IMMFA

INSTITUTIONAL MONEY MARKET FUNDS ASSOCIATION

8 September 2009

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

Dear Ms Murphy

RE: Proposed changes to Rule 2a-7

The Institutional Money Market Funds Association (IMMFA) welcomes the opportunity to comment on the proposed amendments to Rule 2a-7.

IMMFA is the trade association which represents the European triple-A rated money market funds industry. Triple-A[1] money market funds are managed according to rigid and transparent guidelines, in order to offer safety of principal, liquidity and competitive money market returns. Increasingly, these funds are used by institutional investors to manage liquidity and act as important alternatives to cash accounts. Since its inception in 2000, IMMFA's funds in Europe have grown from around $50 billion to over $600 billion (as at July 2009). Further information on the association and triple-A rated funds are available on the IMMFA website, www.immfa.org.

Based upon our experience in Europe, we broadly support the proposals for amendments to the existing US regulatory framework for money market funds. In light of our experience during 2008, we are currently engaged in an exercise to improve the resilience of our Members' money market funds, which will be implemented through revisions to the IMMFA Code of Practice. We therefore welcome the attempts of the SEC to enhance the existing regulatory framework in the US and to better enable money market funds to provide security and liquidity for investors and to increase disclosure. In many respects, our thinking is consistent with that of the SEC as attempts are made to limit the risk inherent within a money market fund and better educate investors on these risks.

Whilst we generally welcome the proposals, we note the request for comment on some more fundamental issues, including the retention of a stable net asset value. Our members and their investors remain committed to a stable net asset value as this more adequately reflects the nature of the product and provides ease of administration and accounting for investors. However, both stable and floating net asset value funds operate in Europe, and

[1] References to money market funds in this letter means funds rated specifically AAAm by Standard & Poor's, Aaa/MR1+ by Moody's Investors Service and AAA/V1+ by Fitch Ratings – that price on an amortised accounting basis.

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both have seen sizeable growth in recent years, an indication of the flight to quality in turbulent times[2]. There is clearly investor appetite for both funds.

However, both fund types contain inherent risks. Moving from one valuation methodology to another will not mitigate this risk, and we therefore consider there to be more prudent means of limiting the risk within the portfolio than altering the valuation methodology. We therefore support the concepts concerning liquidity and maturity and will be implementing similar obligations through the IMMFA Code of Practice, but will continue to operate on a stable net asset value basis.

We comment below on those proposals which directly impact our Members.

If you have any questions, do not hesitate to contact me.

Yours sincerely

Gail Le Coz
CEO, IMMFA

[2] From June 2007 to December 2008, assets under management in IMMFA funds increased by 31% (source: iMoneyNet). For the same period, assets in Tresorerie Reguliere funds increased by 8% (source: Europerformance).

Portfolio quality

Use of NRSROs

The proposals question how greater independent credit risk analysis could be encouraged of money market fund managers, and concurrently question whether references to nationally recognised statistical rating organisations (NRSROs) should be removed. As per our response to similar proposals in 2008, we do not consider that references to NRSROs should be removed from Rule 2a-7. The ratings provide a floor for the credit quality of the underlying instruments within a portfolio below which the fund is not permitted to stray. This provides a minimum level of investor protection. The removal of this standard would provide leeway for interpretation and could potentially result in a lowering of those standards if funds accept greater risk in attempts to secure additional investment.

Given the interconnectedness of the global money market fund industry, we would not welcome any proposal which we consider has the propensity to lower the standards in operation in any part of the global money market fund industry.

Portfolio maturity

Weighted Average Maturity

We welcome the proposal to reduce the maximum weighted average maturity to 60 days. This maximum has been imposed on IMMFA funds since the implementation of the Code of Practice in 2002.

Weighted Average Life

We also welcome the proposal to introduce a maximum weighted average life (WAL) of 120 days. Independent from the recommendations of the ICI, we had determined that a maximum WAL was required in order to restrict credit risk within a fund. Our analysis considered stress periods since 1933 and the impact of a 400-600 basis point spread widening. We identified that a maximum WAL of 120 days would be appropriate to protect the net asset value of the fund from falling below 0.9951. We therefore support the proposed introduction.

The proposed reduction in the WAM and the introduction of a WAL will aid global consistency and facilitate greater understanding amongst investors operating on a global basis. However, our preference is to use the term weighted average final maturity (WAFM) due to the fact that WAL has negative connotations in investors' minds, due to its use with complex asset-backed security structures. In the interests of fostering greater global consistency, we would welcome the adoption of WAFM as the terminology used to measure credit and interest rate spread risks.

Maturity Limit for Portfolio Securities

We note the question regarding the maturity limit for portfolio securities other than government securities, including whether this should be limited to only 270 days. Our members manage over $275 billion of USD denominated money market funds, and are therefore an active aspect of the US money market. Having regard to the criteria of the three principal rating agencies, our members are generally limited to purchasing no asset which has a final maturity of more than 397 days. Indeed, we are considering whether this limit should be explicitly included within the IMMFA Code of Practice.

We consider that a maximum maturity of 270 days for US money market funds could materially alter the securities available to other participants in the money market, and would therefore alter the funding portfolio of the issuers of those securities. It would also limit the diversification which could be achieved within a money market fund portfolio. We consider that duration should be minimised through the introduction of appropriate limits for the maximum WAM and WAFM that a fund may operate, for which the proposals from the SEC on these two aspects should be sufficient.

Portfolio liquidity

Liquidity of securities

We note the proposal to prohibit money market funds from acquiring securities unless at the point of acquisition they can be sold or disposed of in the ordinary course of business within seven days at approximately their amortised value. This is generally consistent with European legislation governing the conduct of UCITS funds.

The Eligible Assets Directive 2007/16/EC limits investment to money market instruments which are defined as liquid instruments with a value that can be accurately determined at any time (which will include but is not limited to treasury and local authority bills, certificates of deposit, commercial paper and banker's acceptances). The guidance associated with this legislation, issued by the Committee of European Securities Regulators, identifies that the liquidity of a money market instrument should be determined having regard to whether the instrument may be repurchased, redeemed or sold within a short period (e.g. seven business days) and at limited cost. The alignment between the proposals and that already in place within Europe are welcomed and should aid global consistency of money market funds.

Minimum liquidity of portfolio

We consider it a necessity to limit the exposure of a money market fund to liquidity risk. We therefore broadly welcome the proposed requirements relating to portfolio liquidity. We plan to impose an obligation on our members to implement a formal liquidity policy, which must be annually reviewed and approved by the fund's Board of directors.

As part of this liquidity policy, we plan to implement minimum amounts of overnight and one week securities which must be held by the fund. In the event that levels fall below these minima, the fund must make best efforts to comply as soon as practicable thereafter having regard to market conditions and the best interests of investors. Whilst this does not oblige funds to sell securities to comply with the minimums, it is intended to require funds to reshape portfolios as and when market conditions are amenable and only if in the best interests of investors. An ongoing obligation should enable a fund to cope with a redemption based liquidity strain over a longer duration than a requirement solely at the point of purchase of new securities, as is the case for the SEC's proposed rule.

Minimum daily and weekly liquidity requirement

As stated above, we agree with the need to implement minimum amounts of overnight and one week securities in order to provide natural liquidity to facilitate redemption requests without recourse to selling securities in illiquid markets.

However, we would not wish for funds to be required to hold unduly burdensome amounts of overnight and/or one week securities which could potentially limit the ability of the funds to function.

Stress Testing

We welcome the proposal for a stress testing requirement to be included within Rule 2a-7. We supported the implemented of a regulatory requirement within Ireland, and as you are aware, issued guidance to our membership on the application of the requirement following its introduction.

Diversification

For liquidity, we have similarly considered the impact of sectoral concentrations within underlying portfolios. We equally recognise that the management of such concentration risk is a necessity for any money market fund manager. However, given the potential complexities of defining sectors which were sufficiently dynamic to reflect changing investor behaviours, we consider it most prudent to impose a general obligation on our members to manager all concentration within the portfolio rather than prescribe specific diversification requirements for sectoral investment. This is being implemented through a formal obligation to implement a liquidity policy which must consider any concentration risks arising within the fund. Such a policy should therefore address not only sectoral concentrations but also any concentrations amongst the investor base.

An obligation to implement a liquidity policy which is reviewed and approved by the fund's Board of directors at least annually will necessitate that the policy adequately reflects the nuances of the portfolio's composition. We consider this the most appropriate means of managing concentration risk rather than attempting to define sectors.

Disclosure of Portfolio Information

Public website posting

As a concept, we are in agreement with the need to improve the disclosure of money market funds in order to provide investors with sufficient information on which to base their investment decisions.

The proposals acknowledge that disclosure of the shadow price could potentially introduce greater instability to money market funds. We agree with this statement. We believe that the provision of the shadow price would be precisely the information that would empower an investor to market time the fund at a close-to break the buck point, and at the expense of other investors. This could potentially lead to more frequent and larger redemption requests and is therefore more likely to result in pro-cyclical systemic shocks.

Based on precedents already established in Europe, we consider that there are other ways to mitigate the risks associated with a $1 share price (in particular, the risk that a significant shareholder might time redemptions to take advantage of price movements) without increasing systemic risk:

- dilution levy. The Prospectuses of most IMMFA funds give Directors the power to impose a 'dilution levy' on redemptions, if considered to be in the best interest of shareholders. A redemption by a concentrated shareholder which potentially worsens the position of remaining shareholders would most likely be deserving of a redemption levy. The levy would equalize the fund to the extent that the 'shadow price' fell as a consequence of the redemption by the concentrated shareholder, ensuring that remaining shareholders were left no worse than if the redemption had not occurred; and

- *in specie* redemptions. The Prospectuses of most IMMFA funds give the Directors the power to meet redemptions by way of an *in specie* redemption of assets within the fund (know in the US as a 'payment in kind'), if that redemption exceeds a given proportion of total fund assets (typically ten per cent), and provided that the action would not be materially prejudicial to the interests of the remaining shareholders. That power is intended to resolve precisely the risks that you have identified. During the recent crisis, this action was taken by Lehman Brothers following the suspension of redemptions in their Irish domiciled money market funds.

Reporting to the SEC

We note the intention for money market funds to provide additional reports to the SEC, and that this information would subsequently be made publicly available two weeks after filing with the Commission. The proposal also questions whether additional information should be supplied to the Commission and subsequently disclosed.

We appreciate the rationale for the submission of this information to the Commission. However, the proposals acknowledge that the disclosure of the shadow net asset value could introduce instability to the industry. We consider that the nature of some of the information being requested from the industry could equally destabilise the industry if this were publicly available.

The nature of the information being requested will allow the Commission to identify any potential systemic risk arising within the industry. If this information is then subsequently made available to the public – even with a two week delay – the public would be equally able to identify the potential for systemic risk. What was a potential could quickly become a reality, exacerbated through large redemption requests. This risk would quickly transcend global markets irrespective of the source of any risk. We therefore consider that any information from which it is able to identify systemic risk should be non-pubic. This would include as a minimum the shadow price of a money market fund and the price of its underlying holdings, and the details of any holdings of distressed assets.

<u>Fund Liquidation</u>

We note the proposal to introduce a new rule that would permit all money market funds to suspend redemptions upon breaking a buck. Whilst we consider this is a prudent action, we would highlight our experience in Europe in which a suspension occurred in advance of the loss of the stable net asset value. This action was taken in the best interests of investors and in order to prevent a capital loss arising for investors.

In September 2008, Lehman Brothers suspended all dealings in one Dublin based money market fund which incorporated three sub-funds in dollars, euros and sterling. This action was taken due to the redemption pressure the sub-funds faced as a result of the headline risk associated with the parent entity, and was not due to any issues associated with the underlying assets in the portfolios. This action was considered to be in the best interests of investors as it would not necessitate selling assets into an illiquid market. At the point of suspension, the sub-funds continued to trade at $1, €1 and £1 respectively.

Three days after the suspension, Lehman Brothers announced a temporary lifting of the suspension of redemptions to permit *in specie* redemption requests. A similar lifting was also effected in October. These actions were considered to be appropriate and in the best interests of investors. They also assisted in the orderly wind-down of the sub-funds, all of which were closed by May 2009 with shareholders having received investment without loss of value.

The fund remained suspended until the orderly wind-down had been completed. The suspension allowed the fund to enact this wind-down. If it had been lifted at any point, the fund would have been exposed to further (and likely greater) redemption pressure which could have resulted in a loss of the stable net asset value due to the wider lack of liquidity in the market.

On the basis of the action taken by Lehman Brothers in September 2008, we would suggest that funds should be capable of suspending redemptions prior to – or immediately following – a break the buck situation if this is in the best interests of all investors. The suspension allows a wind-down to be facilitated.

Floating net asset value

The proposals request comment on the plausibility of requiring money market funds to provide a floating net asset value. Here at IMMFA, we only represent the interests of those money market funds which provide a stable net asset value, facilitated through the use of amortised cost valuation. This method of valuation is more appropriate for our Members' funds - as it more closely reflects the 'hold to maturity' nature of the underlying portfolios and is consistent with their primary investment priorities of capital preservation and liquidity provision, rather than the secondary aim of yield generation. This approach has always formed an important part of our Code of Practice - along with suitable constraints and escalation points to protect the interests of investors.

One of the arguments put forward in favour of the floating net asset value approach is that it will more accurately reflect the underlying value of the assets. However, as has been seen, the market value of assets in turmoil conditions can often represent a 'fire-sale' price rather than 'fair value'. The financial services industry is broadly querying the suitability of mark-to-market pricing on this basis. As such, it is questionable whether the use of this price is in the best interests of investors in our Members' funds – especially if the intention is to hold the majority of assets until maturity, when they will normally redeem at par value.

IMMFA believes that stable net asset value funds which are appropriately managed from a credit and liquidity perspective are sustainable and are in the best interests of investors whose primary goal is stability of principal.

Our Members remain committed to providing stable net asset value money market funds. Further, investors continue to request the ability to invest in a fund which provides a stable net asset value. Based upon the appetite of both fund managers and investors, these stable net asset value money market funds in Europe should continue to attract significant investment.