraordinary levels of redemption requests for affiliated persons of such funds to purchase eligible securities from the funds at the greater of amortized cost or market value (plus accrued and unpaid interest).⁵⁸⁶ In these circumstances, money market funds may need to obtain cash quickly to avoid selling securities into the market at fire sale prices to meet shareholder redemption requests, to the detriment of remaining shareholders. The staff also provided no-action assurances to money market funds for affiliated persons of the fund to purchase at the greater of amortized cost or market value (plus accrued and unpaid interest) certain distressed securities that were depressed in value due to market conditions potentially threatening the stable share price of the fund, but that remained eligible securities and had not defaulted.⁵⁸⁷ Money market funds and their shareholders benefit if affiliated persons are able to purchase securities from the fund at the greater of amortized cost or market value (plus accrued and unpaid interest) in such circumstances without the time, expense, and uncertainty of applying to Commission staff for no-action assurances.

Affiliated persons purchasing such securities will have costs in creating and implementing a system for tracking the purchased securities and remitting to the money market fund any profit ultimately received as a result. We estimate that creating such a system on average would require 5 hours of a senior programmer's time, at a cost of \$1460 for each of the 163 fund complexes with money market funds, and a total cost of \$237,980.⁵⁸⁸ After the initial creation of this system, we expect that the time spent noting in this system that a security was purchased under rule 17a-9 would require a negligible amount of compliance personnel's time. Based on our experience, we do not anticipate that there would be many instances, if any, in which an affiliated person will be required to repay profits in excess of the purchase price paid to the fund. However, if there is a payment, it would be made to the fund. If the payment is sufficiently large, we believe that funds are likely to include it with the next distribution to shareholders, which would not result in any additional costs to the fund. We received no comments on this analysis.

The Commission also is adopting a related amendment to rule 2a-7, which requires that funds report all transactions under rule 17a-9 to the Commission. We believe that this reporting requirement benefits fund investors by allowing the Commission to monitor the purchases for possible abuses and conflicts of interest on the part of the affiliates. It also allows the Commission to observe what types of securities are distressed and which money market funds are holding distressed securities or are subject to significant redemption pressures. This information will assist us in monitoring emerging risks at money market funds. For purposes of the Paperwork Reduction Act analysis, we estimate this amendment will impose relatively small reporting costs on money market funds of \$7625 per year.⁵⁸⁹ We received no comments on this analysis.

C. Rule 22e-3

Rule 22e-3 permits a money market fund that has broken the buck, or is at imminent risk of breaking the buck, to suspend redemptions and postpone the payment of proceeds pending board-approved liquidation proceedings. By facilitating orderly liquidations in

distressed circumstances, we anticipate that rule 22e-3 will reduce the vulnerability of shareholders to the harmful effects of a run on a fund and minimize the potential for market disruption. The rule also enables funds to avoid the expense and delay of obtaining an exemptive order from the Commission, which we estimate would otherwise cost approximately \$75,000, and will provide legal certainty to funds that wish to suspend redemptions during a liquidation in the interest of fairness to all shareholders.

Rule 22e-3 will impose certain minimal costs on funds relying on the rule by requiring them to provide prior notice to the Commission of their decision to suspend redemptions in connection with a liquidation. Furthermore, the rule will impose minimal costs on certain conduit funds that have invested in money market funds that suspended redemptions in reliance on the rule by also requiring those conduit funds to provide notice to the Commission. We estimate that the total annual burden of the notification requirement for all money markets funds and conduit funds will be 110 minutes, at a cost of \$559.⁵⁹⁰ In addition, rule 22e-3 imposes costs on shareholders who seek to redeem their shares, but are unable to do so. In those instances, shareholders may have to borrow funds from another source, and thereby incur interest charges and other transaction fees. We believe, however, that the costs associated with rule 22e-3 are minimal because the rule provides a very limited exemption that is triggered only when a fund breaks the buck, or is in imminent risk of breaking the buck, and liquidates.

D. Rule 30b1-7 and Form N-MFP: Monthly Reporting of Portfolio Holdings

Rule 30b1-7 and Form N-MFP require money market funds to file with the Commission interactive data-formatted portfolio holdings information on a monthly basis. We expect that the rule and form will improve the efficiency and effectiveness of the Commission's oversight of money market funds by enabling Commission staff to manage and analyze comprehensive money market fund portfolio information more quickly and at a lower cost than is currently possible. The interactive data will also facilitate the flow of information between money market funds and other users of this information, such as information services, academics, and

⁵⁸³ See *supra* Section II.G.1.

⁵⁸⁴ Commission staff estimates that the costs to obtain staff no-action assurances range from \$50,000 to \$100,000.

⁵⁸⁵ See amended rule 17a-9(b).

⁵⁸⁶ Many of the no-action letters can be found on our Web site. See <http://www.sec.gov/divisions/investment/im-noaction.shtml#money>.

⁵⁸⁷ *Id.*

⁵⁸⁸ This estimate is based on the following calculation: \$292/hour × 5 hours × 163 fund complexes = \$237,980.

⁵⁸⁹ This estimate is based on the following calculation: 25 (notices) × \$305/hour (attorney) × 1 hour = \$7625. See *supra* note 437 and accompanying text.

⁵⁹⁰ See *supra* note 443 and accompanying text. This estimate is based on the following calculation: \$305/hour × 110 minutes = \$559.

investors. As a result, users of this information, including investors, may benefit by gaining a better understanding of money market funds' risk exposure and becoming better informed in their investment decisions. As the development of software products to analyze the data continues to grow, we expect these benefits will increase. Finally, the portfolio reporting may instill more discipline into portfolio management and reduce the likelihood of a money market fund breaking the buck.

Money market funds may also realize cost savings from the rule. Currently, money market funds provide portfolio holdings information in a variety of formats to different third-parties, such as information services and NRSROs. The rule may encourage the industry to adopt a standardized format, thereby reducing the burdens on money market funds of having to produce this information in multiple formats.

The reporting requirement will also impose certain costs. We estimated in the Proposing Release, that, for the purposes of the PRA, these filing requirements (including collecting, tagging, and electronically filing the report) would impose 128 burden hours at a cost of \$35,968⁵⁹¹ per money market fund for the first year, and 96 burden hours at a cost of \$26,976⁵⁹² per money market fund in subsequent years.⁵⁹³ We requested comment on these estimated costs in the Proposing Release.⁵⁹⁴

As discussed above, two commenters asserted that the Commission's cost estimates did not include time to review the information required in Form N-MFP.⁵⁹⁵ In response to these commenters, we revised our PRA estimates to include an additional 2

⁵⁹¹ See Proposing Release, *supra* note 2, at n.396 and accompanying text. This estimate was based on the following calculation: \$281/hour × 128 hours (senior database administrator) = \$35,968.

⁵⁹² See Proposing Release, *supra* note 2, at n.397 and accompanying text. This estimate was based on the following calculation: \$281/hour × 96 hours (senior database administrator) = \$26,976.

⁵⁹³ We understand that some money market funds may outsource all or a portion of these responsibilities to a filing agent, software consultant, or other third-party service provider. We believe, however, that a fund would engage third-party service providers only if the external costs were comparable, or less than, the estimated internal costs of compiling, tagging, and filing the Form N-MFP.

⁵⁹⁴ See Proposing Release, *supra* note 2, at paragraph following n.398.

⁵⁹⁵ See Bowne Comment Letter; Data Communiqué Comment Letter. Another commenter suggested that we may have underestimated the costs associated with the initial filing of Form N-MFP, but also may have overestimated the ongoing costs associated with subsequent filings. See Clearwater Comment Letter. The commenter, however, did not provide any cost estimates.

hours per filing for review of the information.⁵⁹⁶ As a result of this increase, we have revised our cost estimates. We estimate that, for the purposes of the PRA, these filing requirements (including collecting (and review), tagging, and electronically filing the report) would impose 152 burden hours at a cost of \$42,712⁵⁹⁷ per money market fund for the first year, and 120 burden hours at a cost of \$33,720⁵⁹⁸ per money market fund in subsequent years.⁵⁹⁹ We estimate that the total cost for all money market funds for the first year would be \$30,709,928.⁶⁰⁰ The total annual estimated cost for all money market funds in subsequent years would be \$24,244,680.⁶⁰¹

In addition, funds may incur additional costs as a result of the public availability of a fund's market-based net asset value, which is required to be included in Form N-MFP filings. In particular, some commenters noted that if investors systematically redeem shares for one dollar when the market-based net asset value is less than one dollar, the fund might have difficulty maintaining its stable price. However, in response to concerns about the disclosure of market-based values, we are delaying the public availability of the information filed on Form N-MFP for 60 days after the end of the reporting period.⁶⁰² We acknowledge that investors might choose to sell their money market fund shares that have a low market-based net asset value, and it is possible that a run could develop.

⁵⁹⁶ See *supra* Section IV.C.

⁵⁹⁷ This estimate is based on the following calculation: \$281/hour × 152 hours (senior database administrator) = \$42,712.

⁵⁹⁸ This estimate is based on the following calculation: \$281/hour × 120 hours (senior database administrator) = \$33,720.

⁵⁹⁹ We understand that some money market funds may outsource all or a portion of these responsibilities to a filing agent, software consultant, or other third-party service provider. We believe, however, that a fund would engage third-party service providers only if the external costs were comparable, or less than, the estimated internal costs of compiling, tagging, and filing the Form N-MFP.

⁶⁰⁰ This estimate is based on the following calculation: \$42,712 (total estimated cost per fund for first year) × 719 funds = \$30,709,928.

⁶⁰¹ This estimate is based on the following calculation: \$33,720 (total estimated cost per fund after the first year) × 719 funds = \$24,244,680.

⁶⁰² See rule 30b1-7(b). See also *supra* text accompanying note 320. As noted above, money market funds currently must disclose their market-to-market net asset value per share semi-annually in their Form N-SAR filings [17 CFR 274.101], which are publicly available. Form N-SAR must be filed with the Commission no later than the 60th day after the end of the fiscal period for which the report is being prepared. See *supra* note 337 and accompanying text. Thus, investors already have access to market-based portfolio value information on the basis of which they could make redemptions.

Nevertheless, at least two other factors will reduce the risk of a run. First, portfolio managers may choose to follow less risky investment strategies in an effort to maintain a high market-based net asset value. Second, funds may be quicker to ask for help from their affiliates through, for example, rule 17a-9 transactions.

The money market fund industry is characterized by a mix of competitors with and without affiliates that can provide financial support. The disclosure of a fund's market-based net asset value might encourage funds that have affiliates with the ability to provide financial support to request such support as soon as any problems develop. This support could provide stability to funds that receive the support. This support might also give a competitive advantage to funds that receive it because they may be more willing to invest in securities with higher risk and higher yields. However, the extent of this competitive advantage may be mitigated because the amendments will require the disclosure of the fund's market-based NAV with and without capital support agreements. In addition, much of the extent to which fund managers might take advantage of capital support arrangements to boost fund yields is independent of the amendments we are adopting today and affiliated persons of money market funds are not obligated to support these funds. For the reasons outlined in the discussion on the monthly Web site posting requirement, we estimate that there will be minimal additional costs incurred from predatory trading practices (e.g., front-running or "free riding") as a result of the reporting requirement.⁶⁰³

E. Rule 30b1-6T

We adopted rule 30b1-6T to enable the Commission staff to continue to have effective oversight of money market funds. The rule was designed to improve the efficiency and effectiveness of the Commission's oversight by providing useful information about money market funds that report under the rule, and by enabling the staff to manage and analyze money market fund portfolio information more quickly and at a lower cost than possible without electronic submissions of portfolio schedules. When we adopted rule 30b1-6T in September 2009, we requested

⁶⁰³ See *supra* note 574 and accompanying and following text.

comments on the costs and benefits of the rule but received no comments.⁶⁰⁴

Rule 30b1-6T will impose some costs on funds. For the purposes of the PRA, we estimated that the rule will result in an increase of 2100 burden hours per year. We estimate that these burden hours will cost a total of \$590,100.⁶⁰⁵ We do not believe that rule 30b1-6T will impose other significant costs, especially given the nonpublic nature of the reports required under the rule.

VI. Competition, Efficiency, and Capital Formation

Section 2(c) of the Investment Company Act requires the Commission, when engaging in rulemaking that requires it to consider or determine whether an action is consistent with the public interest, to consider, in addition to the protection of investors, whether the action will promote efficiency, competition, and capital formation.⁶⁰⁶

A. Rule 2a-7

1. Second Tier Securities, Portfolio Maturity, and Liquidity Limits

We are adopting several amendments to rule 2a-7 to tighten the risk-limiting conditions of the rule. As discussed above, we are further restricting money market funds' ability to acquire second tier securities. The amendments reduce the maximum weighted average maturity of a money market fund permitted by rule 2a-7 from 90 days to 60 days.⁶⁰⁷ They also impose a new maturity limitation based on the weighted average "life" of fund securities that limits the portion of a fund's portfolio that can be held in longer term floating- or variable-rate securities.⁶⁰⁸ We are deleting a provision in rule 2a-7 that permitted money market funds not relying on the amortized cost method of valuation to acquire Government securities with a remaining maturity of up to 762 calendar days.

Finally, we are adopting new liquidity requirements for money market funds. In particular, we are amending rule 2a-7 to (i) Require that each money market fund hold securities that are sufficiently liquid to meet reasonably foreseeable shareholder redemptions in light of its obligations under section 22(e) of the Act and any commitments the fund has made to shareholders;⁶⁰⁹ (ii) further

limit a money market fund's investments in illiquid securities (i.e. securities that cannot be sold or disposed of in the ordinary course of business within seven days at approximately the value ascribed to them by the money market fund);⁶¹⁰ and (iii) require a taxable money market fund to hold at least 10 percent of its total assets in "daily liquid assets" and any money market fund to hold at least 30 percent of its total assets in "weekly liquid assets."⁶¹¹

We believe that these changes will reduce money market funds' sensitivity to interest rate, credit, and liquidity risks. These changes will also limit the spread risk produced by longer term securities and second tier securities. A reduction of these risks will help individual money market funds to weather market turbulence and maintain a stable net asset value per share, which will increase the stability of the entire money market fund industry. To the extent that money market funds are more stable, the changes also will reduce systemic risk to the capital markets and ensure a stable source of financing for issuers of short-term credit instruments. We believe that these effects will encourage capital formation by encouraging investment in money market funds as well as the issuance of securities that money market funds can purchase.

These changes also may reduce maturities of short-term credit securities that issuers offer, which may increase financing costs for these issuers who might have to go back more frequently to the market for financing. As discussed above, several commenters stated that the elimination of money market funds' ability to acquire second tier securities could increase second tier security issuers' borrowing costs and thus increase capital formation costs.⁶¹² Some of these commenters also asserted that such a prohibition could require second tier security issuers to rely more on bank financing, which could negatively impact banks' ability to lend to other parts of the economy.⁶¹³ We note that these impacts should be mitigated given that we are limiting and

not eliminating money market funds' ability to acquire second tier securities. However, to the extent that some issuers are unwilling or unable to issue securities that match money market fund demand given these new restrictions or that banks become less willing to lend to finance new businesses, the amendments could have a negative impact on capital formation.

As discussed in the cost benefit analysis above, we expect that the amendments will reduce yields that some money market funds are able to offer. The lower yields may affect the ability of money market funds to compete with other investment vehicles. While money market funds compete with each other, they also compete for investors on the basis of risk-return tradeoff with other lower-risk investment vehicles, such as offshore or unregulated money market funds, bank money market deposit accounts, and deposit accounts in general. The reduction in yield may cause some investors to move their money to, among other places, offshore or unregulated money market funds that do not follow rule 2a-7's strictures and thus are able to offer a higher yield. Beyond the competitive impact, such a change could increase systemic risks to short-term credit markets and capital formation by increasing investment in less stable short-term instruments.

Further limitations on money market funds' ability to acquire second tier securities also may have anticompetitive effects on some relatively small money market funds that may compete with larger funds on the basis of yield. One commenter stated that elimination of money market funds' ability to acquire second tier securities could have a disproportionate impact on smaller money market funds.⁶¹⁴ Our review of money market fund holdings of second tier securities during September 2008 did not reveal smaller money market funds holding second tier securities to a greater extent than larger funds, although smaller funds may try to increase their holdings of second tier securities in different market environments. Even if there were any anticompetitive effects on smaller money market funds, these effects should be reduced by the fact that we are only further limiting, and not eliminating, money market funds' ability to acquire second tier securities.

The further limitations on the ability of money market funds to invest in second tier securities may affect the capital raising ability and strategies of second tier security issuers or otherwise

⁶⁰⁴ See Rule 30b1-6T Release, *supra* note 303, at Section VI.

⁶⁰⁵ This estimate is based on the following calculation: 2100 hours × \$281/hour (senior database administrator) = \$590,100.

⁶⁰⁶ 15 U.S.C. 80a-2(c).

⁶⁰⁷ See amended rule 2a-7(c)(2)(ii).

⁶⁰⁸ See amended rule 2a-7(c)(2)(iii).

⁶⁰⁹ Amended rule 2a-7(c)(5).

⁶¹⁰ Amended rule 2a-7(c)(5)(i). Under the amended rule, a money market fund cannot acquire illiquid securities if immediately after the acquisition, the fund would have invested more than five percent of its total assets in illiquid securities.

⁶¹¹ See amended rule 2a-7(c)(5)(ii)-(iii). See also amended rule 2a-7(a)(8) (defining "daily liquid assets"); 2a-7(a)(32) (defining "weekly liquid assets").

⁶¹² See *supra* notes 48-49 and accompanying paragraph.

⁶¹³ See, e.g., Chamber/Tier 2 Issuers Comment Letter.

⁶¹⁴ See Thrivent Comment Letter.

affect their financing arrangements, and may affect the flexibility of investing options for funds. As a preliminary matter, taking into account commenters' concerns, we have determined not to eliminate money market funds' ability to acquire second tier securities. Further, as noted above, second tier securities represent only a very small percentage of money market fund portfolios today and money market funds are not the primary purchasers of second tier securities, which suggests that our amendments would not in themselves have a material effect on capital formation.⁶¹⁵ Nonetheless, we recognize that some non-rule 2a-7 regulated cash management funds and investment pools voluntarily use rule 2a-7 as an investment guideline.⁶¹⁶ However, since we are only further limiting, and not eliminating, money market funds' ability to acquire second tier securities, we do not believe that the behavior of these non-rule 2a-7 funds will have a material adverse effect on capital formation.

2. Designation of NRSROs

We are adopting amendments requiring money market fund boards to designate at least four NRSROs that the fund will use in determining the eligibility of portfolio securities and that the board determines annually issue credit ratings that are sufficiently reliable for this use.⁶¹⁷ As noted above, several commenters suggested that designating at least three NRSROs could encourage competition among NRSROs to achieve designation by money market fund boards.⁶¹⁸ We assume that three NRSROs issue more than 90 percent of ratings of short-term debt.⁶¹⁹ Requiring the designation of at least four NRSROs will ensure that money market funds will consider NRSROs beyond the dominant three. In addition, the amendment may encourage new NRSROs that issue ratings specifically for money market fund instruments to enter the market. To the extent that requiring designation of at least four NRSROs will further increase

⁶¹⁵ Based on discussions with one commenter to clarify certain aspects of its comment letter, however, we understand that money market funds purchase approximately 80% of the commercial paper of at least one second tier issuer. See Chamber/Tier 2 Issuers Comment Letter. We understand that such a significant reliance on money market funds to purchase a second tier issuer's securities is quite unusual.

⁶¹⁶ See, e.g., Chamber/Tier 2 Issuers Comment Letter.

⁶¹⁷ Amended rule 2a-7(a)(11)(i).

⁶¹⁸ See, e.g., HighMark Capital Comment Letter; Invesco Aim Comment Letter.

⁶¹⁹ See Proposing Release, *supra* note 2, at text accompanying and following n.116. See also *supra* note 104 and accompanying text.

competition, it also should increase the reliability of the credit ratings of designated NRSROs. Having better information about risk could increase the efficiency of fund managers in determining eligibility of portfolio securities. We do not anticipate that the proposed designation of NRSROs will have an adverse impact on capital formation.

3. Stress Testing

We are amending rule 2a-7 to require the board of directors of each money market fund to adopt procedures providing for periodic stress testing of the money market fund's portfolio, reporting the results of the testing to fund boards, and providing an assessment to the board.⁶²⁰ We believe that stress testing will increase the efficiency of money market funds by enhancing their risk management and thus making it more likely that the fund will be better prepared for potential stress on the fund due to market events or shareholder behavior. Money market funds will likely become more stable as a result of the risk management benefits provided by stress testing, allowing them to expand and attract further investment. If so, this result will promote capital formation. We do not believe that stress testing will have an adverse impact on competition or capital formation.⁶²¹

4. Repurchase Agreements

We are adopting, as proposed, changes to the conditions under which a money market fund may take advantage of the special look-through treatment of repurchase agreements under rule 2a-7's diversification provisions.⁶²² In order to obtain such special treatment, a money market fund will be limited to investing in repurchase agreements collateralized by cash items or Government securities and the fund's board of directors or its delegate will have to evaluate the creditworthiness of the repurchase agreement's counterparty.

We believe that these changes will limit the risk that a money market fund incurs losses upon the sale of collateral in the event of a counterparty's default.⁶²³ The lower risk will in turn increase money market funds' ability to maintain a stable net asset value per share, thereby preventing losses to fund

⁶²⁰ Amended rule 2a-7(c)(10)(v).

⁶²¹ No commenters addressed the analysis in the Proposing Release regarding whether the proposed stress testing requirements would promote competition, efficiency, and capital formation.

⁶²² See *supra* Section II.D; Proposing Release, *supra* note 2, at Section II.E.

⁶²³ See *supra* note 272 and accompanying text.

investors. More stable money market funds may attract greater investments, thus promoting capital formation and providing a greater source of financing in the capital markets. The changes will not negatively impact competition, efficiency, or capital formation. In particular, commenters noted that most money market funds typically do not look through to collateral consisting of non-Government securities.⁶²⁴

5. Public Web Site Disclosure

One of the amendments to rule 2a-7 requires money market funds to disclose certain portfolio holdings information on their Web sites on a monthly basis.⁶²⁵ In the Proposing Release, we requested comment on what effect this rule amendment would have on competition, efficiency, and capital formation.⁶²⁶ No commenters addressed the effect of this amendment on competition, efficiency, and capital formation.

The rule amendment will provide greater transparency of the fund's investments for current and prospective shareholders, and may thus promote more efficient allocation of investments by investors.⁶²⁷ We believe the rule amendment may also improve competition, as better-informed investors may prompt funds managers to provide better services and products. We do not anticipate that funds would be disadvantaged, with respect to competition, because so many already have chosen to provide the information more frequently than monthly. In addition, the investments selected by money market funds are less likely than, for example, equity funds, to be investments from which competing funds would obtain benefit by scrutinizing on a monthly basis.

The rule amendment may also promote capital formation by making portfolio holdings information readily accessible to investors, who may thus be more inclined to allocate their investments in a particular fund or in money market funds instead of an

⁶²⁴ See *supra* note 274. Wells Fargo stated that the amendment would negatively affect capital formation because money market funds will no longer invest in repurchase agreements collateralized with securities with the highest rating or unrated securities of comparable quality, which would negatively affect counterparties and issuers of collateral. See Wells Fargo Comment Letter. We discuss those comments above. See *supra* note 273.

⁶²⁵ See *supra* Section II.E.1.

⁶²⁶ See Proposing Release, *supra* note 2, at Section VI.A.4.

⁶²⁷ Due to the availability of the portfolio holding information on fund Web sites, investors may allocate their investments away from funds with riskier portfolios. Among other things, this may reduce systemic risks as money market funds may respond by investing in securities with less risk.

alternative product. Alternatively, the rule amendment might have the reverse effect if the portfolio holdings information makes investors less confident regarding the risks associated with money market funds, including the risk that market participants might use the information obtained through the disclosures to the detriment of the fund and its investors, such as by trading along with the fund or ahead of the fund by anticipating future transactions based on past transactions. We also recognize the potential for runs on money market funds that might result from any investors who compute market-based net asset values from the public disclosure of portfolio holdings. As discussed above, however, most money market funds currently disclose their portfolio holdings on their Web sites, and therefore we do not believe that our requirement that funds post monthly portfolio holdings will have a material effect on the ability of investors to compute market-based values and incite a run on the fund.

6. Processing of Transactions

The amendments to rule 2a-7 require a money market fund to have the capacity to redeem and sell its securities at a price based on the fund's current net asset value per share, even if the fund's current net asset values does not correspond to the fund's stable net asset value or price per share. This amendment increases efficiency at money market funds that break the buck by increasing the speed and minimizing the operational difficulties in satisfying shareholder redemption requests in such circumstances. It may also reduce investors' concerns that redemptions would be unduly delayed if a money market fund were to break the buck. We do not believe that this amendment has a material impact on competition or capital formation.

B. Rule 17a-9

The Commission is amending rule 17a-9 to expand the circumstances under which affiliated persons can purchase money market fund securities. Under the amendments, a money market fund generally will be able to sell a portfolio security that has defaulted to an affiliated person for the greater of the security's amortized cost value or market value (including accrued interest), even though the security continued to be an eligible security.⁶²⁸ In addition, the amendment permits affiliated persons, for any reason, to purchase other portfolio securities from an affiliated money market fund on the

same terms as long as such person is required to promptly remit to the fund any profit it realizes from the later sale of the security.⁶²⁹ These amendments increase the efficiency of both the Commission and money market funds by allowing affiliated persons to purchase portfolio securities from money market funds under distress without having to seek no-action assurances from Commission staff. The money market fund industry is competitive; some money market funds have well-funded affiliates to support the money market fund while others do not. This amendment may increase the competitive advantage of money market funds with well-funded affiliates relative to other money market funds, which we balanced against the need to promote stability in money market funds. We do not believe that the amendments will have any material impact on capital formation. We received no comments on this analysis.

C. Rule 22e-3

Rule 22e-3 permits a money market fund that has broken the buck, or is at imminent risk of breaking the buck, to suspend redemptions and postpone the payment of proceeds pending board-approved liquidation proceedings. We anticipate the rule will promote efficiency in the financial markets by facilitating the orderly disposal of assets during a liquidation. To the extent that investors choose money market funds over alternative investments because the rule provides reassurance as to the protection of fund assets in the event a money market fund breaks the buck, the rule also may promote capital formation. If, however, the possibility that redemptions may be suspended during a liquidation makes money market funds less appealing to investors, the rule may have a negative effect on capital formation. The rule also may help make investors more confident that they will receive the proceeds from their investment in the event of a liquidation. We do not believe that the rule will have any adverse effect on competition. We received no comments on this analysis.

D. Rule 30b1-7 and Form N-MFP: Monthly Reporting of Portfolio Holdings

New rule 30b1-7 and Form N-MFP mandate the monthly electronic filing of each money market fund's portfolio holdings information in XML-tagged format. As discussed above, we believe the new reporting requirement will improve the efficiency and effectiveness of the Commission's oversight of money

market funds. The availability, and usability, of this data will also promote efficiency for other third parties that may be interested in collecting and analyzing money market funds' portfolio holdings information. Money market funds currently are often required to provide this information to various third parties in different formats. To the extent that the new reporting requirement may encourage a standardized format for disclosure or transmission of portfolio holdings information, it may promote efficiency for money market funds. We do not believe that the reporting requirement will have an adverse effect on capital formation.

In the Proposing Release, we requested comment on what effect the proposed rule⁶³⁰ would have on competition, efficiency, and capital formation.⁶³¹ One commenter stated that the Commission's view that the proposed rule would not have an adverse effect on competition may be incorrect for subadvised money market funds, because a number of the information items in Form N-MFP require information that typically is in the possession of the subadviser who manages the portfolio and not the principal adviser who, in most cases, would be responsible for preparing Form N-MFP. The commenter stated that obtaining the data from subadvisers would be costly because it would have to be done on a real-time basis, which would require a significant investment in new infrastructure.⁶³² The information required by the items cited by the commenter, however, already should be readily available to the subadviser.⁶³³ The information also is

⁶³⁰ The rule was proposed as rule 30b1-6. As noted above, in September 2009 we adopted interim final temporary rule 30b1-6T. We therefore have adopted proposed rule 30b1-6 as rule 30b1-7.

⁶³¹ See Proposing Release, *supra* note 2, at Section VI.D.

⁶³² See Committee Ann. Insur. Comment Letter. In particular, the commenter stated that the information required by Items 17 (dollar weighted average life maturity), 20 (CIK of the issuer of security), 26(b) (credit rating given by the NRSROs for the security), and 30-35 (information on enhancements) of proposed Form N-MFP are not typically in the possession of the principal adviser and must be obtained from the subadviser managing the portfolio. The commenter asserted that the Commission's estimate of 128 burden hours per money market fund for the first year (1 filing × 40 hours + 11 filings × 8 hours) is far too low for subadvised funds. For the reasons discussed below, we do not believe that subadvised funds would be subject to significant investment in new infrastructure and thus we believe that the burden estimate is not too low for subadvised funds. The commenter does not state that there would be any ongoing additional costs for compliance with Form N-MFP by subadvised money market funds.

⁶³³ Subadvisers must have all of the information required by the particular items the commenter

⁶²⁸ See amended rule 17a-9(a).

⁶²⁹ See amended rule 17a-9(b).

not needed on a real-time basis by the principal adviser because the form requires information as of the last business day of the preceding month. Moreover, we have lengthened the time for filing Form N-MFP from the proposed two business days after the end of each month to five business days after the end of each month. This change should provide subadvisers with sufficient time to send the information to the principal adviser without having to invest in new infrastructure to provide the information on a real-time basis.⁶³⁴ We therefore continue to believe that the reporting requirement will not have an adverse effect on competition.

The amendments also will require the public disclosure of a money market fund's market-based net asset value. We expect that the disclosure of month-end market-based NAV may discourage the fund's portfolio manager from taking certain risks that could reduce the fund's market-based NAV. The money market fund industry is characterized by a mix of competitors with and without affiliates that can provide financial support. The new disclosure might encourage funds that have affiliates with the ability to provide financial support to request such support as soon as any problems develop. This support could provide stability to funds that receive the support. This support might also give a competitive advantage to funds that receive it because they may be more willing to invest in securities with higher risk and higher yields. However, the extent of this competitive advantage may be mitigated because the amendments will require the disclosure of the fund's market-based NAV with and without capital support agreements. In addition, much of the extent to which fund managers might take advantage of capital support arrangements to boost fund yields is independent of the amendments we are adopting today and affiliated persons of money market funds are not obligated to support these funds.

The disclosure of a market-based net asset value below \$1.00 also might precipitate a run on the fund. If one fund were to fail for this reason, runs might develop in other money market

specifies in order to manage the portfolio on a day-to-day basis in compliance with rule 2a-7, other than an issuer's CIK. Under Form N-MFP, as adopted, the CIK of the issuer of the security is only required if the security does not have a CUSIP and the issuer has a CIK. Under our proposal the CIK number of the issuer would have been required for all securities.

⁶³⁴ By increasing the deadline to five business days, filers also will have at least two non-business days (in addition to the extra three business days) in which to complete and submit the form.

funds, even those with relatively high market-based net asset values. However, we believe that shareholders will benefit from knowing the monthly market-based net asset values of money market funds. We anticipate that the public availability of these values will help investors make informed decisions about whether to invest, or maintain their investments, in money market funds. We also anticipate that retail investors over time will become acclimated to the market-based net asset value information that money market funds will be required to disclose, and that most of those investors will not likely make decisions based on immaterial changes to funds' portfolio values. In response to concerns expressed by some commenters about the potential for harm that immediate public disclosure may pose for funds, we will delay for 60 days after the end of the reporting period, public disclosure of the information filed on Form N-MFP, including the market-based net asset values.⁶³⁵

E. Rule 30b1-6T

Rule 30b1-6T is intended to facilitate oversight of money market funds that present a greater risk that they will be unable to maintain their primary investment objectives. As noted above, the nonpublic reports are designed to improve the efficiency and effectiveness of the Commission's oversight of such money market funds, which may also provide reassurance to investors, which may in turn promote capital formation. We do not believe that the rule will have any effect on competition.

VII. Regulatory Flexibility Act Certification

The Commission certified, pursuant to section 605(b) of the Regulatory Flexibility Act of 1980 that the proposed amendments to rules 2a-7, 17a-9, and 30b1-5, and proposed rules 30b1-6 and 22e-3 under the Investment Company Act would not have a significant economic impact on a substantial number of small entities.⁶³⁶ We included this certification in Section VII of the Proposing Release. Although we encouraged written comments regarding

⁶³⁵ See *supra* Section I.IE.2.

⁶³⁶ 5 U.S.C. 605(b). Based on information in filings submitted to the Commission, we believe that there are no money market funds that are small entities. Under rule 0-10 under the Investment Company Act, an investment company is considered a small entity 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.

this certification, no commenters responded to this request.⁶³⁷

VIII. Statutory Authority

The Commission is adopting amendments to rule 2a-7 under the exemptive and rulemaking authority set forth in sections 6(c), 8(b), 22(c), and 38(a) of the Investment Company Act [15 U.S.C. 80a-6(c), 80a-8(b), 80a-22(c), 80a-37(a)]. The Commission is adopting amendments to rule 17a-9 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), 80a-37(a)]. The Commission is adopting 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 adopting an amendment to rule 30b1-6T 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 adopting new 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)].

List of Subjects in 17 CFR Parts 270 and 274

Investment companies, Reporting and recordkeeping requirements, Securities.

Text of Rules, Rule Amendments, and Form

■ For reasons set out in the preamble, Title 17, Chapter II of the Code of Federal Regulations is amended as follows:

PART 270—RULES AND REGULATIONS, INVESTMENT COMPANY ACT OF 1940

■ 1. 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.

* * * * *

■ 2. Section 270.2a-7 is revised to read as follows:

§ 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).

⁶³⁷ We also certified that rule 30b1-6T would not have a significant economic impact on a substantial number of small entities. See Rule 30b1-6T Release, *supra* note 303, at Section VIII. We received no comment on that certification.

(2) *Amortized Cost Method of valuation* means the method of calculating an investment company's net asset value whereby portfolio securities are valued at the fund's Acquisition cost as adjusted for amortization of premium or accretion of discount rather than at their 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), substantially all of the assets of which consist of Qualifying Assets (as defined in this paragraph). *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* means "Collateralized Fully" 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) 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; or

(iii) Securities that will mature or are subject to a Demand Feature that is exercisable and payable within one Business Day.

(9) *Demand Feature* means:

(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.

(10) *Demand Feature Issued By A Non-Controlled Person* means a Demand Feature 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 Demand Feature (*control* means "control" 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.

(11) *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.

(12) *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)(12)(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).

(13) *Event of Insolvency* means "Event of Insolvency" as defined in § 270.5b-3(c)(2).

(14) *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)(14)(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.

(15) *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.

(16) *Government Security* means any "Government security" as defined in section 2(a)(16) of the Act (15 U.S.C. 80a-2(a)(16)).

(17) *Guarantee* 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 exercise 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).

(18) *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* means "control"

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.

(19) *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.

(20) *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.

(21) *Rated Security* means a security that meets the requirements of paragraphs (a)(21)(i) or (ii) of this section, in each case subject to paragraph (a)(21)(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)(21)(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)(21)(ii) of this section.

(22) *Refunded Security* means "Refunded Security" as defined in § 270.5b-3(c)(4).

(23) *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.

(24) *Second Tier Security* means any Eligible Security that is not a First Tier Security.

(25) *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.

(26) *Tax Exempt Fund* means any money market fund that holds itself out as distributing income exempt from regular Federal income tax.

(27) *Total Assets* means, with respect to a money market fund using the Amortized Cost Method, the total amortized cost of its assets and, with respect to any other money market fund, the total market-based value of its assets.

(28) *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.

(29) *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.

(30) *Unrated Security* means a security that is not a Rated Security.

(31) *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.

(32) *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; and

(B) Have a remaining maturity date of 60 days or less; or

(iv) Securities that will mature or are subject to a Demand Feature that is exercisable and payable within five Business Days.

(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 meets the conditions of paragraphs (c)(2), (c)(3), (c)(4), and (c)(5) of 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 meets the conditions of paragraphs (c)(2), (c)(3), (c)(4), and (c)(5) of this section.

(3) For purposes of this paragraph, a name that suggests that a registered investment company is a money market fund or the equivalent thereof shall include 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 thereunder, may be computed by use of the Amortized Cost Method or the Penny-Rounding Method; provided, however, that:

(1) *Board Findings.* The board of directors of the money market fund

shall determine, in good faith, that it is in the best interests of the fund and its shareholders to maintain a stable net asset value per share or stable price per share, by virtue of either the Amortized Cost Method or the Penny-Rounding Method, and that the money market fund will continue to use such method only so long as the board of directors believes that it fairly reflects the market-based net asset value per share.

(2) *Portfolio Maturity.* The money market fund shall maintain a dollar-weighted average portfolio maturity appropriate to its objective of maintaining a stable net asset value per share or price per share; provided, however, that the money market fund will not:

(i) Acquire any instrument with a remaining maturity of greater than 397 calendar days;

(ii) Maintain a dollar-weighted average portfolio maturity 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 (d) of this section regarding interest rate readjustments.

(3) *Portfolio Quality—(i) General.* The money market fund shall 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 shall Acquire a Second Tier Security with a remaining maturity of greater than 45 calendar days. Immediately after the Acquisition of any Second Tier Security, a money market fund shall 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.

(4) *Portfolio Diversification—(i) Issuer Diversification.* The money market fund shall be diversified with respect to issuers of securities Acquired by the fund as provided in paragraphs (c)(4)(i) and (c)(4)(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 shall not have invested more than 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.

(B) *Single State Funds.* With respect to seventy-five percent of its Total Assets, immediately after the Acquisition of any security, a Single

State Fund shall not have invested more than five percent of its Total Assets in securities issued by the issuer of the security.

(C) *Second Tier Securities.*

Immediately after the Acquisition of any Second Tier Security, a money market fund shall not have invested more than one half of one percent of its Total Assets in the Second Tier Securities of any single issuer.

(ii) *Issuer Diversification Calculations.* For purposes of making calculations under paragraph (c)(4)(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 (c)(4)(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 shall satisfy the diversification requirements of paragraph (c)(4)(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 (c)(4)(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.

(iii) *Diversification Rules for Demand Features and Guarantees.* The money market fund shall be diversified with respect to Demand Features and Guarantees Acquired by the fund as provided in paragraphs (c)(4)(iii) and (c)(4)(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 or security subject to a Demand Feature or Guarantee, a money market fund, with respect to seventy-five percent of its Total Assets, shall 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, subject to paragraphs (c)(4)(iii)(B) and (C) of this section.

(B) *Second Tier Demand Features or Guarantees.* Immediately after the Acquisition of any Demand Feature or Guarantee (or a security after giving effect to the Demand Feature or Guarantee) that is a Second Tier Security, a money market fund shall 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.

(C) *Demand Features or Guarantees Issued by Non-Controlled Persons.* Immediately after the Acquisition of any security subject to a Demand Feature or Guarantee, a money market fund shall

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, unless, with respect to any security subject to Demand Features or Guarantees from that institution (other than securities issued by such institution), the Demand Feature or Guarantee is a Demand Feature or Guarantee Issued By A Non-Controlled Person.

(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 (c)(4)(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 (c)(4) and (c)(6) 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.

(5) *Portfolio Liquidity.* The money market fund shall 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 shall 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 shall 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 shall not apply to Tax Exempt Funds.

(iii) *Minimum Weekly Liquidity Requirement.* The money market fund shall 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.

(6) *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 (c)(3) of this section), or maturity (pursuant to paragraph (d) of this section), or liquidity of a portfolio security, and maintains a record of this determination (pursuant to paragraphs (c)(10)(ii) and (c)(11)(vi) of this section), then the fund may disregard such Demand Feature or Guarantee for all purposes of this section.

(7) *Downgrades, Defaults and Other Events—(i) Downgrades—(A) General.* Upon the occurrence of either of the events specified in paragraphs (c)(7)(i)(A)(1) and (2) 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 and its shareholders:

(1) 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

(2) 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.

(B) *Securities To Be Disposed Of.* The reassessments required by paragraph (c)(7)(i)(A) 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 (c)(7)(i)(A)(2) of this section, the board is subsequently notified of the adviser's actions.

(C) *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.

(ii) *Defaults and Other Events.* Upon the occurrence of any of the events specified in paragraphs (c)(7)(ii)(A) through (D) 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):

(A) The default with respect to a portfolio security (other than an immaterial default unrelated to the financial condition of the issuer);

(B) A portfolio security ceases to be an Eligible Security;

(C) A portfolio security has been determined to no longer present minimal credit risks; or

(D) An Event of Insolvency occurs with respect to the issuer of a portfolio security or the provider of any Demand Feature or Guarantee.

(iii) *Notice to the Commission.* The money market fund shall promptly notify the Commission by electronic mail directed to the Director of Investment Management or the Director's designee, of any:

(A) Default or Event of Insolvency with respect to the issuer of one or more portfolio securities (other than an immaterial default unrelated to the financial condition of the issuer) or any issuer of a Demand Feature or Guarantee to which one or more portfolio securities is subject, and the actions the money market fund intends to take in response to such event, where immediately before default the securities (or the securities subject to the Demand Feature or Guarantee) accounted for ½ of 1 percent or more of

the money market fund's Total Assets; or

(B) Purchase of a security from the fund by an affiliated person, promoter, or principal underwriter of the fund, or an affiliated person of such a person, in reliance on § 270.17a-9, including identification of the security, its amortized cost, the sale price, and the reasons for such purchase.

(iv) *Defaults for Purposes of Paragraphs (c)(7)(ii) and (iii).* For purposes of paragraphs (c)(7)(ii) and (iii) 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:

(A) 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; or

(B) The provider of the Guarantee is continuing, without protest, to make payments as due on the instrument.

(8) *Required Procedures: Amortized Cost Method.* In the case of a money market fund using the Amortized Cost Method:

(i) *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, shall establish written procedures reasonably designed, taking into account current market conditions and the money market fund's investment objectives, to stabilize the money market fund's net asset value per share, as computed for the purpose of distribution, redemption and repurchase, at a single value.

(ii) *Specific Procedures.* Included within the procedures adopted by the board of directors shall be the following:

(A) *Shadow Pricing.* Written procedures shall provide:

(1) That the extent of deviation, if any, of the current net asset value per share calculated using available market quotations (or an appropriate substitute that reflects current market conditions) from the money market fund's amortized cost price per share, shall be calculated at such intervals as the board of directors determines appropriate and reasonable in light of current market conditions;

(2) For the periodic review by the board of directors of the amount of the

deviation as well as the methods used to calculate the deviation; and

(3) For the maintenance of records of the determination of deviation and the board's review thereof.

(B) *Prompt Consideration of Deviation.* In the event such deviation from the money market fund's amortized cost price per share exceeds $\frac{1}{2}$ of 1 percent, the board of directors shall promptly consider what action, if any, should be initiated by the board of directors.

(C) *Material Dilution or Unfair Results.* Where the board of directors believes the extent of any deviation from the money market fund's amortized cost price per share may result in material dilution or other unfair results to investors or existing shareholders, it shall cause the fund to take such action as it deems appropriate to eliminate or reduce to the extent reasonably practicable such dilution or unfair results.

(9) *Required Procedures: Penny-Rounding Method.* In the case of a money market fund using the Penny-Rounding Method, 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 undertakes, as a particular responsibility within the overall duty of care owed to its shareholders, to assure to the extent reasonably practicable, taking into account current market conditions affecting the money market fund's investment objectives, 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 single price established by the board of directors.

(10) *Specific Procedures: Amortized Cost and Penny-Rounding Methods.* Included within the procedures adopted by the board of directors for money market funds using either the Amortized Cost or Penny-Rounding Methods shall be the following:

(i) *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 (c)(3)(iv) of this section, whether such data is publicly available or provided under the terms of the security's governing documentation.

(ii) *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 (c)(3) of this section), maturity (pursuant to paragraph (d) of this section) or liquidity (pursuant to paragraph (c)(5) of this section) of the security subject to the Demand Feature or Guarantee, written procedures shall require periodic evaluation of such determination.

(iii) *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 paragraphs (d)(1), (d)(2) or (d)(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.

(iv) *Asset Backed Securities.* In the case of an Asset Backed Security, written procedures shall require the fund to periodically determine the number of Ten Percent Obligor (as that term is used in paragraph (c)(4)(ii)(D) of this section) deemed to be the issuers of all or a portion of the Asset Backed Security for purposes of paragraph (c)(4)(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 Obligor that are deemed to be issuers of all or a portion of that Asset Backed Security for purposes of paragraph (c)(4)(ii)(D) of this section, and maintains a record of this determination.

(v) *Stress Testing.* Written procedures shall provide for:

(A) 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 a stable net asset value per share based upon specified hypothetical events that include, but are not limited to, 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 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.

(B) 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 shall include:

(1) The date(s) on which the testing was performed and the magnitude of each hypothetical event that would cause the deviation of the money market fund's net asset value calculated using available market quotations (or appropriate substitutes which reflect current market conditions) from its net asset value per share calculated using amortized cost to exceed $\frac{1}{2}$ of 1 percent; and

(2) 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.

(11) *Record Keeping and Reporting—*
(i) *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 (c)(7) through (c)(10) and (e) of this section shall be maintained and preserved.

(ii) *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 shall 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.

(iii) *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.

(iv) *Determinations With Respect to Adjustable Rate Securities.* For a period of not less than three years from the date when the determination was most recently made, a written record shall be preserved and maintained, in an easily accessible place, of the determination

required by paragraph (c)(10)(iii) 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 paragraphs (d)(1), (d)(2) or (d)(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).

(v) *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 shall be preserved and maintained, in an easily accessible place, of the determinations required by paragraph (c)(10)(iv) of this section (the number of Ten Percent Obligor (as that term is used in paragraph (c)(4)(ii)(D) of this section) deemed to be the issuers of all or a portion of the Asset Backed Security for purposes of paragraph (c)(4)(ii)(D) of this section). The written record shall include:

(A) The identities of the Ten Percent Obligor (as that term is used in paragraph (c)(4)(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

(B) Any determination that an Asset Backed Security will not have, or is unlikely to have, Ten Percent Obligor deemed to be issuers of all or a portion of that Asset Backed Security for purposes of paragraph (c)(4)(ii)(D) of this section.

(vi) *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 shall be preserved and maintained, in an easily accessible place, of the evaluation required by paragraph (c)(10)(ii) (regarding securities subject to one or more Demand Features or Guarantees) of this section.

(vii) *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 (c)(10)(v)(B) of this section shall be maintained and preserved.

(viii) *Inspection of Records.* The documents preserved pursuant to this paragraph (c)(11) shall be 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)). If any action was taken under paragraphs (c)(7)(ii) (with respect to defaulted securities and events of insolvency) or (c)(8)(ii) (with respect to a deviation from the fund's share price of more than 1/2 of 1 percent) of this section, the money market fund will file an exhibit to the Form N-SAR (17 CFR 274.101) filed for the period in which the action was taken describing with specificity the nature and circumstances of such action. The money market fund will report in an exhibit to such Form any securities it holds on the final day of the reporting period that are not Eligible Securities.

(12) *Web Site Disclosure of Portfolio Holdings.* The money market fund shall post on its Web site, 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 of the prior month, that includes the following information:

(i) With respect to the money market fund and each class thereof:

(A) The dollar-weighted average portfolio maturity; and

(B) The dollar-weighted average portfolio maturity determined without reference to the exceptions in paragraph (d) of this section regarding interest rate readjustments;

(ii) With respect to each security held by the money market fund:

(A) Name of the issuer;

(B) Category of investment (indicate the category that most closely identifies the instrument from among the following: Treasury Debt; Government Agency Debt; Variable Rate Demand Note; Other Municipal Debt; Financial Company Commercial Paper; Asset Backed Commercial Paper; Other Commercial Paper; Certificate of Deposit; Structured Investment Vehicle Note; Other Note; Treasury Repurchase Agreement; Government Agency Repurchase Agreement; Other Repurchase Agreement; Insurance Company Funding Agreement; Investment Company; Other Instrument);

(C) CUSIP number (if any);

(D) Principal amount;

(E) Maturity date as determined under this section;

(F) Final legal maturity date (taking into account any maturity date extensions that may be effected at the option of the issuer), if different from the maturity date as determined under this section;

(G) Coupon or yield; and

(H) Amortized cost value; and

(iii) 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.

(13) *Processing of Transactions.* The money market fund (or its transfer agent) shall 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 shall include the ability to redeem and sell securities at prices that do not correspond to a stable net asset value or price per share.

(d) *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 (d)(1) through (d)(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.

(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.

(e) *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)(11)(i) (designation of NRSROs); (c)(1) (board findings); (c)(7)(ii) (defaults and other events); (c)(8)(i) (general required procedures: Amortized Cost Method); (c)(8)(ii)(A) (shadow pricing), (B) (prompt consideration of deviation), (C) (material dilution or unfair results); (c)(9) (required procedures: Penny Rounding Method); and (c)(10)(v)(A) (stress testing procedures) of this section; provided that:

(1) *Written Guidelines.* The Board shall establish and periodically review written guidelines (including guidelines for determining whether securities present minimal credit risks as required

in paragraph (c)(3) of this section) and procedures under which the delegate makes such determinations.

(2) *Oversight.* The Board shall 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 to which it is subject that requires notification of the Commission under paragraph (c)(7)(iii) of this section) to assure that the guidelines and procedures are being followed.

■ 3. Section 270.17a-9 is revised to read as follows:

§ 270.17a-9 Purchase of certain securities from a money market fund by an affiliate, or an affiliate of an affiliate.

The purchase of a security from the portfolio of an open-end investment company holding itself out as a money market fund by any affiliated person or promoter of or principal underwriter for the money market fund or any affiliated person of such person shall be exempt from section 17(a) of the Act (15 U.S.C. 80a-17(a)); provided that:

(a) In the case of a portfolio security that has ceased to be an Eligible Security (as defined in § 270.2a-7(a)(12)), or has defaulted (other than an immaterial default unrelated to the financial condition of the issuer):

(1) The purchase price is paid in cash; and

(2) The purchase price is equal to the greater of the amortized cost of the security or its market price (in each case, including accrued interest).

(b) In the case of any other portfolio security:

(1) The purchase price meets the requirements of paragraph (a)(1) and (2) of this section; and

(2) In the event that the purchaser thereafter sells the security for a higher price than the purchase price paid to the money market fund, the purchaser shall promptly pay to the fund the amount by which the subsequent sale price exceeds the purchase price paid to the fund.

■ 4. Section 270.22e-3 is added to read as follows:

§ 270.22e-3 Exemption for liquidation of money market funds.

(a) *Exemption.* A registered open-end management investment company or series thereof ("fund") that is regulated as a money market fund under § 270.2a-7 is exempt from the requirements of section 22(e) of the Act (15 U.S.C. 80a-22(e)) if:

(1) The fund's board of directors, including a majority of directors who are not interested persons of the fund, determines pursuant to § 270.2a-7(c)(8)(ii)(C) that the extent of the deviation between the fund's amortized cost price per share and its current net asset value per share calculated using available market quotations (or an appropriate substitute that reflects current market conditions) may result in material dilution or other unfair results to investors or existing shareholders;

(2) The fund's board of directors, including a majority of directors who are not interested persons of the fund, irrevocably has approved the liquidation of the fund; and

(3) The fund, prior to suspending redemptions, notifies the Commission of its decision to liquidate and suspend redemptions by electronic mail directed to the attention of the Director of the Division of Investment Management or the Director's designee.

(b) *Conduits.* Any registered investment company, or series thereof, that owns, pursuant to section 12(d)(1)(E) of the Act (15 U.S.C. 80a-12(d)(1)(E)), shares of a money market fund that has suspended redemptions of shares pursuant to paragraph (a) of this section also is exempt from the requirements of section 22(e) of the Act (15 U.S.C. 80a-22(e)). A registered investment company relying on the exemption provided in this paragraph must promptly notify the Commission that it has suspended redemptions in reliance on this section. Notification under this paragraph shall be made by electronic mail directed to the attention of the Director of the Division of Investment Management or the Director's designee.

(c) *Commission Orders.* For the protection of shareholders, the Commission may issue an order to rescind or modify the exemption provided by this section, after appropriate notice and opportunity for hearing in accordance with section 40 of the Act (15 U.S.C. 80a-39).

■ 5. Section 270.30b1-6T is amended by revising paragraph (d) to read as follows:

§ 270.30b1-6T Weekly portfolio report for certain money market funds.

* * * * *

(d) *Expiration.* This section will expire on December 1, 2010.

■ 6. Section 270.30b1-7 is added to read as follows:

§ 270.30b1-7 Monthly report for money market funds.

(a) *Report.* 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 of the previous month, no later than the fifth business day of each month.

(b) *Public availability.* The Commission will make the information filed on Form N-MFP available to the public 60 days after the end of the month to which the information pertains.

PART 274—FORMS PRESCRIBED UNDER THE INVESTMENT COMPANY ACT OF 1940

■ 7. 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), 78l, 78m, 78n, 78o(d), 80a-8, 80a-24, 80a-26, and 80a-29, unless otherwise noted.

* * * * *

■ 8. Section 274.201 and Form N-MFP (referenced in § 274.201) are added to read as follows:

§ 274.201 Form N-MFP, portfolio holdings of money market funds.

This form shall be used by registered open-end management investment companies that are regulated as money market funds under § 270.2a-7 of this chapter to file reports pursuant to § 270.30b1-7 of this chapter no later than the fifth business day of each month.

Note: The text of Form N-MFP 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 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 I.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:

“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.

“Master-Feeder Fund” means a two-tiered arrangement in which one or more Funds (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 maturity, quality, and diversification 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)].

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM N-MFP MONTHLY SCHEDULE OF PORTFOLIO HOLDINGS OF MONEY MARKET FUNDS

Report for [Month, Day, Year]

CIK Number of Registrant:

EDGAR Series Identifier:

Total number of share classes in the series:

Do you anticipate that this will be the fund’s final filing on Form N-MFP? [Y/N]

Is the fund liquidating? [Y/N]

Is the fund merging with, or being acquired by, another fund? [Y/N]

If so, identify the successor fund by CIK, Securities Act file number, and EDGAR series identifier.

If this is not a final filing: has the fund acquired or merged with another fund since the last filing? [Y/N]

If so, identify the acquired or merged fund by CIK, Securities Act file number, and EDGAR series identifier.

Part I: Information about the Fund

A. Series-Level Information

- Item 1. Securities Act File Number.
- Item 2. Investment Adviser.
- a. SEC file number of investment adviser.
- Item 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 4. Independent Public Accountant.
- a. City and state of independent public accountant.
- Item 5. Administrator. If a fund has one or more administrators, disclose the name of each administrator.
- Item 6. Transfer Agent.
- a. CIK Number.
- b. SEC file number of transfer agent.
- Item 7. Master-Feeder Funds. Is this a feeder fund? [Y/N]
- a. Identify the master fund by CIK.
- b. Securities Act file number of the master fund.
- c. EDGAR series identifier of the master fund.
- Item 8. Master-Feeder Funds. Is this a master fund? [Y/N]
- a. If this is a master fund, 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 9. Is this series primarily used to fund insurance company separate accounts? [Y/N]
- Item 10. Category. Indicate the category that most closely identifies the money market fund from among the following: Treasury, Government/ Agency, Prime, Single State Fund, or Other Tax Exempt Fund.
- Item 11. Dollar weighted average portfolio maturity.
- Item 12. Dollar weighted average life maturity. Calculate the dollar weighted average portfolio maturity without reference to the exceptions in rule 2a-7(d) regarding interest rate readjustments.
- Item 13. Total value of portfolio securities at amortized cost, to the nearest cent.
- Item 14. Total value of other assets, to the nearest cent.
- Item 15. Total value of liabilities, to the nearest cent.
- Item 16. Net assets of the series, to the nearest cent.
- Item 17. 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 at least the nearest hundredth of one percent. The 7-day gross yield should not reflect a deduction of shareholders fees and fund operating expenses.

- Item 18. Shadow Price of the Series.
- a. The net asset value per share most recently calculated using available market quotations (or an appropriate substitute that reflects current market conditions), including the value of any capital support agreement, to the nearest hundredth of a cent;
- b. The date as of which the market-based net asset value disclosed in Item 18a was calculated;
- c. The net asset value per share most recently calculated using available market quotations (or an appropriate substitute that reflects current market conditions), excluding the value of any capital support agreement, to the nearest hundredth of a cent; and
- d. The date as of which the market-based net asset value disclosed in Item 18c was calculated.

B. Class-Level Information. For each Class of the Series, disclose the following:

- Item 19. EDGAR Class identifier.
- Item 20. Minimum initial investment.
- Item 21. Net assets of the Class, to the nearest cent.
- Item 22. Net asset value per share for purposes of distributions, redemptions, and repurchase, to the nearest cent.
- Item 23. Net shareholder flow activity for the month ended (subscriptions less redemptions), to the nearest cent.
- a. Gross subscriptions for the month ended (including dividend reinvestments), to the nearest cent.
- b. Gross redemptions for the month ended, to the nearest cent.
- Item 24. 7-day net yield, as calculated under Item 26(a)(1) of Form N-1A.
- Item 25. Shadow Price of each Class.
- a. The net asset value per share most recently calculated using available market quotations (or an

appropriate substitute that reflects current market conditions), including the value of any capital support agreement, to the nearest hundredth of a cent;

- b. The date as of which the market-based net asset value disclosed in Item 25a was calculated;
- c. The net asset value per share most recently calculated using available market quotations (or an appropriate substitute that reflects current market conditions), excluding the value of any capital support agreement, to the nearest hundredth of a cent; and
- d. The date as of which the market-based net asset value disclosed in Item 25c was calculated.

Part 2: Schedule of Portfolio Securities. For each security held by the money market fund, disclose the following:

- Item 26. The name of the issuer.
- Item 27. The title of the issue (including coupon or yield).
- Item 28. The CUSIP. If the security has a CUSIP, filers must provide the security's CUSIP pursuant to this Item and may skip Items 29 and 30.
- Item 29. Other unique identifier, if the security has a unique identifier. If a CUSIP is provided pursuant to Item 28, skip this Item.
- Item 30. The CIK of the issuer, if the issuer has a CIK. If a CUSIP is provided pursuant to Item 28, skip this Item.
- Item 31. The category of investment. Indicate the category that most closely identifies the instrument from among the following: Treasury Debt; Government Agency Debt; Variable Rate Demand Note; Other Municipal Debt; Financial Company Commercial Paper; Asset Backed Commercial Paper; Other Commercial Paper; Certificate of Deposit; Structured Investment Vehicle Note; Other Note; 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 32. 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]
- For repurchase agreements, describe the securities subject to the repurchase agreement, including:

- a. The name of the issuer;
 b. Maturity date;
 c. Coupon or yield;
 d. The category of investments, selected from Item 31 above;
 e. The principal amount, to the nearest cent;
 f. Value of collateral, to the nearest cent.
- 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 33. 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 34. 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 35. The maturity date as determined under rule 2a-7. Determine the maturity date, taking into account the maturity shortening provisions of rule 2a-7(d).
- Item 36. The final legal maturity date, taking into account any maturity date extensions that may be effected at the option of the issuer.
- Item 37. Does the security have a Demand Feature? [Y/N]
- a. The identity of the Demand Feature issuer.
- b. Designated NRSRO(s) for the Demand Feature or provider of the Demand Feature.
- 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."
- Item 38. Does the security have a Guarantee? [Y/N]
- a. The identity of the Guarantor.
- b. Designated NRSRO(s) for the Guarantee or Guarantor.
- 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."
- Item 39. Does the security have any enhancements, other than those identified in Items 37 and 38 above, on which the fund is relying to determine the quality, maturity or liquidity of the security? [Y/N]
- a. The type of enhancement.
- b. The identity of the enhancement provider.
- c. Designated NRSRO(s) for the enhancement or enhancement provider.
- 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."
- Item 40. The total principal amount of the security held by the series, to the nearest cent.
- Item 41. The total current amortized cost, to the nearest cent.
- Item 42. The percentage of the money market fund's net assets invested in the security, to the nearest hundredth of a percent.
- Item 43. Explanatory notes. Disclose any other information that may be material to other disclosures related to the portfolio security.
- Item 44. Is this an Illiquid Security as of the date of this report? [Y/N]
- Item 45. The value of the security, calculated using available market quotations (or an appropriate substitute that reflects current market conditions), including the value of any capital support agreement, to the nearest cent.
- Item 46. The value of the security, calculated using available market quotations (or an appropriate substitute that reflects current market conditions), excluding the value of any capital support agreement, to the nearest cent.

Dated: February 23, 2010.

By the Commission.

Elizabeth M. Murphy,
Secretary.

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