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Federated
WORLD-CLASS INVESTMENT MANAGER ®

September 8, 2009

Ms. Elizabeth M. Murphy, Secretary
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, DC 20549-1090

Re: File No. S7-11-09
Money Market Fund Reform

Dear Ms. Murphy:

This letter presents the comments of Federated Investors, Inc. and its subsidiaries ("Federated")[1] on the recent issuance by the Securities and Exchange Commission ("SEC," or "Commission") of a release proposing, and seeking comments on, proposed amendments to Rule 2a-7 under the Investment Company Act of 1940 (the "1940 Act") and related regulatory reforms.[2] As of June 30, 2009, Federated managed U.S. money market funds ("Money Funds") having total net assets of $312.8 billion, making Federated the third largest manager of Money Funds. The registration statement for Federated's Money Market Management fund first became effective on January 16, 1974, making it perhaps the longest continuously operating Money Fund to use the Amortized Cost Method.[3] Federated also received one of the initial exemptive orders permitting use of the Amortized Cost Method in 1979.

As a preliminary matter, Federated participated in the Investment Company Institute's Money Market Working Group (the "Working Group") and supported the recommendations published in the Working Group's Report (Mar. 17, 2009) (the "Report"). The Report documents

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1 Federated Investors, Inc. is one of the largest investment management firms in the United States, managing $401.8 billion in assets as of June 30, 2009. With 147 mutual funds and a variety of separately managed account options, Federated provides comprehensive investment management to more than 5,400 institutions and intermediaries including corporations, government entities, insurance companies, foundations and endowments, banks and broker/dealers.

2 The amendments were published for comment in Release No. IC-28807, Money Market Fund Reform, 74 Fed. Reg. 32688 (July 8, 2009) (the "Proposing Release"). "Proposed Rule 2a-7" refers to the rule as proposed in the Proposing Release.

3 Unless otherwise defined, this letter uses capitalized terms with the definitions given in Rule 2a-7(a) as currently in effect.

the growing significance of Money Funds to the U.S. economy over the past thirty-five years. With nearly $4 trillion in assets, an amount comparable to U.S. bank deposits, Money Funds represent approximately 35% of the mutual fund industry.[4] The Report estimated that Money Fund portfolios hold nearly a third of taxable money market instruments, including over 40% of commercial paper. Tax Exempt Funds represent an even larger share of the tax-exempt money market, providing perhaps two-thirds of the short-term financing used by states and local governments to finance their daily operations.

Federated also has reviewed a draft comment letter on this subject being prepared by the Investment Company Institute ("ICI") and as a general matter expresses its strong support for the points made therein. Federated's thinking on the proposed reforms has evolved, however, such that our current position differs from the ICI's comment letter on the following points.

- Federated does not support further restrictions on investments in Second Tier Securities.
- While continuing to strongly support the ability of Money Funds to trade their shares at a stable $1.00 NAV, Federated believes that Money Funds should be prepared to process transactions at a price other than $1.00, although an annual determination by the Money Fund's board of directors or trustees (the "Board") should not be required.
- Although redemptions in-kind should not be mandated for Money Funds, Federated believes that additional guidance from the SEC could make redemptions in-kind a more feasible alternative for dealing with a liquidity crisis within a limited range of circumstances.
- Federated does not support the expansion of Rule 17a-9.

Federated fully supports the SEC's objectives of "mak[ing] money market funds more resilient to certain short-term market risks, and [providing] greater protections for investors in a money market fund that is unable to maintain a stable net asset value per share."[5] As evidenced by these comments, Federated believes that most of the proposed reforms will further these objectives and that more can be done to accomplish them. Federated also hopes the SEC understands that prohibiting Money Funds from offering shares at a stable net asset value or price ("NAV") is antithetical to these objectives, as it would expose investors to market risks by consigning them to funds "unable to maintain a stable net asset value per share." The thirty-five year history of money market funds demonstrates persuasively that these products have been an exceptionally useful and popular investment vehicle.

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4 Investment Company Institute, Trends in Mutual Fund Investing (July 2009).

5 Proposing Release at 32688.

I. SUMMARY OF COMMENTS

A. Liquidity Requirements and Stress Testing

- Federated supports the inclusion of liquidity requirements in Proposed Rule 2a-7, but would place more emphasis on the general liquidity requirements. Board involvement should be required if a Money Fund cannot meet the general liquidity requirement.
- Federated's analysis of redemption activity in September 2008 demonstrates that the proposed higher floors for so-called "Institutional Funds" would impose an unwarranted cost on most of its institutional investors. Federated therefore continues to support the liquidity floors recommended by the Working Group
- Federated recommends including short-term, fixed rate agency securities in the definitions of Daily and Weekly Liquid Assets, and continuing to permit Money Funds to invest in illiquid securities as traditionally defined.
- Federated supports the proposed stress testing requirements, but does not think they should require a special risk assessment by the adviser.

B. Suspension of Redemptions

- Federated believes that it is important for a Board to have the option of temporarily suspending redemptions in circumstances in which Rule 2a-7 requires the Board to determine what course of action is in the interest of shareholders.
- Federated supports proposed Rule 22e-3, with some minor modifications.

C. Second Tier Securities and Maturity Limitations

- Federated believes that Money Funds, especially Tax Exempt Funds, should continue to have the ability to invest in Second Tier Securities.
- Federated opposes all of the proposed changes to ratings references in Proposed Rule 2a-7.
- Federated continues to support the Working Group's recommendation of a 75-day limit on weighted average portfolio maturity and a 120-day limit on weighted average portfolio life, with no other changes to the maturity requirements for Money Funds using the Amortized Cost Method.

D. Other Proposed Changes to Rule 2a-7 and Disclosure Requirements

- Federated opposes the reimposition of a separate creditworthiness requirement for repurchase agreements, but does not object to the limitation of the "look through" exception to Government Securities.
- Federated supports requiring a Money Fund to have the capacity to convert to a fluctuating NAV if it can no longer maintain a stable NAV, provided that there is an extended transition period.

- Federated supports the ICI's position on monthly disclosure of Money Fund portfolios, but opposes the public disclosure of Form N-MFP information.
- Federated suggests reexamining whether Form N-MFP is the appropriate means of obtaining some of the information needed to monitor Money Funds.

E. Other Rule Proposals and Requests for Comment

- Federated opposes the expansion of Rule 17a-9 as it may exacerbate the unwarranted expectations of shareholders regarding advisors support for their Money Funds.
- Federated opposes any attempt to repeal Rule 2a-7 (*i.e.*, to no longer permit Money Funds to seek to maintain a stable NAV), or weaken the NRSRO controls of Rule 2a-7.
- Federated believes that redemption in-kind may be a feasible alternative in limited circumstances, and requests additional guidance on how it could be implemented. Neither redemption in-kind nor redemption fees should be mandated for Money Funds, however.
- Federated recommends clarifying that certain assumptions should not be made in determining whether Asset Backed Securities present minimum credit risks, but the SEC should not require that these securities have Unconditional Demand Features.

II. LIQUIDITY REQUIREMENTS

Federated has always regarded meeting redemptions on a timely basis while continuing to maintain a stable NAV as a primary objective of managing a Money Fund's portfolio. This is how Federated defines "liquidity" or "liquidity risk" for Money Funds: the ability to meet redemptions in accordance with the terms of the Money Fund's prospectus at a stable $1.00 NAV. Under this definition, the "demand" for liquidity (net redemptions by shareholders) is as important as the "supply" of liquidity (the Money Fund's cash balances and capacity to generate cash through portfolio transactions and borrowings) to the formulation of a Money Fund's investment strategy.

The Money Fund's portfolio management team is responsible for assessing liquidity risks, just as they are responsible for assessment of potential interest rate changes and credit risks. As with interest rate and credit risks, assessments of liquidity risks are never certain, but can be improved by information and experience. Federated's portfolio managers recognize and prepare for seasonal patterns in liquidity demands (*e.g.*, days on which tax payments are due and quarter ends), patterns associated with certain types of investors (*e.g.*, payroll dates for corporations or coupon payments by indenture trustees) and patterns unique to particular investors (*e.g.*, amounts awaiting dispersal upon approval of a plan of reorganization or settlement). Federated also finds that direct communication between portfolio managers and investors is vital to their assessment of liquidity risks.[6]

Federated therefore supports the amendment of Rule 2a-7 to recognize the need for Money Funds to manage their liquidity risks and to place outside limits on the liquidity risks Money Funds may take. Federated believes that the SEC should apply the same pattern of regulation to liquidity risks as it has for interest rate and credit risks—namely a general requirement to manage the liquidity risks in a manner consistent with maintaining a stable NAV, *see*, *e.g.*, Rule 2a-7(c)(2) ("[t]he money market fund shall maintain a dollar-weighted average portfolio maturity appropriate to its objective of maintaining a stable net asset value per share"), subject to clear objective risk limitations, *e.g.*, the 90-day limitation on average weighted portfolio maturity and 397-day limit on the maturity of individual securities. In addition, a failure to comply with the general liquidity requirement due to changes in market conditions should be addressed by requiring the Board to assess what action, if any, is required to respond to the change in conditions, rather than as a violation of Rule 2a-7. *See*, *e.g.*, Rule 2a-7(c)(7)(ii)(B) (requiring "the board of directors [to] promptly consider what action, if any, should be initiated" if the Money Fund's shadow price per share ("shadow NAV") deviates by more than one-half of one percent from its stable NAV due to, among other factors, changes in interest rates).

Federated does not support any attempt to differentiate between so-called "retail" and "institutional" Money Funds for purposes of the new liquidity requirements. In Federated's experience, the liquidity risks posed by retail and institutional investors are far more heterogeneous than the SEC supposes. Federated expects that the SEC could confirm this by examining the data underlying the aggregate cash flow information cited in the Proposing Release, which would show many institutional funds that did not have significant redemptions and some retail funds that had very sizable redemptions. Federated therefore recommends using the proposed general liquidity requirement to address the different liquidity risks associated with different types of Money Funds, rather than setting unduly high liquidity floors for many of the "Institutional Funds" defined in Proposed Rule 2a-7(a)(17).

A. The Commission Should Adopt the General Liquidity Requirement and Make It a Focus of Future Examinations

Federated agrees with the general liquidity requirement contained in Proposed Rule 2a-7(c)(5)(ii). We also agree with the approach of stating the general liquidity requirement as a rule, rather than requiring a Board to make determinations or adopt procedures regarding

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[6] In Federated's experience, it is difficult for anyone not engaged in the day-to-day management of a Money Fund to interpret cash flow activity and detect potential liquidity risks. Federated would therefore oppose any requirement that a Board monitor cash flows for "hot money" or take direct responsibility for assessing liquidity risks. *See*, Proposing Release at 32707.

liquidity risks.[7] We do, however, have two suggestions regarding this requirement. First, this requirement should be moved to the body of the paragraph so as to clarify that this is the primary requirement for managing liquidity risks, while the Daily and Weekly Liquid Asset requirements (Proposed Rule 2a-7(c)(5)(iii)-(iv)) are limitations.

Second, and more importantly, the general liquidity requirement should permit consideration of cash resources in addition to Daily and Weekly Liquid Assets. Many Money Funds have overdraft arrangements, lines of credit and interfund borrowing arrangements which provide ready sources of cash for meeting redemptions. The manager of a Money Fund needs to factor these alternative sources of cash into any assessment of liquidity risks. Therefore, we recommend changing the wording of the requirement from "shall hold Daily Liquid Assets and Weekly Liquid Assets sufficient to meet reasonably foreseeable shareholder redemptions" to "shall have available sources of cash (including Daily Liquid Assets and Weekly Liquid Assets) sufficient to meet reasonably foreseeable shareholder redemptions."

As with the general requirements for weighted average portfolio maturities and minimal credit risk, the efficacy of the new general liquidity requirement will depend largely on the SEC's examination staff. Periodic examinations are the best means for the SEC to assess the extent of the liquidity risks faced by different Money Fund managers and to assure that they manage these risks in a manner consistent with maintaining a stable NAV. We expect that the examination staff learned a good deal about liquidity management during their sweep examinations of Money Funds at the end of 2007 and early 2008, and the staff of the Division of Investment Management (the "Division") has learned more during their research on the proposed reforms. Federated recommends putting that knowledge to good use by developing examination criteria for the new requirement.

In Federated's experience, effective liquidity management requires some means for the portfolio management team to research cash flow activity, just as they must research market and financial conditions in order to manage interest rate and credit risks. Therefore, the examination staff should, at a minimum, expect managers to have some process whereby portfolio managers can request information regarding the sources of significant cash inflows and outflows, and then obtain more detailed information from the investors responsible for such cash flows. Proper assessment of liquidity risks requires understanding the motives underlying cash flow activity, in addition to reports of the activity itself. Procedures that rely entirely on passive reporting of cash flow activity to manage liquidity risks might warrant careful scrutiny during examinations.

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7 Federated also would recommend modernizing Rule 2a-7 by eliminating references to Board determinations and procedures for most of the rule's day-to-day requirements (*e.g.* minimal credit risk determinations or shadow pricing). As noted in the Proposing Release, the adoption of Rule 38a-1 eliminates the need to include separate procedural requirements in other regulations promulgated under the 1940 Act. Stripping most of the procedural provisions from Rule 2a-7 would not only shorten and clarify the rule, but it also would eliminate a potential source of confusion for directors regarding the responsibility of the fund's chief compliance officer for the procedures specified in Rule 2a-7 rather than Rule 38a-1. Using this approach, Rule 2a-7 would only retain references to the Board with respect to their non-delegable responsibilities, leaving compliance with the other requirements to Rule 38a-1.

B. The SEC Should Adopt Uniform Minimal Requirements for Daily and Weekly Liquidity

Federated objects strongly to any requirement that Boards classify their Money Funds as either "Institutional" or "Retail." Forcing a false dichotomy on Money Funds will require some Money Funds to maintain unnecessarily high levels of liquidity and could mislead investors as to the relative liquidity risks of competing Money Funds. Federated believes that the general liquidity requirement, if properly administered, will prove to be a far more effective means of assuring that Money Funds with higher liquidity risks maintain high levels of liquidity.

1. <u>Boards Cannot Differentiate Between "Institutional" and "Retail Funds" Under the Proposed Definitions</u>

Under Proposed Rule 2a7(a)(17), a Board would have to determine that a Money Fund is "Institutional" if either: (a) the Money Fund "is intended to be offered primarily to institutional investors," or (b) the Money Fund has the characteristics of a Money Fund intended to be offered to institutional investors. The second part of the definition presupposes that Money Funds offered to institutional investors will have common "characteristics" that distinguish them from "Retail Funds." Three particular characteristics are identified:

- Nature of the record owners;
- Minimal initial investment requirements; and
- Historical and expected cash flows from share activity.

The principal problem with the proposed definition is that none of these characteristics reliably separate "institutional" from "retail" investors, as generally understood, because "Institutional Funds" do not have unique characteristics. For example, many retail and institutional investors invest through their broker, both on a cash sweep and directed basis. So both "Institutional" and "Retail" Funds will have large omnibus accounts in which a registered broker-dealer is named as the record owner. Moreover, if the omnibus accounts satisfy the minimal investment limitations, the broker may use this as a means of giving its retail clients access to what might otherwise be regarded as "Institutional Funds."[8] Thus, the first two characteristics cannot be relied upon to differentiate "Institutional" from "Retail Funds."

The third characteristic, cash flows from share activity, is the nub of the issue. The SEC is not proposing higher minimum liquidity requirements for Institutional Funds as a means of regulating their record holders or minimum investment requirements. The proposal is simply trying to use the "Institutional Fund" label as a proxy for Money Funds with higher liquidity

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[8] It might be suggested that a Money Fund could "look through" the omnibus accounts to see if it was composed of institutional or retail investors. Money Funds (which are excepted from Rule 22c-2) currently have no ability to obtain this data from omnibus accountholders. Even if they did, they have no means of preventing a shift in the mix of investors in an omnibus account, so the accounts would have to be monitored on a continual basis. Federated believes that the cost of this type of monitoring would be prohibitive, and would not provide any real benefits to Money Fund shareholders.

risks due to potential large-scale shareholder redemptions. The fact is, however, that *some* institutional investors pose lower liquidity risks than *some* retail investors. Given this fact, *all* Money Funds are potentially "Institutional Funds" under the second part of the proposed definition, because they could share the historical and expected cash flow activity of a Money Fund intended to be sold to institutional investors with low levels of cash flow activity (such as a bank proprietary Money Fund sold to its trust and corporate accounts). Put another way, if a Board finds that any Money Fund "intended to be offered primarily to institutional investors" has the characteristics of Retail Funds, the second part of the proposed definition *requires* the Board to treat the Retail Funds as Institutional Funds, rather than treating the exceptional Institutional Fund as a Retail Fund. This will result in many (if not most) Money Funds having unduly high minimum levels of liquidity.

Federated is not aware of any characteristic of a Money Fund that can serve as a proxy for liquidity risk. That is why we support the general liquidity requirement, because it requires Money Funds to manage liquidity risks directly, taking into account all of the relevant facts regarding their investor base and developing market conditions. The Daily and Weekly Liquid Asset requirements are, therefore, rightly viewed as a "floor," with the Money Fund's adviser responsible for assessing the level to be maintained above that floor.

We therefore do not believe that Boards will be able to make useful distinctions between "Institutional" and "Retail" Funds, particularly using the proposed vague and potentially all encompassing definition of "Institutional Fund." Further, given that there is no sanction for imposing higher minimum Daily and Weekly Liquid Asset requirements on a Money Fund, we expect that conservative Boards will limit their risks by sweeping all Money Funds into the "Institutional" category. Although Federated continues to believe that the Daily and Weekly Liquid Asset floors recommended by the Working Group (5% in Daily Liquid Assets for taxable Money Funds and 20% in Weekly Liquid Assets for all Money Funds) are appropriate, if other floors are chosen, it would be better to impose the higher floors directly on Money Funds, rather than reaching the same end circuitously through a new Board requirement.

2. Federated's Experience Demonstrates that Retail and Institutional Investors May Pose Similar Liquidity Risks

Federated is concerned that the SEC has placed too much emphasis on the superficial labels of "institutional" and "retail" used to report Money Fund statistics. Federated suspects that, regardless of how they are labeled, most Money Funds have a mixture of institutional and retail investors. Therefore, to properly assess whether institutional investors pose greater liquidity risks than retail investors, the SEC should look through the industry statistics to the actual trading records of Money Fund shareholders.

Federated has performed this analysis[9] for its Money Funds during September 2008, which includes the aftermath of The Reserve Primary Fund's (the "Primary Fund") announcement that it had broken a dollar. We have attached as Exhibit A a graph showing the relative percentage of retail and institutional redemptions during the month. The results demonstrate that the redemption activity of retail investors in Federated's Money Funds was *more* volatile than the redemption activity of institutional investors. Specifically:

- Retail investors redeemed the largest percentage of shares on any single day during the month. (7.9% on September 15).
- The largest percentage of shares redeemed by institutional investors (5.8%) occurred on September 17, the day after the Primary Fund "broke a dollar." However, retail investors redeemed almost the same percentage of their shares (5.6%) on this date.
- Redemptions by institutional omnibus accounts, which comprise over 80% of Federated's institutional Money Fund assets, were less volatile than the overall level of either retail or institutional redemptions. These omnibus accounts redeemed only 3.8% of their shares on September 17.
- Although the average daily redemptions by retail and institutional investors were the same (2.8%), retail daily redemptions were more volatile, with a standard deviation of 1.9% as compared to 1.4% for institutional investors. Average daily redemptions by institutional omnibus accounts were only 2.1%, however, and were more regular than retail daily redemptions, with a standard deviation of just 1.0%.

This data proves that, for at least one complex, institutional investors are *not* more prone to "run" from a Money Fund than retail investors. Retail investors may in fact respond more strongly to certain market events (*e.g.*, the Lehman Brothers bankruptcy, coupled with the crisis at AIG, the acquisition of Merrill Lynch by Bank of America and a nearly 200 point drop in the Dow Jones Index) than most institutional investors, even if these events are unrelated to the Money Fund (none of these events affected any Federated Money Fund). In addition, one implication of the relatively stable redemption rate of omnibus institutional accounts is that the larger swings in institutional redemptions were driven entirely by the remaining 20% of institutional investors. This suggests that the SEC's concern that "retail investors [might] bear the cost of maintaining liquidity for institutional investors"[10] is unfounded. In Federated's case, it is

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9 Federated's transfer agent assigns "social codes" to accounts to identify the type of investor. Federated analyzed the purchase and redemption activity of each social code, treating social codes associated with individual investors as "retail," and social codes associated with other types of investors as "institutional." The transfer agent uses different social codes for omnibus accounts maintained primarily for individual investors (including broker omnibus accounts) and those maintained primarily for institutional investors. The analysis excluded social codes associated with accounts maintained by financial intermediaries who do not disclose sufficient information to classify the underlying investor. The excluded social codes represent approximately 20% of the assets held in Federated's Money Funds, and illustrate how difficult it would be for a Board to obtain the data necessary to classify a Money Fund as an "Institutional" or a "Retail Fund."

10 Proposing Release at 32705.

the 80% of stable *institutional* assets that allowed Federated's Money Funds to provide ready liquidity to retail investors and to the remaining institutional investors. This is particularly true of Federated Money Funds that offer both institutional and retail classes of shares.

This data also illustrates the relative importance of the general liquidity requirement as compared to the Daily and Weekly Liquid Asset floors. Redemptions on September 17 exceeded the Working Group's proposed 5% Daily Liquid Asset floor, and redemptions for the week of September 15 exceeded the 20% Weekly Liquid Asset floor. Yet Federated was able to pay redemptions during the period, and even had sufficient liquidity to assume the assets and redemption obligations of the Putnam Prime Money Market Fund during the following week. The Federated's portfolio managers' decision to build and maintain additional liquidity in anticipation of volatile market conditions contributed greatly to this result, demonstrating that, as with interest rate and credit risks, quantitative limits are no substitute for professional judgment.

3. Tax Exempt Funds Could Not Comply with a Daily Liquid Asset Floor

Finally, we strongly caution the SEC against imposing a Daily Liquid Asset requirement on Tax Exempt Funds. Tax Exempt Funds cannot engage in repurchase agreements and the supply of tax-exempt securities with daily Demand Features is extremely limited.[11] In some states, there is only one provider of Daily Demand Features. Therefore, imposition of a Daily Liquid Asset requirement on Tax Exempt Funds may force many funds to be uninvested for extended periods, and will create a substantial barrier to entry to new Tax Exempt Funds.

C. Daily and Weekly Liquid Assets Should Include All Fixed-Rate Government Securities with Remaining Maturities of 95 Days or Less

Federated continues to support the Working Group's recommended definition of Daily and Weekly Liquid Assets. In fact, after reviewing the data, Federated now believes that Daily, as well as Weekly, Liquid Assets should include fixed-rate Government Securities with remaining maturities of 95 days or less. Our analysis of the period from September 1 to December 31, 2008,[12] one of the most volatile on record, indicates that three-month Treasury Bills and three-month Government agency discount notes experienced about the same degree of volatility. The average daily implied (absolute) percentage change in price for 3-month T-Bills during the period was approximately 0.026%, as compared to 0.025% for 3-month agency notes. The largest one day percentage increase in price for 3-month T-Bills was 0.16%, as compared to 0.18% for agency discount notes. The largest decrease in price was 0.21% for 3-month T-Bills,

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11 The risks to a provider of a daily Demand Feature is significantly greater than the risks to a provider of a weekly Demand Feature, insofar as the daily Demand Feature leaves only a few hours in which to locate a purchaser after the Demand Feature is exercised, rather than several days as is the case for a weekly Demand Feature. Consequently, increased demand for daily Demand Features may not generate a corresponding increase in supply.

12 Bloomberg: US Generic 1 Month T-Bill GB1M <Index>, US Generic 3 Month T-Bill GB3 <Govt>, Agency Discount Note 30 Day Yield AGDN030Y <Index>, and Agency Discount Note 90 Day Yield AGDN090Y <Index>.

as compared to 0.10% for 3-month agency discount notes. While the use of generic market indices does not capture some of the nuances of actual trading, the conclusion that this analysis suggests – which also would encompass agency securities of shorter maturities - is consistent with Federated's own observations of and experiences in the short-term Treasury and agency markets during this time.

Trading volumes for both T-Bills and agency discount notes of all maturities rose during the period. The trading volume of T-Bills during the period doubled from the average volume for the same four month period over the last five years; the trading volume of agency discount notes (which is typically higher than the volume of T-Bills during normal market conditions) also increased, but not as significantly.[13]

The tables below capture the same price and volume data for various time periods over a broader span of time.

Daily (Absolute) Implied Percentage Price Changes for Three-Month Treasury and Agency Securities		
Source: Bloomberg	**Treasury Bills**	**Agency Discount Notes**
Average from Jan '00 to Jul '09	0.0078%	0.0043%
Average from Jan '00 to Sep '08	0.0074%	0.0035%
Average from Sep '08 to Dec '08	0.0262%	0.0253%
Average from Jan '09 to Jul '09	0.0035%	0.0033%

Primary Dealer Daily Average Trading Volume ($ Billions)		
Source: Federal Reserve/Bloomberg	**Treasury Bills**	**Agency Discount Notes**
Average from Jan '00 to Jul '09	$48.24	$61.05
Average from Jan '00 to Sep '08	$44.08	$60.42
Average from Sep '08 to Dec '08	$100.95	$74.13
Average from Jan '09 to Jul '09	$79.22	$62.68

By any measure, the markets for short-term,[14] fixed-rate agency securities is at least as stable and deep as the markets for comparable Treasury obligations. Our analysis includes the date on which Fannie Mae and Freddie Mac were placed in conservatorship, an event that prompted less volatility in their discount notes than the general market crisis later in September.

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13 Weekly trading volumes for T-Bills during the period from September through December averaged $49 billion for the years from 2003 to 2007, and increased to $101 billion in 2008. Weekly trading volumes for agency discount notes during the period from September through December averaged $62 billion for the years from 2003 to 2007, and increased to $74 billion in 2008. Bloomberg: Primary Dealer Daily Avg Trading Volume - Treasury Bills PDPLBILL Index and Discount Notes PDPLDISC Index.

14 Although the secondary market for agency securities with maturities longer than 95 days is also robust, we do not propose including those securities in the definition of Daily and Weekly Liquid Assets in the event that Government agencies funding needs in that area change in the future.

We believe this data demonstrates that agency notes provide a source of liquidity as least as reliable as comparable direct U.S. government obligations, and therefore warrant equal treatment as Daily and Weekly Liquid Assets.

D. The SEC Should Require Money Funds that Fail to Meet the General Liquidity Requirement to Sell Securities Unless the Board of Directors Determines that Sales Would Not Be in the Money Fund's Interest

The Proposing Release does not discuss the consequences of a Money Fund failing to meet the new liquidity requirements. This leaves open the possibility that the SEC might view a failure to satisfy the liquidity requirements as a violation of Rule 2a-7. This may be appropriate for acquisition requirements, such as the proposed Daily and Weekly Liquid Assets requirements, because the Money Fund can test for compliance at the time of each acquisition. It is not appropriate, however, for the general liquidity requirement because a Money Fund may find itself without sufficient liquidity to meet expected redemptions due to circumstances beyond the Money Fund's control.

In similar circumstances, such as when a security no longer qualifies as an Eligible Security or presents more than minimal credit risks, Rule 2a-7(c)(6)(ii) requires the Money Fund to "dispose of such security as soon as practicable consistent with achieving an orderly disposition of the security." The Money Fund can avoid disposition of the security only if its Board finds "that disposal of the portfolio security would not be in the best interests of the money market fund." Federated suggests that the SEC take the same approach with respect to the general liquidity requirement, *i.e.*, require dispositions of securities other than Daily and Weekly Liquid Assets to raise cash to the level needed to meet reasonably expected redemptions, unless the Board determines that such dispositions are not in the Money Fund's best interest. The only difference from the current rule would be that, rather than requiring disposition of a particular security, this provision would require disposition of unspecified portfolio securities in an amount sufficient to restore needed liquidity.

Federated believes that this approach would be preferable to requiring Money Funds to comply continuously with the Daily and Weekly Liquid Asset floors. In many cases, a Money Fund may utilize Daily or Weekly Liquid Assets to meet anticipated redemptions, knowing that cash flows from maturing securities and sales of new shares will allow it to quickly restore Daily or Weekly Liquid Assets to required levels without disposing of other securities. Requiring Money Funds to constantly dispose of securities in order to stay above the Daily or Weekly Liquid Assets floors also would contribute to market volatility, as any redemption could potentially lead to the mandatory sale of a portfolio security. If we have learned anything over the past two tumultuous years, it is that forced sales of securities are not good for financial markets.

Indeed, Federated anticipates that requiring Money Funds to constantly maintain a minimum percentage of Daily and Weekly Liquid Assets would cause Money Funds to maintain Daily and Weekly Liquid Assets needed for anticipated redemptions *in addition* to the minimum percentage to avoid inadvertently violating the requirement. Federated does not see any benefit to investors in effectively requiring Money Funds to maintain liquidity well in excess of reasonably anticipated redemptions. We believe that an acquisition rule is more appropriate for these minimum requirements, as it would assure that Money Funds use cash flows to restore minimum levels of Daily and Weekly Liquid Assets before making longer-term investments.[15]

Federated therefore recommends that the SEC require Money Funds to continuously comply with the general liquidity requirement rather than the Daily and Weekly Liquid Assets requirements. If redemptions exceed reasonably anticipated amounts, then the Money Fund should be required to dispose of securities (other than Daily and Weekly Liquid Assets) in order to build its available cash in accordance with the general liquidity requirement. If market conditions may make the disposition of securities contrary to the Money Fund's interest, then the Money Fund's Board should be informed of the impending liquidity problem and determine what action, if any, to take in response. This approach would have required the managers of the Primary Fund to inform the Board when the fund's custodian stopped providing overdrafts to fund redemptions. This approach also would avoid placing the Money Fund's adviser in a Catch-22 if the Money Fund needs to sell assets to avoid violating the general liquidity requirement, but cannot sell the securities without risking its stable NAV.

E. The SEC Should Not Prohibit Money Funds from Making Illiquid Investments

Federated believes that the proposed reforms go too far in restricting "illiquid" securities, both in terms of the definition of a "liquid" security and in prohibiting their acquisition by Money Funds. Federated concedes that it may be appropriate for the SEC to further limit Money Fund holdings of truly illiquid securities. The SEC should realize, however, that some "basket" for illiquid securities is necessary to foster continued innovation in the money markets.

1. <u>The SEC Should Retain the Current Definition of a "Liquid Security"</u>

Proposed Rule 2a-7 would change the definition of a "liquid security" from "a security that can 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,"[16] to "a security that can be sold or disposed of in the ordinary course of business within seven calendar days at

[15] This assumes that wording of the Weekly Liquidity Requirement is conformed to the Daily Liquidity Requirements, so that acquisitions of Weekly Liquid Assets are permitted until the requirement is satisfied.

[16] This is the definition proposed by the SEC last year, in a release purporting to codify existing liquidity requirements for money market funds. Release No. IC–28327, References to Ratings of Nationally Recognized Statistical Rating Organizations, 73 Fed. Reg. 40124, 40126 (July 11, 2008).

approximately *its amortized cost*."[17] The change in definition would reverse an interpretation of "liquid" as old as Rule 2a-7 itself. The release originally adopting Rule 2a-7 had a section on the importance of liquidity to Money Funds. In the course of this discussion, the SEC stated that: "Where the fund is using amortized cost valuation, such an instrument need not be regarded as an illiquid security if, when the fund monitors the deviation, it uses a market value for such security, which includes the effect of the penalty charge."[18] Any other interpretation of "illiquid securities" would have subjected Money Funds using the Amortized Cost Method to a higher standard of liquidity than Money Funds using the Penny Rounding Method (which carry their securities at market value), even though both types of Money Funds have exactly the same liquidity commitments to their shareholders.

The proposed definition also is inconsistent with other important elements of Rule 2a-7. The shadow pricing requirement,[19] for example, presupposes that Money Funds will hold securities whose market values deviate from their amortized cost. The definition of "Variable Rate Security" also presumes that, prior to the interest rate adjustment, the security's market value will not approximate its amortized cost. These requirements are designed, in part, to limit the potential loss that might be incurred upon disposition of these securities. The proposed definition of "liquid security," however, appears designed to eliminate the risk of loss altogether, which is simply not possible.

2. <u>The SEC Should Continue to Permit Money Funds to Purchase a Limited Amount of Illiquid Securities</u>

Two recent no action letters, Citigroup Global Markets, Inc. (pub. avail. May 28, 2009) and Straight-A Funding LLC (pub. avail. July 28, 2009), provide the best argument for why Money Funds should retain some ability to invest in illiquid securities. Both no-action letters deal with structured financial products designed for Tax Exempt Funds (in the case of the Citigroup no-action letter) and government Money Funds (in the case of the Straight-A Funding no-action letter). The products have maturities for purposes of Rule 2a-7 in excess of 90-days and neither product has a Demand Feature that permits the securities to be tendered for purchase upon seven days' notice. The Money Funds that acquired these products initially did not have any basis for concluding that the new products were liquid, and the underwriters could not provide any assurance that a secondary market would develop. If Money Funds were barred from investing in illiquid securities, then neither of these products would have had a chance to establish itself in the market.

Many innovative money market products start out by filling a portion of the Money Funds' illiquid security baskets. Federated therefore believes it is critical for Money Funds to

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17 Proposed Rule 2a-7(a)(18) [added emphasis].

18 Release No. IC-13380, Valuation of Debt Instruments and Computation of Current Price Per Share by Certain Open-End Investment Companies (Money Market Funds), 48 Fed. Reg. 32555, 32561 n. 37 (July 18, 1983).

19 Rule 2a-7(c)(7)(ii).

maintain some ability to acquire illiquid securities in order to foster new products until they are accepted in the wider market. Given the current size of Money Funds, where 1% of any type of Money Funds represents several billion dollars, the SEC might reasonably conclude that the Money Funds can support innovation with a limit below 10% for illiquid securities. Federated would recommend that the SEC not reduce the limit on illiquid securities below 5%, however. Below this level, new products could not contribute meaningfully to a Money Fund's yield without paying prohibitively high returns.

III. SUSPENSION OF REDEMPTIONS

As critical as the objective of liquidity is for a Money Fund, there are times when it must give way to the objective of fairness to shareholders. Fairness has always been an overriding objective of Rule 2a-7, which requires the Board of an Amortized Cost Money Fund to "take such action as it deems appropriate to eliminate or reduce to the extent reasonably practicable [material] dilution or *unfair* results."[20] The circumstances that led the Primary Fund to break a dollar and its aftermath have shown, however, that directors do not have all of the tools needed to reduce the unfair results that might arise from a default or other significant adverse event. In particular, the Board does not have the legal authority to suspend redemptions in situations where continued redemptions might advantage one group of shareholders at the expense of another. A timeout—even for a few days—could have allowed the Primary Fund to avoid the substantial disparity in treatment that resulted from the waive of redemptions prompted by the Lehman Brothers bankruptcy, which the Primary Fund was forced to honor until it literally ran out of cash.

Theoretically, an immediate and seamless shift from a stable to a fluctuating NAV (*i.e.*, "breaking a dollar") should prevent redemptions from producing unfair results once a Money Fund suffers a material and irreversible impairment to its portfolio. So long as the portfolio is accurately valued and the fluctuating NAV is calculated to the nearest one-tenth percent,[21] redemptions at the calculated fluctuating NAV should not produce dilution to a greater extent than other types of investment companies. The circumstances leading up to a Money Fund breaking a dollar, however, are likely to impede this theoretical outcome. For example, if the shift to a fluctuating NAV is prompted by defaults or other adverse events, it may be difficult to obtain valuations for the securities affected. Moreover, if the announcement of the Money Fund's breaking of a dollar produces wide spread market disruptions, valuation of the rest of the portfolio may become difficult. Finally, the decision to break a dollar is not to be made lightly, and most Boards will have spent significant time exhausting other possible solutions before switching to a fluctuating NAV, leaving little time to effectuate the change.

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[20] Rule 2a-7(c)(7)(ii)(C) [added emphasis].

[21] As required by Accounting Series Release No. 219 (May 31, 1977) (codified in the Codification of Financial Reporting Policies §404.5). ASR 219 generally permits investment companies to use amortized cost to fair value securities with remaining maturities of 60-days or less, so a Money Fund that converts to a fluctuating NAV would not have to obtain valuations for its entire portfolio.

A. The SEC Should Permit the Board of Directors of a Money Fund to Suspend Redemptions Temporarily While Making Determinations Mandated by Rule 2a-7

Section 22(e) of the Act provides, in pertinent part, that:

> No registered investment company shall suspend the right of redemption, or postpone the date of payment or satisfaction upon redemption of any redeemable security in accordance with its terms for more than seven days after the tender of such security to the company or its agent designated for that purpose for redemption, except—
>
> …
>
> (2) for any period during which an emergency exists as a result of which (A) disposal by the company of securities owned by it is not reasonably practicable or (B) it is not reasonably practicable for such company fairly to determine the value of its net assets;
>
> ….
>
> The Commission shall by rules and regulations determine the conditions under which … (ii) an emergency shall be deemed to exist within the meaning of this subsection.

Rule 2a-7 currently requires a Money Fund to dispose of portfolio security that (i) defaults (other than an immaterial default unrelated to the financial condition of the issuer), (ii) ceases to be an Eligible Security, (iii) has been determined to no longer present minimal credit risks or (iv) is subject to an Event of Insolvency, unless the Board finds "that disposal of the portfolio security would not be in the best interests of the fund (which determination may take into account, among other factors, market conditions that could affect the orderly disposition of the portfolio security) …."[22] As explained above, Federated recommends including another circumstance in which a Money Fund must dispose of portfolio securities—when the Money Fund determines that it cannot meet the general liquidity requirement. Federated also recommends giving the Board the authority to find that disposal of portfolio securities would not be in the best interest of the Money Fund in these circumstances.

If the Board makes a finding that it is not in the interest of the Money Fund to dispose of securities in such circumstances, and the Board has not found some other means (such as a Rule 17a-9 transaction or credit or liquidity support provided by the Money Fund's sponsor) to remedy the underlying problem, then clearly "an emergency exists as a result of which … disposal [of certain portfolio securities] is not reasonably practicable" for the affected Money Fund. It therefore seems clear that the SEC has authority under Section 22(e) to adopt a regulation defining such circumstances as an "emergency" in which the Board would be permitted to suspend redemptions for a limited period. Federated believes that this analysis also applies to a situation in which a Money Fund's shadow NAV deviates from its stable NAV by

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[22] Rule 2a-7(c)(6)(ii).

more than one-half of one percent and the Board cannot implement whatever action it determines is appropriate before the redemptions are required to be processed under Rule 22c-1. In this circumstance, however, the nature of the emergency is the inability to fairly determine the NAV at which such redemptions should be processed.

Federated does not take lightly the consequences of a Money Fund suspending redemptions under these circumstances. The suspension of redemptions by the Primary Fund and the Putnam Prime Money Market Fund in September 2008 contributed to the wave of redemptions from prime Money Funds during that period. The transfer of the Putnam Prime Money Market Fund's shareholders and assets to a Federated Money Fund demonstrates, however, how even a few days grace can allow a Board to resolve problems in a manner that serves the interest of their shareholders and reassures the general market as to the continued stability of Money Funds. It is simply too much to expect that every Board will be able to resolve every problem that threatens a Money Fund's stable NAV within the course of a single day.[23]

For example, Federated has determined that it would take intermediaries several days to convert a Money Fund from a stable NAV to a fluctuating NAV on their systems, or to adjust their records for a reverse split of Money Fund shares. The intermediaries would not require this time to reprogram or redesign their systems, but simply to implement changes for accounting, tax and reporting purposes and verify that the changes had been implemented appropriately. Federated believes that implementation of redemptions in-kind or to third-party credit support could require similar lead times.

A short break in redemptions also could allow a Money Fund to respond to erroneous news stories or false rumors. For example, in August 2007, the press reported that a "money market fund" had stopped honoring redemptions.[24] This was actually a commodities pool, not a Money Fund. Fortunately, the reports occurred early in the day and the corrections were made quickly. If it had occurred at the end of the day, however, a one-day suspension of redemptions might have helped to avoid redemptions based on a false report.

Although it is impossible to predict how many days will be required in every circumstance, Federated believes that the Working Group's recommendation of up to five Business Days strikes the right balance between the Board's need for time in which to evaluate and implement solutions and the shareholders' interest in certainty regarding their ability to redeem. Federated also believes that, as part of the determination to suspend redemptions, the

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[23] Rule 22c-1(b)(1) requires every mutual fund to compute its "current net asset value … no less frequently than once daily, Monday through Friday …." This effectively requires the Board to establish at least one time each day as of which the NAV is computed, and therefore make any findings and determinations regarding maintenance of a stable NAV before this time.

[24] Report at 48 ("On August 14, 2007, an unregistered commodity cash pool managed by Sentinel Management Group, Inc., erroneously described by CNBC as a money market fund, halted redemptions and failed within a week.")

Board should specify when redemption orders will be deemed to be received, so as to permit the processing of checks and other orders submitted before the date on which redemptions were suspended. Finally, Federated would require that any Board authorizing the suspension of redemptions also suspend sales of the Money Fund's shares.

Federated expects that granting Boards this authority may increase investor concerns regarding the reliability of Money Funds as cash investments. More sophisticated investors probably already appreciate that redemptions may be suspended in fact, if not by law, whenever a Money Fund runs out of available cash. In any event, Federated would recommend that, as with the suspension of redemption payments for up to seven days, the SEC should permit Money Funds to reserve or disclaim the right to suspend redemptions in their registration statement. This would give Money Funds essentially two options: (i) reserve the right to suspend redemptions and disclose the risk that they may be suspended, or (ii) disclaim the right to suspend redemptions and disclose the risk the Board may not be able to prevent dilution resulting from redemptions other than by breaking a dollar.

If the Board determines to temporarily suspend redemptions, the Money Fund should promptly sticker its prospectus and post the sticker on its website. It also will be important to immediately inform intermediaries of the suspension, particularly those that use the Money Fund as a cash sweep option. Federated does not believe that it will be necessary to address this in the rule, however, as intermediaries will amend their contracts in response to any rule permitting suspension of redemptions.

B. Federated Supports the SEC Proposal to Permit the Suspension of Redemptions during the Liquidation of a Money Fund

The protracted process of winding up the Primary Fund demonstrates the importance of allowing a Board to take prompt action in connection with the liquidation of a Money Fund. Although the SEC granted an order permitting the Primary Fund to suspend redemptions, it took several days for the order to be promulgated and required the SEC to grant relief retroactively. The time spent by the Primary Fund's attorneys drafting and amending the application for the order, and spent by the Division reviewing and commenting on the application and publishing the notice and order, could have been spent on more vital issues.

Federated cannot think of a sound policy reason for allowing a liquidating Money Fund to continue to honor redemption requests in cash. If the problem is isolated to the liquidating Money Fund, so that most portfolio securities can be disposed of in a liquid market, then all shareholders should benefit from those dispositions, not just redeeming shareholders. If the problem is not isolated, because markets have become generally illiquid, or the liquidating

Money Fund holds a distressed security, then the value of the shares for redemption is probably uncertain, and the remaining shareholders should not bear the risk of this uncertainty.[25] As noted at the outset of this section, under these circumstances, fairness should take precedence over liquidity.

Federated is uncertain about one provision of proposed Rule 22e-3: the requirement that the "fund's current price per share calculated pursuant to § 270.2a-7(c) is less than the fund's stable net asset value or price per share." Paragraph (c) permits a Money Fund to compute its current share price using either the Amortized Cost or Penny Rounding Method. So long as these methods are employed, a Money Fund's current price per share will not deviate from its stable NAV. Only realized losses could force the NAV (determined using the Amortized Cost Method) to 99¢.

We doubt that the SEC intended to require a Board to realize losses as a condition to suspending redemptions during liquidation.[26] This would defeat one of the purposes of liquidation—avoiding the disposition of portfolio securities that would not be in the interest of the Money Fund's shareholders. Perhaps the condition is intended to make certain that the liquidating Money Fund has "broken a dollar" before suspending redemptions. We fail to see the utility of such a condition, however. If a Board knows that honoring redemptions eventually will lead to a Money Fund breaking a dollar, and there is no better alternative to liquidating the Money Fund, then this is precisely the situation in which the Board should suspend redemptions. Federated therefore recommends omitting the first condition for Rule 22e-3(a), particularly if the SEC determines not to allow Boards to temporarily suspend redemptions.

The Proposing Release suggests that, if temporary suspensions are permitted, a Money Fund would not be able to do so more often than once in any five-year period. Federated doubts that a Money Fund that suspends redemptions once will be able to do so a second time without liquidating. In any event, Federated does not believe that the temporary suspension of redemptions should prevent a Money Fund from suspending redemptions during the course of its liquidation. Any liquidation may require a suspension of redemptions to protect shareholder interests, regardless of whether the Money Fund had temporarily suspended redemptions at some earlier point.

C. Responses to Requests for Comments Regarding Suspension of Redemptions

The Proposing Release included several requests for comments on particular issues relating to suspension of redemptions. Federated would like address a few of these requests.

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25 If markets are liquid and valuations readily available, Federated expects that a Board would be more likely to simply switch to a fluctuating NAV than to adopt a plan of liquidation.

26 The only explanation of the conditions of Rule 22e-3 provided in the Proposing Release is that they "are intended to ensure that any suspension of redemptions will be consistent with the underlying policies of section 22(e)."

1. Should the exemption be available to other types of open-end investment companies? Should there be a limit on the suspension period so that shareholder assets are not "locked up" for an unduly lengthy period?

Money Funds are the only type of mutual fund with absolute limits on the maturity of its portfolio. Consequently, the SEC can adopt Rule 22e-3 with confidence that the portfolio will be liquidated and distributed within 397 days, and (with the new weighted average life limitation) a majority of the portfolio will be liquidated within 120 days (and probably sooner). The only exception would be defaulted securities which may require some additional time before a bankruptcy or other workout can be completed. Delays resulting from such defaults are unavoidable and should not prevent the SEC from adopting the proposed rule.

If the SEC extends Rule 22e-3 to other types of mutual funds, then neither the SEC nor the liquidating Money Fund's shareholders will have any assurance as to when the liquidation will be substantially completed. Winding up other types of investment companies could easily take several years, with erratic distributions to shareholders. It may be more appropriate for these other types of investment companies to go through the order process, so that the SEC has an adequate opportunity to consider these issues.

2. Should the fund be required to disclose its liquidation plan to shareholders?

Federated believes that shareholder communication is critical in times of financial crisis. While we would expect the Board of a liquidating Money Fund to communicate regularly with shareholders regarding the status of the liquidation, requiring this as a condition to suspensions of redemptions would help to assure this result.

3. Should we permit or require a fund board to recognize that investors will have different preferences for liquidity and capital preservation? For example, a fund that decides to liquidate and suspend redemptions could be allowed to offer shareholders the choice of redeeming their shares immediately at a reduced net asset value per share that reflects the fair market value of fund assets, *i.e.*, at a price below the fund's stable net asset value. Remaining shareholders would receive their redemption proceeds at the end of the liquidation process and may receive the economic benefit of an orderly disposal of assets. Would such an approach be fair to all fund shareholders?

Allowing investors a choice between maximizing liquidity and maximizing recovery may be an ideal approach, but would probably be impractical. This approach assumes that every security in the portfolio can be sold at some price, which may not be the case in every liquidation. For example, if the Money Fund holds a defaulted security, there may be no buyers at any price. Moreover, if the Money Fund participates in a workout committee, it may be prohibited from trading the security due to its access to material nonpublic information.

One solution for securities that the Money Fund cannot dispose of would be to deliver these to the redeeming shareholder in-kind. As explained in more detail below, however, not all shareholders will be qualified to hold such securities. In addition, the shareholder's pro rata share of the security may not correspond to a permissible denomination.

Ultimately, Federated does not see how this approach can work unless the SEC permits the redeeming shareholder to waive its right to a *pro rata* share of securities that cannot be disposed of or transferred in-kind without regarding the waiver as a violation of Section 18(f) and the definition of a "redeemable security." This is the only means of protecting the remaining shareholders against the risk of misvaluing these assets. In all events, Federated would not recommend *requiring* a Board to include this option as a condition to suspending redemptions during liquidation.

4. Should funds be able to deduct an additional discount or "haircut" from earlier redeeming shareholders to provide additional protection for later redeeming shareholders?

Federated does not see how an arbitrary "haircut" would be fair to redeeming shareholders. To the extent that this is intended to prevent uncertainty as to the valuation of the portfolio, the better course of action would be to have the liquidating Money Fund use its best efforts to sell the redeeming shareholder's pro rata share of the portfolio, and use the trades to determine the redemption amount. This would effectively impose the full costs of liquidity on redeeming shareholders, instead trying to estimate these costs through a "haircut" that is almost certain to be too high or too low.

IV. SECOND TIER SECURITIES

Federated strongly believes that the Commission should continue to allow investment companies to hold Second Tier Securities. As noted by the Commission in the Proposing Release, Second Tier Securities were not directly implicated in the recent strains on Money Funds and the economy.[27] Given the additional investment protections included in Proposed Rule 2a-7, Federated believes that the benefit of investing in Second Tier Securities far outweighs any potential increased credit risk.

Investments in Second Tier Securities by Money Funds (i) reduce concentration in the financial sector, (ii) provide greater credit diversification of investments, particularly for Tax Exempt Funds, and (iii) provide a more affordable means of financing issuers of Second Tier Securities. Exhibit B shows the Second Tier issuers who might lose funding as a result of this proposed reform. It is noteworthy that all of these issuers are outside of the financial sector, and thus reduce overall concentration while enhancing a portfolio's diversity. Additionally, Tax Exempt Funds, and in particular single state Tax Exempt Funds, may not have sufficient supply of First Tier Securities to diversify their assets, especially during periods of economic stress in a state's economy. Prohibiting Tax Exempt Funds from holding Second Tier securities could leave them incapable of dealing with down cycles in the state's economy, when a state or locality may receive a Second Tier rating.

[27] Proposing Release at 32695

The current situation in California is instructive, as the state has received Second Tier ratings. Until the state's economy improves, under Proposed Rule 2a-7, all Money Funds holding California securities would be required to dispose of the securities. Under these circumstances, the Money Funds would have difficulty managing an orderly disposition of the securities and could realize losses that could have been avoided by holding the securities to maturity. Proposed Rule 2a-7 also would deprive a clearly creditworthy issuer of an important source of financing during a critical point in the State's economic recovery.

If, however, the Commission is determined to revise the regulations surrounding investments by Money Funds in Second Tier Securities, there are alternative means of reducing a fund's exposure to the credit risk inherent in Second Tier securities other than an outright prohibition on investment. Federated would support any Commission action to:

- reduce, but not eliminate, the percentage of Money Fund assets permitted to be invested in Second Tier Securities;
- limit the final maturity of permissible Second Tier Securities, noting however the mismatch in maturities issued by tax-exempt issuers;[28] or
- limit any prohibition on investment in Second Tier Securities to taxable Money Funds.

Regardless of the methodology chosen by the Commission to regulate Second-Tier Securities, Federated strongly believes that Money Funds should not be required to treat any First-Tier Security that is downgraded to a Second Tier Security in the same manner as a defaulted security.

A. Limitations on Unrated Securities

Federated supports the ICI's position, outlined in its comment letter, that Tier-1 short term ratings generally are correlated to the top three tiers of long-term ratings, making a change to Rule 2a-7's quality standards associated with securities that have received long-term ratings unnecessary.

B. Conditional Demand Features Should Not Be Limited to Underlying Securities Rated in the Highest Long-Term Rating Category

Federated supports the ICI's position, outlined in its comment letter, that Conditional Demand Features should not be limited to underlying securities rated in the highest long-term rating category.

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[28] Tax exempt issuers of Non-Conduit Second Tier Securities typically issue securities with a final maturity of one year. Tax exempt issuers utilize a one year final maturity in order to align their revenue stream (*i.e.*, their receipt of taxes) with the final maturity of their securities. Consequently, further limitations on the maturity of Non-Conduit Second Tier Securities may have the same effect as excluding such securities from the definition of an Eligible Security.

C. Second Tier Non-Conduit Municipal Securities and Second Tier Conduit Securities

Federated strongly believes that Second Tier Non-Conduit Municipal Securities should not be treated in the same manner as Second Tier Conduit Securities. Rule 2a-7 distinguishes between Conduit and Non-Conduit Securities as the Commission has recognized that Non-Conduit securities present lower default risks due to the structural factors. If the Commission determines to prohibit Money Funds from investing in Second Tier Securities or determines to reduce the percentage of Second Tier Securities a Money Fund may invest in, such limitations should not apply to Second Tier Non-Conduit Municipal Securities. As proposed, both Second Tier Non-Conduit Municipal Securities and Second Tier Conduit Securities would be prohibited, which would subject Tax Exempt Funds to a higher standard than taxable Money Funds. Second Tier Non-Conduit Securities, because of the demonstrably lower default risks presented by these securities as compared to corporate commercial paper, should continue to be permissible investments for Tax Exempt Funds.

V. STRESS TESTING

Federated continues to support the Working Group's recommendation that Rule 2a-7 require Money Funds to adopt and implement written procedures requiring a Money Fund's adviser to conduct regular portfolio analysis that incorporates stress testing. As such, Federated generally agrees with the framework set forth in the Proposing Release and agrees that stress testing to assess a portfolio's ability to meet hypothesized levels of credit risk, shareholder redemptions, and interest rate changes could provide the adviser with a better understanding of its clients' needs, assist in determining appropriate levels of portfolio liquidity, and, if appropriately measured, provide Boards the framework to evaluate the magnitude of the events that would cause the Money Fund to break the buck.

Federated believes that stress tests should evaluate various market scenarios and the advisor should determine the assumptions used for stress tests. Federated does not believe it is necessary to test various scenarios that result in the same interest rate shift, as a shift in interest rates of x% will have the same impact on a Money Funds NAV, regardless of the circumstance that triggered it. Additionally, stress testing procedures should permit different tests for different types of Money Funds. For example, a test to evaluate the effect of downgrades might be appropriate for a prime Money Fund but not appropriate for a treasury Money Fund. It also might be appropriate to test the impact of changes in income tax rates on the value and redemption activity of a Tax Exempt Fund, but not any other type of Money Fund.

Federated does not, however, believe that requiring an adviser to provide an assessment of a "Money Fund's ability to withstand the events that are reasonably likely to occur within the following year"[29] will provide a Board with any meaningful information. The point of a stress test is to assess the risk of unexpected and unusual market events. An advisors' assessment of

[29] Proposed Rule 2a-7(c)(8)(ii)(D)(3).

anticipated events should always be positive and will tend to diffuse the results of the stress testing. Moreover, an adviser managing a portfolio consisting largely of securities maturing in 90 days or less will not necessarily regard one year as a logical period for assessment. In the unlikely event that the adviser expects a problem to arise that it cannot deal with, the adviser should report to the Board directly and not bury the problem in the context of stress testing results. Moreover, any assessment provided to a Board should include only the lowest combination of tested factors (*e.g.*, rate shifts and redemptions) that would reduce a Money Fund's shadow NAV below $0.995. This would focus Boards on only the most likely of the unlikely "break the dollar" scenarios tested.

Regardless of the type of stress testing mandated, Federated believes that all Money Funds, not just those using the Amortized Cost Method, should be required to conduct stress tests and report the results of such test to its Board. A stress test will assess the same risks even for Money Funds using the Penny-Rounding Method of pricing.

VI. PORTFOLIO MATURITY

Federated continues to support the Working Group's recommendations to (a) shorten the maximum dollar-weighted average portfolio maturity ("WAM") of all Money Funds to 75 days and (b) impose a new 120 day limit on the what the Proposing Release terms the dollar-weighted average portfolio life ("WAL") of a Money Fund. The WAL would be calculated differently than the WAM by treating securities as maturing on the earlier of their final legal maturity or the date on which the full principal amount would be paid upon exercise of a Demand Feature, while the WAM would be continue to treat certain Floating and Variable Rate Securities as maturing on their next scheduled interest rate adjustment.

Federated does not support the SEC proposal to limit the WAM to 60 days or less. As noted in our estimated impacts of the proposed reforms below, we believe that a reduction in the WAM to 60 days would reduce a taxable Money Fund's yield by twice as much (6 basis points) as a reduction in the WAM to 75 days (3 basis points). The reduced WAM would only decrease the portfolio's sensitivity to interest rate changes by about 4%, however, from a duration of slightly over .205 years at 75 days to slightly under .165 years at 60 days. Stated differently, a 4 basis point reduction in the sensitivity to a 100 basis point shift in interest rates would come at a continuous cost of 3 basis points a year. Clearly, the cost outweighs the benefit of this change.

The Proposing Release also asked for comment on whether the maximum permitted maturity of portfolio securities should be further limited. Currently, for Amortized Cost Money Funds, the only securities without Demand Features that can have final maturities in excess of 397 days are Government Floating and Variable Rate Securities. While the risk that such a security will begin to deviate significantly from its Amortized Cost increases with its maturity, the new 120-day WAL limit should control this risk.[30] To illustrate with an extreme example, a

[30] This risk is also controlled by the current requirement that the Money Fund reasonably expect the security's market value to return to its approximate Amortized Cost upon every interest rate adjustment throughout the security's remaining life. There is a limit (probably less than five years) to the period over which such an

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government Money Fund could invest 16% of its portfolio in two-year Variable Rate Securities and comply with the 120-day WAL limitation by investing the balance of the fund in overnight investments, but could only invest 11% in three-year Variable Rate Securities and remain in compliance with the WAL limitation. Thus, the WAL limitation operates to automatically tighten the risk controls if a Government Money Fund increases risks by extending maturities of Floating and Variable Rate Securities.

With respect to other types of Money Funds, Federated opposes any shortening of the 397-day maturity limitation on individual portfolio holdings. First, the SEC should realize that many issuers, particularly municipalities, do not have a choice as to the maturity of their notes. If the note is to be repaid with revenues that come in once a year (like taxes), then the note cannot mature before the revenues come in. The original justification for the thirteen-month limitation, to allow Tax Exempt Funds to agree to acquire one-year municipal notes up to a month prior to issuance, remains as valid today as it was when Rule 2a-7 was first adopted. One-year Treasury and Agency notes also are purchased on a "when-issued" basis, so a reduction of the maturity limit to even 365 days would effectively take Money Funds out of this vital part of the Government Securities market.

Second, the maturity of portfolio securities did not contribute to the problems that the SEC seeks to address with Proposed Rule Rule 2a-7. While many of the structured investment vehicle notes were issues with maximum final maturities of 397-days, they could have been issued just as easily with shorter maturities, particularly on an extendible basis. The final maturity of these notes had no significance for Money Funds, because the notes originally qualified as Variable Rate Securities deemed to mature on the date of their next interest rate adjustment. Here again, the new WAL limitation should provide a more effective control on the extent of the risks that can arise from reliance on Variable Rate Securities.

VII. OTHER PROPOSED CHANGES TO RULE 2A-7 AND OVERALL IMPACT

A. Repurchase Agreements

So far as Federated is aware, no adviser has had to provide any support to its Money Funds due to any default or other problem with a repurchase agreement, and repurchase agreements have performed well throughout the financial turmoil of the past twenty-four months. Nevertheless, Federated does not object to the limitation of the definition of "Collateralized Fully" to repurchase agreements for cash and Government Securities. Federated's Money Funds have never relied on the broader definition, choosing to treat repurchase agreements collateralized by non-Government Securities as obligations of the counterparty for purposes of diversification.

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expectation can be reasonably maintained. Here again, additional scrutiny during examinations as to the basis of the expectation for longer term Government Floating and Variable Rate Securities may be the best means of regulating this risk.

Federated does object, however, to the reintroduction of a separate “creditworthiness” requirement for repurchase agreements. This requirement was properly dropped in the last major revisions to Rule 2a-7, because it is already an element of the minimal credit risk requirement. The credit analysis of *any* investment, not just repurchase agreements, should begin with the question of whether the debtor can pay its obligation when due, before preceding to the question of what other recourse the fund would have if the debtor defaults. Reinstating a separate “creditworthiness” determination will leave Money Funds in the impossible position of explaining to their directors why the Board must review each repurchase agreement twice for what is essentially the same determination. If the SEC is determined to turn back the clock on repurchase agreements, it would be better to reinsert “including Demand Features and repurchase agreements” in the minimal credit risk requirement than to reimpose a creditworthiness determination by the Board.

B. Capacity to Convert to a Fluctuating NAV

Federated agrees that Money Funds should have the ability to sell and redeem securities at values other than a stable NAV. As with the ability to suspend redemptions, it is critical that a Board have this alternative available to it in the event of a crisis affecting a Money Fund’s ability to maintain a stable NAV. However, Proposed Rule 2a-7 would require an inordinate amount of effort to answer a fairly simply question: can everyone who processes orders for Money Fund shares do so at a fluctuating NAV calculated to the nearest tenth of a cent?

There is no reason to require the Board to make this determination, as it is entirely an operational issue. As with other changes, if Proposed Rule 2a-7 requires that Money Funds have this capacity, then Rule 38a-1 will require chief compliance officers to develop procedures for testing compliance with the new requirement and reporting the results to the Board. Moreover, once the capacity is developed, it should not just “go away,” so there is no reason to mandate an annual determination. Periodic testing of the capacity should suffice.

Federated has confirmed that the transfer agent systems used by its Money Funds can process share transactions at a fluctuating NAV. We also have determined that many intermediaries who process such transactions cannot. It will be expensive for these intermediaries to reprogram their systems to comply with the proposed requirement. While Federated regards this as a necessary expense, we encourage the SEC to provide a long transition period (at least a year) for compliance with this requirement. We also suggest that the SEC consider adopting regulations that would require all registered transfer agents, clearing agencies and broker-dealers who sell mutual funds (not just Money Funds) to develop the procedures and systems necessary to sell and redeem the funds in accordance with the terms of their prospectus.

C. Estimated Impact of Proposals on Money Fund Returns

The Proposing Release requested data on the potential effects of the various reforms on Money Fund yields. Federated therefore analyzed how it would have to restructure a prime Money Fund portfolio in response to the various proposals, and how the seven-day yield of the restructured portfolio would compare to a portfolio run in compliance with the current requirements of Rule 2a-7. Generally, Federated assumed for purposes of analysis that the

Money Fund was operating during normal market conditions, and not today's extraordinarily low rates. Federated also assumed, however, that Daily and Weekly Liquid Assets would continue to offer historically low spreads over the effective Fed Funds rate, due to reduced supply and increased demand for these investments. The following table summarizes the results of our analysis.

Requirement	**SEC Proposal**	**Impact** (in basis points)	**Federated Recommendation**	**Impact** (in basis points)
Second Tier Securities	0%	- 3	5%	0
WAM	60 days	- 6	75 days	- 3
WAL	120 days	- 3	120 days	- 3
Daily Liquid Assets	10%	- 0	5%	0
Weekly Liquid Assets	30%	- 9	20%	0
Illiquid Securities	0%	- 3	10%	0
Total Impact		**-24**		**-6**

Federated believes that the SEC should weigh this data carefully in considering whether the benefits of certain proposals are likely to outweigh the reduction in investor returns. The SEC should also consider that, until prevailing interest rates rise substantially, Money Fund cannot afford to lose much yield as a result of reform efforts.

VIII. MONITORING MONEY MARKET FUNDS

As noted in the discussion of the new liquidity requirements, Federated believes that active examination and oversight of the money market fund industry by the SEC is as important as any of the proposed regulatory reforms. Improved reporting by Money Funds to the SEC could facilitate the Division's oversight of Money Funds and alert them to emerging issues. It also could assist the examination staff in determining whether certain securities are widely held throughout the industry, or whether the funds under examination are outliers in some respect.

Reporting is costly, however, and it is important that the SEC tailor the new report to require only significant information that cannot be obtained more efficiently through other means. Federated also believes that the report should be used exclusively to monitor Money Funds, and should not be made publicly available. This would allow the report to include critical information for oversight purposes, without requiring public disclosure of sensitive information.

A. Comments on Form N-MFP as Proposed

As proposed, Form N-MFP requires a Money Fund to provide a great deal more information than a simple schedule of portfolio holdings. Federated does not believe that two business days is an adequate amount of time to collect the requested information (which must be obtained from a variety of systems) and verify its accuracy. Federated therefore joins in the ICI's recommendation of a ten-day filing period.

Federated also believes that Form N-MFP would require Money Funds to provide the SEC with redundant information that the SEC could obtain more efficiently from other sources. NRSRO rating information is an example of this.[31] As proposed, each month the SEC will receive hundreds of reports, each of which will contain the current ratings of all of the major banks and financial companies widely held by the industry. This rating information is available to the SEC through its Bloomberg subscription, and feeds can be obtained directly from the NRSROs. The cost of this ratings data would be far less than what it would cost every Money Fund to pull the information into a report, verify its accuracy and transmit it to the SEC. Issuer CIK numbers are another example, although in this case the SEC already has the information and most Money Funds do not maintain this information on their systems.

Items 32 and 33 appear to be internally redundant. Guarantee insurance is a form of credit enhancement, so all of the information that might appear under these items also will be reported in Items 30 and 31. It also would be helpful to use defined terms from Rule 2a-7 (namely, "Guarantee" and "Demand Feature") rather than "credit enhancement" and "liquidity provider," as Money Funds already use these classifications for purposes of complying with the rule. The form also should include an instruction that an Unconditional Demand Feature only needs to be reported in Items 30 and 31, and not repeated in Items 34 and 35.

Federated does not understand some of the other elements of proposed Form N-MFP. For example, why should amortized cost values be calculated to the nearest one-hundredth of a percent? So long as a Money Fund maintains a stable NAV, this will simply add two more zeros to the $1.00 reported in Item 14. In the case of the total portfolio (Item 12) and individual holdings (Item 37), a hundred dollars is insignificant, much less a hundredth of a cent. Moreover, accounting systems only carry costs in whole cents.

Items 9 and 29 are ambiguous. The "cash collateral" referred to in Item 9 could include corporate trust accounts (indentures typically grant a security interest in trustee accounts) and escrows as well as collateral for securities loans or over-the-counter derivatives. Why would the SEC want to track these investments? How will a Money Fund know when it starts being used "primarily" for these investments? With respect to Item 29, does "extendable" mean beyond the final legal maturity date? The answer to this will always be no, unless the report is trying to identify securities that are extendable at the Money Fund's option. Why would the SEC be interested in these securities?

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[31] We are referring to Item 26, not Item 25 which, though captioned "Rating," calls for each portfolio security's status as a First Tier Security, Unrated Security or no longer Eligible Security. Item 25 is confusing as well, because Unrated Securities can be First Tier Securities, and, as proposed, only First Tier Securities would qualify as Eligible Securities. If the SEC ultimately adopts this proposal, it may make more sense for this item to identify securities as Rated or Unrated Eligible Securities, or securities that are no longer Eligible Securities. If the Second Tier Securities are still permitted, they could be identified in this item. The SEC also should consider having the form identify Conduit Securities and the underlying issuer of a Conduit Security.

The significance of some other items also is unclear. For example, while we can understand why it would be useful to know why a Money Fund was making its final report, we are not sure why it would matter whether the Money Fund was "merged" or "acquired." The request for FAS 157 information is also puzzling. This information is required in financial reports that Money Funds prepare semi-annually, not monthly. The valuations used in these financial reports are, with rare exceptions, the amortized cost values, which are classified as Level 2 under FAS 157.[32] These are not the valuations used to shadow price the portfolio. Such shadow pricing is not subject to FAS 157.

Finally, Federated requests that the SEC consider coordinating the categories of investments listed in Item 24 with the information rated Money Funds provide to certain NRSROs. A list of categories used by Standard & Poor's is attached as Exhibit C to this letter. As many Money Fund complexes have at least some rated funds, they will have already categorized securities according to the NRSRO requirements. Using the same categories will prevent the Money Funds from having to repeat the exercise using a somewhat different, and not fully consistent, set of categories.

B. Other Items to Consider Monitoring

Ideally, the data provided in Form N-MFP should conform to the monthly report that the Division will use to monitor developments in the money market fund industry. We anticipate that the staff will want to monitor the three significant risks addressed in revised Rule 2a-7: interest rates, credit and liquidity. The proposed form omits, however, information that would be useful in monitoring these risks. For example, although Form N-MFP will provide the current WAM and WAL for each Money Fund, it will not identify which securities are Variable or Floating Rate Securities, the frequency with which they are adjusted or the benchmark on which adjustments are based. If the SEC does not already have another means of obtaining this information (interest terms are available on Bloomberg for many securities, but not universally), it may be worth the cost to have the Money Funds report it on the form. Even if the details of the interest adjustment are not reported, it would still be useful for the staff to know if some Money Funds treat a security as Variable or Floating while others do not.

With respect to credit, as already noted, the proposed form would provide largely redundant rating information. However, the form would not require disclosure of any change in the Money Fund's own credit assessment. We expect that the staff would find it useful to know that an issuer is no longer approved for acquisition by a Money Fund, or that the Money Fund has determined that a security no longer presents minimal credit risks. In many cases, these changes may precede a downgrading of the issuer by an NRSRO.

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[32] The proposed form allows for an "Other" category of valuation inputs, which is not recognized by FAS 157.

Finally, with respect to liquidity, we presume that the staff will be able to monitor the amount of Daily and Weekly Liquid Assets based on the maturity information and investment categories already called for in Form N-MFP. The form also provides for monthly net cash flows. The form does not, however, require any indication as to whether a portfolio security is considered illiquid. This may reflect the proposed prohibition on the acquisition of illiquid securities, but it is possible for liquid securities to become illiquid. Here again, it may be useful to know that different Money Funds have taken different positions regarding the liquidity of a commonly held security.

C. The SEC Should Not Make the Information Reported on Form N-MFP Publicly Available

It is important for the SEC to appreciate that, while this type of information may enhance the staff's ability to monitor the money market fund industry in many respects, Money Funds regard this information as highly sensitive and confidential. Money Funds would have a legitimate fear that, if disclosed, certain information could be used to create a competitive disadvantage. Therefore, Federated urges the SEC to use the information provided in Form N-MFP solely for monitoring purposes, and not to disclose the information publicly. If the SEC is willing to retain such information in confidence, then it may be appropriate to include even more sensitive information, such as whether the shadow NAV has deviated from the stable NAV beyond a specified threshold. In all events, the SEC should be mindful that a Money Fund's competitors will monitor any information publicly disclosed from the report, and may use the information for competitive purposes that are not consistent with the interests of the overall market.

IX. AFFILIATED TRANSACTIONS

Several Money Funds held Lehman Brothers obligations after the company announced its bankruptcy filing on September 15, 2008. Large scale redemptions did not begin, however, until the Primary Fund announced on September 16 that its adviser could not support the share price at $1.00. This strongly suggests that the ensuing "run on the funds" resulted less from expectations as to the ability of Money Funds to avoid defaults and more from what some shareholders expected the adviser to do in response to a default. In other words, the unwarranted belief of some shareholders, in direct contradiction to the expressed disclosures made in all Money Fund prospectuses and advertisements, that a Money Fund's adviser will guarantee a stable NAV may be the greatest systemic risk faced by the industry.

Federated does not believe that the SEC should make any changes that would reinforce such unwarranted beliefs. What is needed at this point, now that the credit markets are recovered and there is ample liquidity, is a frank, public discussion of the risks of investing in Money Funds, leading to an acceptance of these risks by investors. Shareholders who cannot accept such risk should leave Money Funds now, rather than in a panic at a time of crisis.

Federated fears that the proposed amendments to Rule 17a-9 will serve to foster shareholders' expectations of a rescue in the event of a default by further facilitating an adviser's ability to support its Money Funds. Thus, the amendments would be counterproductive to the SEC's overall aim of reducing systemic risks in the securities markets. Although the current practice of providing rapid no-action relief for affiliated transactions is time-consuming for the Division's staff, it at least allows them to consider the policy implications of the adviser's actions, rather than simply allowing the adviser to inform the Division after the fact.

X. OTHER REQUESTS FOR COMMENT

The Proposing Release contains numerous requests for comments. Two of the general requests, regarding whether the SEC should continue to permit Money Funds to use a stable NAV or to be limited by NRSRO ratings, revive issues that were fully vetted and resolved thirty years ago when the SEC issued the initial exemptive orders. Although there is little point in rehashing these issues, they are too significant to pass by without some comment. Federated also would like to respond to the questions posed regarding redemption in-kind, redemption fees and asset backed securities, which pose novel issues and have at least some potential to further the SEC's objective of "mak[ing] money market funds more resilient to certain short-term market risks, and [providing] greater protections for investors in a money market fund that is unable to maintain a stable net asset value per share."

A. The SEC Should Not Outlaw Money Market Funds

Rule 2a-7 is an exemption from "section 2(a)(41) of the Act … and of [Rules] 2a-4 and 22c-1 thereunder," which require open-end management investment companies to calculate their NAV to the nearest tenth of a percent (*i.e.*, one penny on an NAV of $10.00) using available market quotations. If Money Funds are required to calculate a fluctuating NAV like every other mutual fund, then Rule 2a-7 will no longer serve any purpose. Therefore, any proposal to no longer permit Money Funds to maintain a stable NAV is essentially a proposal to repeal Rule 2a-7. Even if the SEC were to retain some vestigial version of Rule 2a-7 for purposes of regulating the name "money market fund" (a name that Federated coined with its first fund), from the shareholder's perspective there would not be any difference between a Money Fund and any other bond fund.

Federated's experience leaves us with no doubt as to the consequences of forcing Money Funds to use a fluctuating NAV. In addition to Money Funds, Federated manages and distributes a full range of "Ultrashort" bond funds, the least volatile of the fluctuating NAV funds.[33] For extended periods, the relative yields on Federated's Ultrashort funds were substantially higher than the yields on comparable Money Funds. Although Federated actively marketed its Ultrashort funds during these periods, it found that few investors wanted to use a fluctuating NAV fund for cash management purposes, and the assets in the Ultrashort funds have never exceeded 1.65% of the assets held in Federated's Money Funds.

[33] Unlike some other Ultrashort funds, Federated's have a solid track record of stability. In the ten years after the introduction of the first Federated Ultrashort fund in 1997, the lowest annual return was -2.54%.

Federated's experience is consistent with the industry's. At their high point July 2003, Ultrashort funds reported assets of just over $70 billion—one-twentieth of the assets then held in taxable Money Funds.[34] Our experience and market data all support one conclusion—that only a small fraction of the trillions of dollars currently invested in Money Funds would remain there if the SEC required them to use fluctuating NAVs. The SEC's proposal would force trillions of dollars out of the industry and into banks and other, less regulated, stable value products.

The adverse consequences to investors of such a shift in money market assets would be enormous. The Working Group estimated that retail investors alone earned over $200 billion more in returns from Money Funds than they would have earned from bank deposit accounts during the ten years ending in 2008.[35] We would expect that actual losses to investors to be much greater if Money Funds were forced to use fluctuating NAVs, as banks would no longer have any meaningful competition for deposit accounts. Elimination of Money Funds as a substantial participant in the short-term market also would produce substantial economic disruptions, as companies would be forced out of the commercial paper market and back to banks as their principal source of working capital.[36] In short, Federated does not see any tangible benefit that would justify the hundreds of billions of dollars of lost economic opportunities that would result from prohibiting Money Funds from seeking to maintain a stable NAV.

B. NRSRO Ratings

Federated supports the ICI's comments on the need to maintain NRSRO rating standards in Rule 2a-7. Federated also reiterates the comments made in its September 5, 2008, letter on the earlier proposal to eliminate references to NRSRO ratings from Rule 2a-7. Federated would amend its earlier recommendation, however, to require that Money Funds designate no fewer than *five* NRSROs that would be used for purposes of making determinations required under Rule 2a-7. Federated does not think that five is an unreasonably large number of NRSROs for a Money Fund's adviser to subscribe to and monitor. This also will support new entrants into the NRSRO market by forcing advisers to consider credit agencies in addition to the big three. If the SEC takes this approach, it also should make it clear that an adviser can designate an NRSRO for select types of securities, *e.g.*, insurance company or municipal obligations, and may therefore disregard ratings of other non-designated types of securities.

We do not think that the Board is qualified to select which NRSROs should be used, however, and would not recommend adding this to the Board's responsibilities. Obviously, the adviser should inform the Board as to which NRSROs have been designated and the basis for

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34 Ultrashort Fund assets determined from Lipper LANA; Money Fund assets from ICI.

35 Report at 25.

36 Moreover, Federated does not see how the SEC could possibly transition Money Funds to a fluctuating NAV without risking another run on the funds and freezing up of the credit markets. Investors seeking a stable value investment would undoubtedly pull their money from the Money Funds in advance of the conversion date, and the Money Funds would have to stop acquiring new investments in anticipation of the mass of redemptions.

their selection. We are less sure that the registration statement should disclose the designated NRSROs, as most investors will probably not consider this material information and it would be costly to sticker the registration statement every time a new NRSRO is designated.

C. The SEC Should Facilitate Redemptions In-Kind by Distressed Money Market Funds, without Requiring Them

A team at Federated has analyzed the feasibility of using redemptions in-kind for large redemption requests under illiquid market conditions. The team's analysis has identified the following significant challenges to implementing redemptions in-kind on a large scale under such conditions:

1. Non-Transferable Securities. Certain securities, such as master notes, funding agreements and term repurchase agreements, do not permit transfers without the consent of the issuer. Federated does not believe that issuers would consent to such transfers for purposes of redemption in-kind. Although other portfolio securities might be allocated to redeeming shareholders in lieu of non-transferrable securities, at some point this would produce unfair results for the remaining shareholders.

2. Restricted Securities. Other securities can be transferred only if certain conditions are satisfied. For example, most securities acquired by a Money Fund in reliance on Rule 144A can be transferred to only another "Qualified Institutional Buyer" as defined in that rule. A Money Fund cannot tell whether a redeeming shareholder meets these conditions without obtaining additional information from the shareholder. If the redeeming shareholder holds it shares through an intermediary, this requires the intermediary's cooperation. If the redeeming shareholder does not qualify, redemption in-kind will have the effect of increasing the share of restricted securities represented in the remaining portfolio, which may produce unfair results for the remaining shareholders.

3. Minimum Denominations. Many securities restrict the minimum face amount that may be transferred. Clearing agencies do not, however, provide a systematic way to determine such minimum transferable denominations. To the extent a pro rata redemption would require transfers below the minimum denomination, a larger share of other securities must be transferred instead. In the case of smaller redemption amounts (*e.g.*, under 1% of Total Assets), the preponderance of securities that would not meet the minimum denomination requirements may make an in-kind redemption impractical.

4. Multiple Redemptions. Redemption in-kind works best when a large shareholder redeems all of its shares. Nothing prevents a shareholder from making daily redemption requests in an amount too small to be dealt with through redemption in-kind, however. This strategy could allow a shareholder to effectively circumvent redemption in-kind.

5. Section 18(f) and Rule 18f-1. All of Federated's Money Funds that have reserved the right to redeem in-kind have made the election permitted under Rule 18f-1. Rule 18f-1 provides that shareholders are entitled to receive, during any ninety-day period, cash redemptions equal to the lesser of $250,000 or 1% of the Money

> Fund's assets. The SEC adopted Rule 18f-1 in response to undertakings required by certain state securities administrators "that, as to residents within their respective jurisdictions, redemptions will be effected in cash only, or that redemptions in kind will not be effected unless specific approval therefor is first obtained from the securities administrator."[37] In the release adopting Rule 18f-1, the SEC stated that: "Such requirements would involve priorities as to distribution of assets and thus give rise to prohibited senior securities within the meaning of Section 18 of the Act."[38]
>
> This cryptic statement raises some doubt as to the extent to which a Money Fund could use redemption in-kind selectively among shareholders. For example, the minimum denomination requirements make it likely that redemption in-kind would not be practical for redemptions below a certain threshold. If this is the case, and a Board determined to pay all redemptions in cash up to an amount greater than $250,000, could the commitment to a higher limit than specified in Rule 18f-1 risk a potential violation of Section 18(f)?
>
> Alternatively, does the SEC consider Section 18(f) to require a Money Fund to treat all shareholders who redeem the same number of shares in the same manner? Suppose, for example, a shareholder who is a Qualified Institutional Buyer redeems the same number of shares as a shareholder who is not. Would the Money Fund violate Section 18(f) if it gave the Qualified Institutional Buyer restricted securities and the other shareholder freely tradable securities? Suppose further that one shareholder gave a week's notice of its redemption, giving the Money Fund ample time to raise the cash necessary for the redemption, and another shareholder notifies the Money Fund of its redemption of the same number of shares at the last minute. Could the fund proceed to redeem the first shareholder in cash, while redeeming the second shareholder in kind?

Notwithstanding these challenges, Federated believes that redemption in-kind could be a viable alternative in a limited range of circumstances. The circumstances would involve large redemptions (probably well in excess of $250,000) to allow redemptions in-kind in excess of the minimum denominations; however, the aggregate amount of redemptions in-kind would have to be limited so as to avoid leaving the remaining shareholders with a less favorable portfolio. Further guidance by the SEC on the application of Section 18(f) to such redemptions would aid Money Funds in implementing a redemption in-kind program should the need arise. Nevertheless, given the inherent limitations and challenges of redemption in-kind, Federated does not see any basis on which the SEC could require Money Funds to implement, or even to reserve the right to implement, redemption in-kind. Redemption in-kind should be an alternative available to the Board (along with breaking a dollar or liquidation), but should not be required by Rule 2a-7.

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[37] Investment Company Act Release No. 6561, Adoption of Rule 18f-1 and Form N-18F-1 Under the Investment Company Act, [1970-71 Transfer Binder] Fed. Sec, L. Rep, ¶ 78,124, (June 14, 1971).

[38] *Id.*

D. The SEC Should Not Require Money Market Funds to Impose Redemptions Fees

A redemption fee would be contrary to the "dollar in/dollar out" benefit of a Money Fund. Although less intrusive, Federated expects that the affect of a regular redemption fee (*i.e.*, a fee charged if an individual's redemptions over a specified period exceed a specified amount) would be the same as simply capping the maximum amount that could be invested in a fund. Shareholders would maintain their account balances just below the amount that would trigger the redemption fee. This would give larger funds (which could set higher thresholds before redemption fees are charged) a competitive advantage over smaller funds, resulting in further concentration of assets and increased systemic risks.

On the other hand, a redemption fee that is "triggered," *e.g.*, by redemptions exceeding a certain percentage in the aggregate, might have much the same effect as breaking a dollar. We would expect sophisticated shareholders to monitor the "trigger" for the redemption fee, and try to redeem before the fee is imposed. Thus, an exception-based redemption fee may create precisely the risk it is intended to avoid—a run on the fund.

E. Asset Backed Securities

The Proposing Release includes several requests for comment on Asset Backed Securities ("ABS"). We would like to address two of these requests.

1. <u>Whether rule 2a-7 should explicitly require fund boards of directors (or their delegates) to evaluate whether the security includes any committed line of credit or other liquidity support. Are there other factors that we should require money market fund boards to evaluate when determining whether SIV investments or other new financial products pose minimal credit risks?</u>

Although the lack of fully committed liquidity support contributed to the failures of structured investment vehicles in 2007, not all ABS require such support. For many ABS, the regular cash flow from the Qualifying Assets is more than sufficient to repay the ABS sold to Money Funds. Other ABS require less than 100% liquidity support to supplement the cash flow from the Qualifying Assets. Although it might be useful for Rule 2a-7 to distinguish between ABS that require liquidity support and ABS that do not, this would require adding another detailed definition to an already complicated rule.

Federated suggests a simpler approach to the same end by requiring Money Funds to base their minimal credit risk determination for ABS on factors other than (a) the Special Purpose Entity's ability to obtain funding that no one has committed to provide or (b) the Special Purpose Entity's ability to dispose of Qualifying Assets in market transactions. This approach will prevent an investment adviser from assuming that a Special Purpose Entity will obtain uncommitted funding, either by continuing to roll over ABS or selling Qualifying Assets, without having to catalogue the myriad forms that committed funding may take.

2. Alternatively, should the rule itself require ABSs to be subject to unconditional demand features to be eligible securities?

This proposal would have disastrous economic consequences. Properly structured, ABS allow Money Funds to isolate Qualifying Assets from the risks associated with their originator's business. This leads to a true increase in diversification, as each Special Purpose Entity can continue to perform and pay its obligations regardless of what happens to the originators of their Qualifying Assets. Requiring that all ABS be effectively Guaranteed (through an Unconditional Demand Feature or otherwise) would eliminate the benefit of this diversification, by requiring Money Funds to limit their ABS investments in compliance with the diversification limits of Rule 2a-7. Given the limited number of entities whose Guarantees could currently qualify as Eligible Securities (most of which also issue direct obligations held by Money Funds), this would sharply curtail the supply of Eligible ABS for Money Funds. It also would impose enormous and needless expense on companies financing through ABS, as they would need to compensate the Guarantors for the risk capital required by regulations to cover the Guarantees. Federated strongly discourages the SEC from considering this proposal.

XI. CONCLUSION

Federated hopes that the SEC finds these comments helpful and constructive. We have noted the SEC's comments that it may take a multi-step approach to Money Fund reform, and encourage the SEC to follow this approach. This would entail adopting only those changes to Rule 2a-7 that have been fully vetted through the comment process and would provide clear benefits to investors. Other proposed changes, including modified versions of proposals included in the Proposing Release as well as new proposals generated by responses to request for comment, should not be adopted without first obtaining comments on the specific proposal. Federated believes that, by following this approach, the SEC will be able to implement the most important revisions (such as the proposed liquidity requirements) without creating unintended consequences that may damage the Money Fund industry or the credit markets generally.

Please feel free to contact us if you have any questions or require additional information relating to our comments.

Yours very truly,

/s/ John W. McGonigle
Executive Vice President and Chief Legal Officer

EXHIBIT A

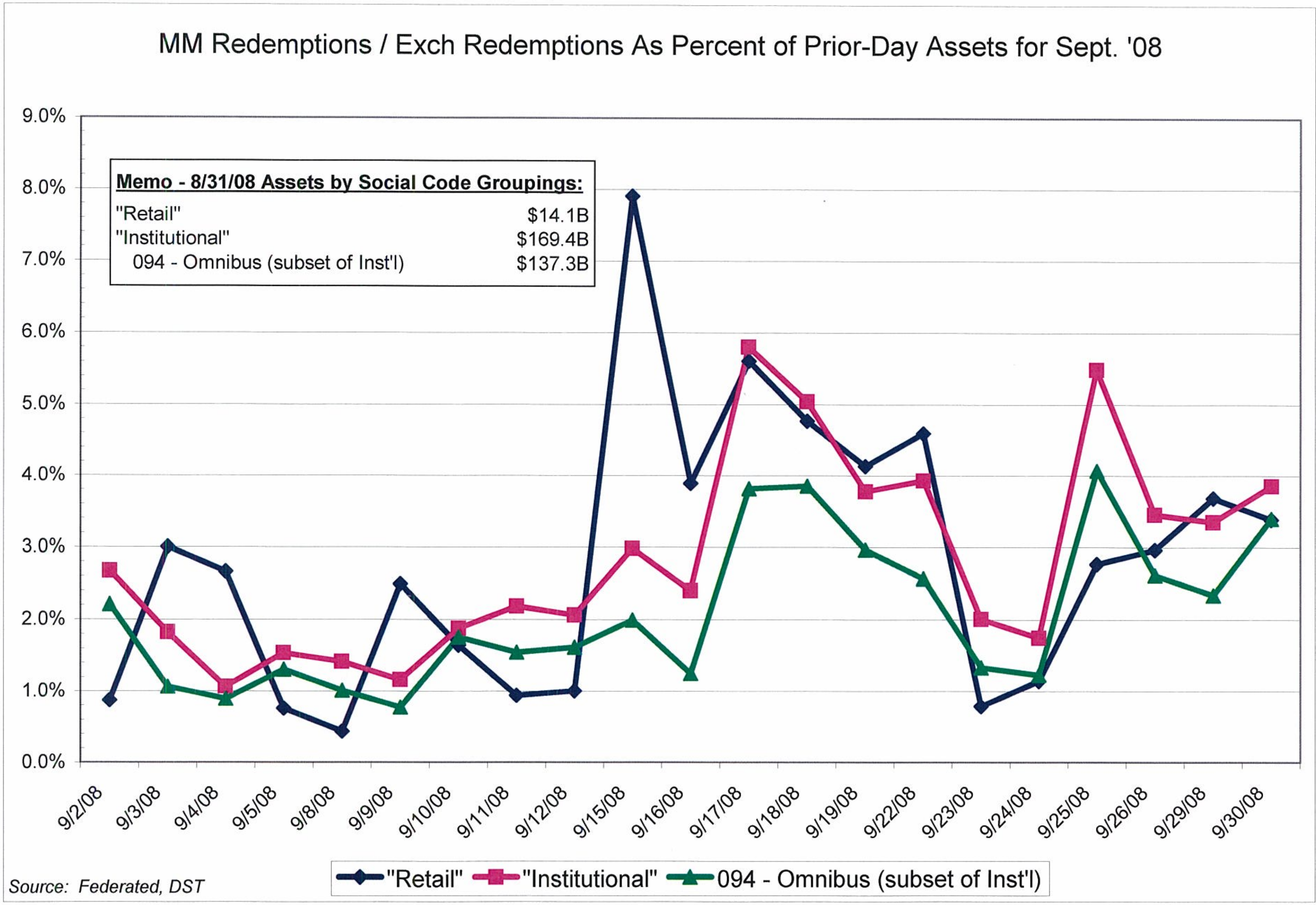
MM Redemptions / Exch Redemptions As Percent of Prior-Day Assets for Sept. '08
9.0%
8.0%
7.0%
6.0%
5.0%
4.0%
3.0%
2.0%
1.0%
0.0%
Memo - 8/31/08 Assets by Social Code Groupings:
"Retail" $14.1B
"Institutional" $169.4B
094 - Omnibus (subset of Inst'l) $137.3B
9/2/08
9/3/08
9/4/08
9/5/08
9/8/08
9/9/08
9/10/08
9/11/08
9/12/08
9/15/08
9/16/08
9/17/08
9/18/08
9/19/08
9/22/08
9/23/08
9/24/08
9/25/08
9/26/08
9/29/08
9/30/08
Source: Federated, DST
"Retail"
"Institutional"
094 - Omnibus (subset of Inst'l)

EXHIBIT B

#	Security Description	Industry	Credit Provider	Credit Type	S&P	Moody's	Fitch	Explanation
1	Bemis Co., Inc.	Container/Packaging			A-1	P-2	NA	Manufacturer of flexible packaging and pressure sensitive materials. Strong market share, moderate liquidity profile, and relatively conservative financial policies.
2	Clorox Corp.	Consumer Products			A-2	P-2	F2	Strong portfolio of market-leading products; strong & stable margins, cash flow, and profitability.
3	CVS Caremark Corp.	Retail			A-2	P-2	F2	A large U.S. retailer in pharmacy space; 80% non-front end retail; strong cash flows; access to term markets; strong bank-line support; strong diversification away from pure front-end retail sales.
4	General Mills, Inc.	Food & Beverage			A-2	P-2	F2	Strong brand name and market share; diversified mix of products; international presence; strong cash flow, but thin capital levels.
5	H.J. Heinz Finance Co.	Food & Beverage	H.J. Heinz Co.	GTD	A-2	P-2	F2	Guarantee from H.J. Heinz Co. - Heinz is a market leader in food industry; strong portfolio of products; good cash flow; shareholder activism remains a concern.
6	Hartford Life Insurance Co.	Insurance			A-1	P-2	NA	Part of Hartford Financial Services Group. A broadly diversified insurance company.
7	Home Depot, Inc.	Retail			A-2	P-2	F2	The leading home improvement retailer in the U.S.; solid liquidity profile; strong cash flow.
8	ITT Corp.	Diversified			A-2	P-2	F2	ITT Corp. is a multi business conglomerate; revenues are growing via acquisitions and organically; cash flow is strong; management is committed to debt reduction.
9	Vodafone Group PLC	Telecommunications			A-2	P-2	F2	A large U.K. based global telecom provider; strong cash flows; access to term markets; strong bank-line support; strong diversification.

As of September 2, 2009

EXHIBIT C

Categories of Securities

Taxable Securities:

Asset Backed Notes	ABS
Agency Floating Rate	AFR
Agency (Fixed Rate)	AGCY
Banker Acceptance	BA
Corporate Floating Rate	CFR
Certificate of Deposit/Bank Notes	DCD
Commercial Paper	DCP
Credit Lined Notes	CLN
Collateralized Debt Obligations	CDO
Extendible Asset-Backed (SLN/TLN)	EABS
Extendible Commercial Note (corporate)	ECN
Extendible At Holder Option (corporate)	EATO
Funding Agreement	FA
Loan Participation	LP
Corporate Note	NOTE
Money Market Funds	OTHR_MMF
Promissory Notes	PROM
Repurchase Agreement	REPO
Treasury Bill	TBILL
Time Deposits	TD
Taxable Muni	TMUNI
Treasury Notes	TNOTE
Cash	CASH
Other (Please Specify)	OTHER

Tax Exempt Securities:

Municipal Notes	MUNT
Municipal Bonds	MUBD
Municipal Zeros	MUZRO
Variable Rate Demand Notes	MUVR
Muni Commercial Paper	MUCP
Tender Option Bonds	MUTEN
Cash	CASH
Other (Please Specify)	OTHER