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19 September 2013

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

Re: Money Market Fund Reform; Amendments to Form PF (File No. S7-03-13)

Dear Ms. Murphy:

CFA Institute[1] appreciates the opportunity to comment on the SEC's proposal for amending rules governing money market mutual funds ("money market funds"). As stated in an earlier letter to the Financial Stability Oversight Council, we believe that the SEC is in the best position to address any needed reforms to money market funds, and thus applaud its formulation of a proposal.

CFA Institute represents the views of investment professionals before standard setters, regulatory authorities, and legislative bodies worldwide on issues that affect the practice of financial analysis and investment management, education and licensing requirements for investment professionals, and on issues that affect the efficiency, integrity and accountability of global financial markets.

Executive Summary

Systemic Risk. CFA Institute shares deep concern about the systemic risk implications of the current money market fund industry and strongly supports the SEC's undertaking through this proposal to begin to address them. We believe that both alternatives presented in the proposal for reforming the money market fund industry have merits. We support Alternative One as the one most likely to address systemic risk while minimizing the disruption to markets and investor confusion.

Floating NAV. CFA Institute has long advocated for fair-value reporting for financial reporting and with regard to financial instruments. We believe it provides investors with a more accurate picture of an entity's financial condition. We thus agree with requiring institutional money market funds (as defined in the proposal) to use a floating NAV. While Alternative One allows Retail and Government funds (as defined)

[1] CFA Institute is a global, not-for-profit professional association of more than 122,600 investment analysts, advisers, portfolio managers, and other investment professionals in 142 countries, of whom nearly 115,000 hold the Chartered Financial Analyst® (CFA®) designation. The CFA Institute membership also includes 138 member societies in 60 countries and territories.

to continue using a stable NAV, we encourage further regulatory or industry-driven action ultimately to move *all* money market funds, including Retail and Government funds, to a floating NAV pricing method.

Investor Options. We believe in providing investors with options by allowing sponsors to offer money market funds with different structures wherever practicable and provided that they a) are required to provide investors with meaningful disclosures that fully address the investment risks and b) do not put the financial system at risk of collapse.

Thus, while we recognize the current confusion surrounding investing in money market funds with a stable NAV, we believe the proposed disclosure requirements go a long way toward mitigating this confusion. As noted above, we hope that over time, investors will appreciate the benefits/value of investing in floating NAV funds and that the industry will, of its own accord, move in that direction without the need for regulatory intervention.

Discussion

Needed reforms to money market funds have focused primarily on two areas: (1) concerns about the potential systemic risk posed by the funds and (2) the misperception by investors that investments in money market funds are essentially risk-free. We believe that the SEC's proposal is a pragmatic attempt to balance these concerns.

As recognized and hotly debated over the last years, changes to the money market fund industry raise a host of complicated issues. In particular, reliance upon money market funds as a vehicle for cash management and short-term funding by many institutions, including municipalities, has reinforced a call to retain a stable NAV. On the other hand, the effect on the market precipitated by Reserve Primary Fund's "breaking of the buck" — the start of an investor run that was quelled only with unprecedented and massive financial support from the U.S. federal government — highlighted the potential systemic risk implications embedded in retaining the current money market fund structure.

We agree that retail investors misperceive money market funds as risk-less investment vehicles and generally are unaware of past sponsor actions to stabilize the NAV at $1.00/share. Therefore, they are unaware of the potential for loss if there were a run on the fund in which those investors hold shares. It is these runs and the systemic risk implications that have particularly focused on the need for reform.

While some in the industry remain concerned about the dangers of allowing any money market funds to maintain a stable NAV, our members have not affirmatively taken that position. In an October 2012 CFA Institute survey of European and US members[2], only 39% of US respondents agreed that money market funds with a stable NAV should have to switch to a variable rate NAV. In the same survey, only 7% of total respondents (5% from the US and 19% from the EU) thought that only institutional investors should be allowed to invest in stable NAV money market funds. In keeping with these findings, we support the provisions in Alternative One that require institutional funds to use a floating NAV while allowing Retail and Government money market funds to continue pricing shares in accordance with a stable NAV, so long as important changes suggested below are made to what the SEC has proposed.

CFA Institute strongly supports efforts to reduce systemic risk in the financial markets. Moreover, we have a long-standing position that the reporting of financial instruments should reflect their fair values rather than amortized or historic values. And we have long held the belief that activities, instruments and/or services should be regulated in a manner similar to all other activities that are similar in nature. At the same time, we support providing investors with an optimal range of investment choices as long as strong investor and systemic risk protections accompany those options.

Alternative One—Variable and Stable NAV Options

As one alternative to the current structure, the SEC proposes to require prime institutional money market funds to use a floating NAV, with market-based valuation and rounding to the nearest basis point, or 1/100th of 1%. Money market funds described as Government and Retail under this Alternative would be exempted from the floating NAV requirements and could continue to use penny rounding. "Government funds" would be required to have at least 80% of total assets in cash, government securities or repurchase agreements collateralized with government securities. "Retail funds" would be defined as funds in which no single shareowner can redeem more than $1 million in a single day.

In general we agree with this proposal, but with important caveats, as described below.

A floating NAV is seen as a mechanism to discourage investor runs by reducing the advantage that first-redeemers have by getting out before other investors. It would do this by restricting redemptions to no more than their pro rata share of fund assets in times of stress when NAV drops below $1.00/share. By investing in funds with a

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[2] The survey was sent to CFA members in the European Union and a random sample of 15,000 members in the United States, to which 637 members responded. Results were re-weighted to reflect the differences in the response rates (57% from the US and 17% from the European Union). The breakdown in respondent preferences (while only 39% of US members favored such a switch, 53% of European Union respondents favored a change to a variable rate NAV) may reflect regional differences in regulatory treatment and use of money market funds.

fluctuating NAV, investors would also be put on notice that money funds are not guaranteed to maintain a $1.00 per share value.

CFA Institute has a longstanding position of supporting fair-value reporting in the belief that it provides investors a more accurate understanding of an entity's current financial condition. At the same time, we recognize the difficulties in applying a fair value requirement for some instruments that money market funds hold and the difficulties that a floating NAV would create for the fund firms, investment managers, and certain investors who are restricted from buying into such vehicles.

Nevertheless, Institutional funds (instead of Retail funds) are generally seen as more susceptible to runs of the type precipitated by Reserve Primary's breaking the buck in 2008, and thus the greatest source of systemic risk. These funds comprise nearly two-thirds of all money market funds, according to Investment Company Institute data, and Retail funds comprise most of the remainder. While the floating NAV provisions of Alternative One do not eliminate all risk from money market funds, subjecting what amounts to nearly two-thirds of the money funds market in the U.S. to this new requirement would be a substantial move toward addressing systemic risk concerns.

Consequently, we support the provision of Alternative one requiring institutional money market funds to float their NAV per share as a necessary and appropriate change in money market fund structure.

We are somewhat uneasy about the provision to permit institutional fund sponsors to financially support their funds as they determine. Our unease is due to the fact that such support might preserve the misconception among investors that these institutional funds will maintain a stable NAV. Nevertheless, these proposals include important improvements to the disclosure requirements about the risk of loss, which should remedy some of these concerns. Moreover, the willingness of sponsors to support the funds in times of stress is an important investor protection, though we would prefer a structure whereby the funds and/or their sponsors provide a capital support structure that wouldn't rely upon sponsor discretion.

We also believe the proposals for Government and Retail funds have problems that need correcting. First, we believe Government funds should have to invest much more of their assets in federal government — and federal agency — instruments or cash. A more appropriate percentage would be at least 95 percent. Our reasoning is that the 80 percent requirement in this Alternative would undermine the implied NAV stability of a Government funds structure. Allowing fund managers to invest as much as 20 percent of their assets in securities and instruments with greater volatility in value than government securities, while continuing to operate as stable NAV funds creates potential problems. This provision is particularly troubling when considering that Reserve Primary's problems developed because of a 3% decline in NAV caused by the default on 1.2% of its total assets which were invested in the unsecured commercial paper of Lehman Brothers.

With regard to Retail funds, we believe these funds should be restricted to truly retail investors, with maximum daily redemptions restricted to a more reasonable range—between $250,000 and $500,000. We also have concerns that omnibus accounts could create problems unless their ability to take advantage of such redemptions is either restricted or banned altogether from investing in such Retail funds. Should the SEC adopt this Alternative, we encourage it to provide clear guidance as to the types and applicability of restrictions for this purpose.

Ultimately, we believe that with these important changes, a stable NAV structure for Government and Retail funds would not pose a significant risk to the financial system. Over time, it is hoped that market forces may compel this sector of the industry also to adopt a fair-value approach.

Finally, the proposal has at least two other potential difficulties which we believe the SEC needs to address. First, funds typically offer classes of shares rather than separate funds for retail and institutional investors, which could make this proposal difficult to implement. Second, investors in floating rate money market funds would need to consider the tax and legal consequences/implications of investments that can generate gains and losses. While the Internal Revenue Service has said it is considering relief, there is no guarantee that a determination will eliminate the tax complexities created by a floating NAV.

Alternative Two—Fees and Gates

The second alternative would allow funds to continue valuing shares based on a stable NAV but only if in times of stress they take specific measures designed to curtail/prevent runs on the funds. Under this proposal, all except Government funds would have to meet two requirements in circumstances that are "not normal" and that could trigger an unusual rush by shareowners to redeem their shares.

First, if a fund's weekly liquid assets fall below 15% of its total assets, the fund would have to impose a 2% liquidity fee on redemptions unless the fund's board decides a lower fee, or no fee at all, would be in the fund's best interest. Second, once a fund's weekly liquidity threshold is reached, the board could also temporarily suspend redemptions (the "gate") for a period of time (not to exceed 30 days within any 90-day period) if the board decides it is in the fund's best interest.

The fees and gates approach intends to curb contagion in the industry during times of market stress by slowing down the rush to redeem. It also aims to spread out redemption costs among shareowners during those times by imposing fees on early redeemers and thus protecting those investors left behind with shares valued at less than $1.00 per share. Investors who otherwise might be early redeemers would be expected to reassess their options when faced with having to pay a liquidity fee, which in turn, could lend stability to a volatile time. This would ultimately benefit both individual investors in the fund and the market at large. We understand that imposition of the liquidity fee in times of stress is the "default" mechanism in that it will be imposed automatically, with the hope that redemption gates will not be needed.

CFA members have indicated that they do not prefer using liquidity fees to control risk. In the October 2012 CFA Institute survey, 85% of respondents agreed that all money market funds should have liquidity risk management mechanisms to manage runs on the fund, with 77% of US respondents and 81% of EU respondents indicating that those mechanisms should apply only in times of heavy redemptions or stressed markets. However, respondents in both the US and the EU strongly did *not* support the use of liquidity fees as a risk management tool, and favored the use of gates even less. The preferred option was a capital buffer for such funds.

If this Alternative is chosen, however, we recommend that fund managers forego their management fees during the times that such measures are in effect.

Proposals Aimed at Increasing Market Trust and Investor Protection

We appreciate that the SEC has proposed a number of measures intended to increase the transparency of money market fund risks and to strengthen the stability overall of the funds. We support these changes, regardless of which (if either) of the proposed Alternatives is adopted and believe they address concerns about the money market fund industry.

Enhanced and Additional Disclosures

The perception that money market funds maintain a stable NAV, while the primary attraction for most investors, has also conveyed a false sense of security. Many investors mistakenly have come to believe that investments in money market funds are riskless and guaranteed to maintain $1/share value. We strongly support required disclosures that correct these misconceptions. As noted in our earlier letter,[3] we particularly support prominent disclosure in all important communications highlighting that investments in these funds may be subject to loss of principal and interest.

As proposed, statements in prospectuses, advertisements, and sales materials for all floating NAV money market funds would be required to include bold and clear expressions to investors that investing in the funds carries risk. These include an explicit warning that one could lose money, one should not invest in the fund if needing to maintain a stable NAV, and that investments are not insured or guaranteed by the government. Additional statements would note that an investor should not

[3] See 28 April 2001 letter to Elizabeth M. Murphy from Kurt N. Schacht and James C. Allen re President's Working Group Report on Money Market Fund Reform (File No. 4-619).

expect financial support to the fund from the sponsor, who is under no legal obligation to provide it, and that the value of fund shares can vary. Retail and Government money market funds permitted to retain a stable NAV valuation would be required to provide a modified version of these disclosures.

Funds allowed to maintain a stable NAV under the liquidity fees/gates Alternative Two would also have to make similar disclosures to investors that they could lose money by investing in this type of fund, that the $1.00/share price is not guaranteed, and that when under "considerable stress" the fund could impose a fee upon the sale of the investor's shares or temporarily suspend the right to redeem. The fund also would have to note that investments in it are not insured or guaranteed by the government and that an investor should not expect financial support to the fund from the sponsor, who is under no legal obligation to provide it.

We strongly support providing investors with the information they need to make informed investment decisions, and presenting that information in a meaningful format. Disclosures are needed to alert investors to the potential for loss of principal and interest and that these investments are not guaranteed by the government. This would put investors on notice that money market funds are not riskless and would provide the information in a clear and succinct manner.

We have in the past called for prompt public disclosure whenever a fund's NAV falls below the current regulatory threshold of valuation. We therefore strongly support proposed disclosures aimed at requiring funds to post daily on their Web site information pertaining to their daily and weekly liquid assets, market-based per-share NAV, and instances of when sponsors have lent support. We believe that these types of disclosures are essential for empowering investors with information with which they can adjust their investment strategies in an ongoing manner. By better understanding the risks of investing in money market funds and having current and ongoing information on fund performance, investors will be on notice and thus less likely to run in instances where fund performance dips.

Diversification Requirements

Current Rule 2a-7 requires a fund to invest no more than 5% of its assets in the securities of any one issuer of a first tier security (other than government securities). Proposed amendments to the 5% issuer diversification requirements would now require funds to limit their exposure not just to a single issuer but to a group of affiliated entities.

Rule 2a-7 also requires a fund to limit its investments in securities that are subject to a demand feature or guarantee to no more than 10% of fund assets from one provider, with an exception for those subject to the 25% "basket" rule. Under that rule, a fund currently may have as much as 25% of the value of its securities subject to a guarantee or demand feature of a single institution. Proposed amendments would include ABS sponsors as guarantors, so as to limit the amount of a fund's exposure to ABS sponsors providing support (express or implicit) for the ABS.

We support these proposed changes as means to help lessen the fund's vulnerability by limiting its exposure.

Form N-CR

We support proposed new Form N-CR which would be used by money market funds to reflect the occurrence of any of the following events: default or insolvency of an issuer of one or more of the fund's portfolio securities that are more than one-half of one percent of fund assets; fund receipt of financial support; significant downward deviations for funds with $1.00/share valuation; and consideration or use of a liquidity fee or redemption gate. We believe requiring funds to file this form with the SEC, which would then be made available to the public, serves two important purposes. First, it alerts the SEC to issues the funds may be having. Second, it provides the public with current information that investors need.

We particularly endorse the proposed requirement that money market funds would have to post on their websites much of the information required in Form N-CR. While Form N-CR information is publicly available upon SEC filing, investors will more readily find and make use of this information if posted on a particular fund's website.

Conclusion

We believe that the options presented in this proposal provide thoughtful mechanisms for addressing many of the concerns relating to money market funds. While in this context we prefer Alternative One with the improvements suggested above, we hope that these changes ultimately will lead the industry and investors toward a floating NAV for all money market funds.

Should you have any questions about our positions, please do not hesitate to contact Kurt N. Schacht, CFA at kurt.schacht@cfainstitute.org or 212.756.7728; or Linda L. Rittenhouse at linda.rittenhouse@cfainstitute.org or 434.951.5333.

Sincerely,

/s/ Kurt N. Schacht

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