

MEMORANDUM

To: Money Market Fund Reform Proposal (File No. S7-03-13)

From: Kay-Mario Vobis
Senior Counsel, Division of Investment Management

Date: March 11, 2014

Re: Meeting with Representatives of Federated Investors, Inc.

On March 11, 2014, Diane Blizzard (Associate Director, Division of Investment Management (“IM”)), Eun Ah Choi (Associate Director, IM), Sarah ten Siethoff (Senior Special Counsel, IM), Richard Rodgers (Senior Special Counsel, IM), Sharon Pichler (Financial Analyst, IM), Kay-Mario Vobis (Senior Counsel, IM) and Jennifer McHugh (Senior Advisor to Chair White) met with Peter Germain (General Counsel, Federated Investors, Inc.) and Steve Keen (Counsel, Reed Smith LLC). Among other things, the parties discussed the Commission’s proposal on money market fund reform. Federated also provided the attached presentation materials on money market fund reform.

Federated

Money Market Reforms: Marginal Cost/Marginal Benefit Analysis

Presented by:

Peter Germain

General Counsel

Federated Investors, Inc.

Background

- The SEC has proposed two alternatives to “Improve the Resiliency of Money Market Funds”: Floating the NAV (FNAV) and Fees and Gates.
- Commenters have voted overwhelmingly against FNAV.
- So how do these alternatives fare in marginal cost/marginal benefit terms?

Voluntary Gating and Fees

- Preserves MMFs as a viable cash management alternative
- Cost effective (can be implemented with relatively little incremental cost)
- Stops runs regardless of cause
- Mitigates so-called first mover advantage
- Transparently demonstrates that MMFs involve a degree of risk
- Promotes competition, capital formation and market efficiency
- Furthers the goal of investor protection

Weighing the Marginal Cost of FNAV on a Stand Alone Basis or in Addition to Fees and Gates

- Survey data strongly suggests that investors will avoid FNAV products for cash investment.* This means:
 - Decreased issuers access to markets
 - Increased borrowing costs
 - Higher financing costs means less working capital resulting in a corresponding loss of jobs
- FNAV will require costly reprogramming/replacement of accounting and trading systems
- FNAV will decrease returns over time on cash for investors
- FNAV creates tax uncertainty
- FNAV may cause shift to unregulated investment alternatives

* Source: Treasury Strategies, Inc. "Money Market Fund Regulations: The Voice of the Treasurer," April, 2012

Weighing the Marginal Benefit of FNAV

- FNAV really only addresses “First Mover Advantage” which is highly theoretical and has only occurred once in 40 years. There are many other reasons why investors run, for example investors may seek the safety of treasury securities in periods of extreme market uncertainty.
- Gates stop runs, so there is no incremental benefit to adding FNAV to gates and fees.
- With enhanced disclosure and highly visible gates and fees, the marginal benefit of FNAV’s transparency is further diminished.

Increased Transparency

An important component of the SEC's proposed money market fund reforms focused on increased disclosure and enhanced transparency. These also further the goal of investor protection through:

- Improved investor knowledge and decision making
- Enhanced regulatory oversight

How Do the Proposals Stack Up?

(The analysis assumes increased disclosure and reporting is adopted as part of final rule)

| | Alternative 1 (FNAV) | Alternative 2 (Voluntary Gates and Fees) | Combined 1 & 2 |
|---------------------------------|-------------------------|---|----------------|
| Prevent Runs | ✗ | ✓ | ✓ |
| Minimizes First Mover Advantage | ✓ | ✓ | ✓ |
| Promotes Capital Formation | ✗ | ✓ | ✗ |
| Promotes Competition | ✗ | ✓ | ✗ |
| Promotes Market Efficiency | ✗ | ✓ | ✗ |
| Cost Effective | ✗ | ✓ | ✗ |
| Protects Investors | ✗ | ✓ | ✗ |

FNAV will cause a massive exit from Money Market Funds which in-turn will constrain capital formation and reduce competition and market efficiency. The burdensome costs of FNAV are well-documented. And FNAV will drive investors to less regulated alternative investments or exacerbate the "too big to fail" problem by pushing them into insured deposits.

Result of Analysis

- There is simply no credible case for FNAV at this time.
- SEC would be well justified in adopting voluntary gates and fees along with measures to increase transparency.
- The SEC could use data from enhanced reporting to monitor the effects of the reforms, reserving options like Alternative One in the unlikely event these reforms prove inadequate.
- More work by the Fed and the SEC outside of money fund reform could help further reduce risks to short-term markets in periods of market instability.

Thank You

Federated®

Federated®

Federated Investors, Inc.
Federated Investors Tower
1001 Liberty Avenue
Pittsburgh, PA 15222-3779
1-800-341-7400
FederatedInvestors.com

42712 (3/11)

Federated is a registered trademark of
Federated Investors, Inc.

2011 ©Federated Investors, Inc.