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SEC Proposes Changes To Money Market Funds

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On June 5, 2013, the Securities and Exchange Commission (the “SEC”) proposed long-anticipated amendments to Rule 2a-7 and other rules under the Investment Company Act of 1940 (the “1940 Act”) and amendments to related disclosure requirements (the “Proposal”).¹ These recommendations are the result of a lengthy process of consideration of the responses to concerns triggered by the 2007-2008 financial crisis over the susceptibility of money market funds to significant shareholder redemptions and related risks to the U.S. financial system.

The Proposal, which totals nearly 700 pages, primarily consists of two approaches for restructuring money market fund operations. The first approach would require any money market fund (other than a government money market fund or a retail money market fund) to “float” its net asset value (“NAV”) per share. The second approach would require a money market fund (other than



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a government money market fund) whose weekly liquid assets fall below 15 percent of its total assets to impose a liquidity fee of 2 percent on all redemptions (unless the fund’s board determines that the liquidity fee is not in the best interests of the fund). Under this second approach, once a money market fund crosses the 15 percent threshold, the fund’s board in its discretion could temporarily suspend redemptions (or “gate” the fund) for up to 30 days if the board determines that doing so is in the best interests of the fund. The SEC could adopt one of the two approaches separately or could combine the two approaches.

Under either approach, however, the Proposal would eliminate the use of the amortized cost method of valuation for money market funds, a method that has been relied upon by money market funds since the 1970s.² The SEC also proposed enhanced diversification requirements and stress testing, disclosure enhancements, changes to related forms, the addition of a new form, and certain clarifying amendments.

The Proposal is discussed in more detail below, including discussion of the floating NAV and liquidity fees and redemption gate approaches and other proposed changes to money market fund regulation.

Background

As an initial attempt to enhance the resilience of money market funds, the SEC amended Rule 2a-7 in 2010 by improving liquidity, reducing interest rate and credit risks, increasing reporting, and adding requirements to “stress-test” portfolios. In 2011, the SEC then held a roundtable on further reforms, and in 2012, the Financial Stability Oversight Council (“FSOC”) separately recommended additional changes to money market fund operations. In 2012, at the request of certain Commissioners, the SEC’s Division of Risk, Strategy, and Financial Innovation issued a study (the “RSFI Study”), which analyzed the effects to date of the 2010 amendments, including the likelihood that a money market fund with a maximum permitted weighted average maturity would “break the buck,” and how money market funds would have performed during September 2008 had the 2010 amendments been in place. The RSFI Study found that, among other things, the expected probability of a money market fund breaking the buck was lower as a result of the additional liquidity required by the 2010 amendments, and the 2010 amendments would have been unlikely to prevent a money market fund from breaking the buck when faced with large credit losses, as occurred in 2008.

Based on these findings, the SEC concluded that while the 2010 amendments were an important step in enabling money market funds to withstand heavy redemptions when there are no portfolio losses, they are insufficient to address the incentives to redeem in the face of portfolio losses or when short-term credit markets come under stress. Accordingly, the Commission voted unanimously to propose changes to money market funds that aim,

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in the SEC's view, to reduce incentives for investors to redeem money market fund shares during times of market stress and limit contagion associated with potential investor runs, and to increase the transparency of risks associated with investing in a money market fund, while preserving, as much as possible, the benefits of a money market fund.

Approach One: Floating Net Asset Value

The SEC's first proposed approach would require a money market fund (other than a government or a retail money market fund) to "float" its net asset value instead of using a stable \$1.00 per share price. The Proposal would amend Rule 2a-7 by removing certain exemptions that currently permit a money market fund to maintain a stable price through amortized cost valuation and penny-rounding portfolio pricing. Under the Proposal, a money market fund's NAV would be based on current market values, so that, according to the SEC, "incentives to redeem early to take advantage of transacting at a stable value are ameliorated."³ The SEC stated that a money market fund's use of a stable share price is one of several features of a money market fund that creates an incentive for investors to redeem shares heavily in times of fund and market stress.⁴ The floating NAV approach is intended to reduce the incentive for investors to redeem shares in times of fund and market stress and also aims to improve money market fund pricing transparency by increasing investor awareness of money market fund risks.

Money Market Fund Pricing

Under this approach, a money market fund (other than a government or a retail money market fund) would be required to round its NAV to the fourth decimal place, also known as "basis point" rounding.⁵ This approach differs from current Rule 2a-7, under which a money market fund may use the penny-rounding pricing method, subject to certain conditions, which provides that the fund's NAV is rounded to the nearest one percent. This proposed new pricing method for a money market fund is intended to increase the observed sensitivity of a fund's NAV to changes in the market values of the fund's portfolio securities and enhance the potential advantages of having a floating NAV.

Exemption for Government Money Market Funds

Under this approach, a government money market fund would be able to continue to provide a stable NAV.⁶ A government money market fund would be permitted to continue to use the penny-rounding method of pricing, but would no longer be permitted to use the amortized cost method of valuation for securities maturing in more than 60 days. Citing the RSFI Study, the SEC stated that it does not appear that a government money market fund is as susceptible to the risks of mass investor redemptions as other money market funds, and requiring a government money market fund to float its NAV may be unnecessary to achieve the policy goals of the Proposal.⁷ A government money market fund would be defined as a money market fund in which 80 percent or more of its total assets are invested in cash, government securities, and/or repurchase agreements that are fully collateralized.⁸ Securities issued by state or local municipal governments would not fall under the definition of a government security, and therefore a municipal money market fund would not be eligible for this exemption from the floating NAV requirement. The SEC noted, however, that most municipal (or tax-exempt) funds would likely be covered by the retail money market fund exemption, as discussed below.⁹

Exemption for Retail Money Market Funds

Under this approach, a retail money market fund would be able to continue to provide a stable NAV, using the penny-rounding method of pricing, but not the amortized cost method of valuation for securities maturing in more than 60 days. A retail money market fund would be defined as a fund that limits the redemptions of each shareholder of record to no more than \$1,000,000 per business day.¹⁰ The SEC noted that the Proposal would permit a retail money market fund to limit daily redemptions. The SEC selected the daily redemption limit as its means to differentiate between a retail and an institutional fund due, in the SEC's view, to its relative ease of implementation, lack of dependence on a fund's ability to monitor certain shareholder characteristics, potential to reduce the risk that a retail fund would experience heavier redemption requests than it could effectively manage, and the incentive it provides institutions

to self-select as an institutional floating money market fund.¹¹

The SEC recognized that the operational challenges of implementing the retail exemption are "numerous and complex."¹² Many money market funds are owned by both retail and institutional investors, often through separate classes. A money market fund currently serving retail and institutional customers would need to reorganize in order to rely on the retail exemption, offering separate money market funds to retail and institutional investors. Furthermore, applying the daily redemption limit of \$1,000,000 may pose difficulties for a money market fund whose shareholders hold its shares through an omnibus account. Proposed Rule 2a-7 provides that a money market fund may permit an omnibus account holder to redeem more than \$1,000,000 on any one business day so long as the money market fund has policies and procedures reasonably designed to ensure that the omnibus account holder does not permit any beneficial owner of the money market fund's shares, directly or indirectly, to redeem more than \$1,000,000 on any one business day.¹³ Intermediaries with omnibus accounts would need to provide transparency regarding underlying shareholders showing that each redemption by a beneficial owner was below the limit or the fund could arrange with the intermediary to carry out the fund's policies to impose the redemption limitation. If a money market fund could not reasonably conclude that such policies are enforced by the intermediaries, then the money market fund must apply the redemption limit at the aggregate omnibus account-holder level.

Another potential challenge identified by the SEC concerns shareholders owning shares of a money market fund through multiple accounts, either directly with the fund or through an intermediary. If a shareholder is the shareholder of record for multiple accounts, the fund would need to aggregate redemption requests from all accounts of the shareholder of record and impose the daily redemption limit on the shareholder's total redemptions. If an account is held through an intermediary, the fund would not be able to identify that a shareholder has an account with the fund and redemptions of that account would not be aggregated with an account held directly with the fund.¹⁴ The Proposal also acknowl-

edges that a money market fund would incur additional costs associated with tracking gains and losses, providing cost-basis reporting, and monitoring for potential wash-sale transactions.

Approach Two: Liquidity Fees And Redemption Gate

As a second approach, the SEC proposed to:

- require money market funds to institute a liquidity fee in certain circumstances, and
- provide money market funds with the ability to impose a temporary suspension of redemptions (a “gate”) for a limited period of time.

Under this approach, a money market fund would continue to use a stable share price through the penny-rounding method of pricing, but would no longer use the amortized cost method of valuation for securities maturing in more than 60 days.¹⁵

Liquidity Fee

Under this approach, if, at the end of a business day, a money market fund has invested less than 15 percent of its total assets in weekly liquid assets,¹⁶ the fund *must* institute a liquidity fee in the amount of 2 percent of the value of the shares redeemed, effective as of the beginning of the next business day, *unless* the fund’s board of directors, including a majority of the directors who are not interested persons of the fund, determines that imposing the liquidity fee is not in the best interests of the fund. The fund’s board of directors may also vary the level of the liquidity fee if it determines that a lower fee is in the best interests of the fund. Once imposed, the liquidity fee will remain in effect until the money market fund’s board of directors determines that imposing the fee is not in the best interests of the fund. If, however, the money market fund has invested 30 percent or more of its total assets in weekly liquid assets, the fund must cease charging the liquidity fee, effective as of the beginning of the next business day.¹⁷

For beneficial owners holding money market fund shares through omnibus accounts, the liquidity fee would be applied in accordance with contractual arrangements between the fund or its transfer agent and the financial intermediary. The SEC expects that some money market fund sponsors will review their contractual arrangements to determine whether liquidity fees will be appropri-

ately applied to the beneficial owners of money market fund shares.¹⁸

A government money market fund would be exempt from any liquidity fee requirement. These money market funds, however, are permitted to voluntarily opt into the requirement, provided that the fund complies with all of the provisions in the proposed Rule 2a-7 and the liquidity fee or gate is appropriately disclosed in the fund’s prospectus.¹⁹ A retail money market fund would not be exempt from the liquidity fee requirement.

Redemption Gate

If, at the end of a business day, a money market fund has invested less than 15 percent of its total assets in weekly liquid assets, the fund’s board of directors, including a majority of the directors who are not interested persons of the fund, may determine to suspend the right of redemption temporarily. The suspension would remain in effect until the earlier of (i) the board (including a majority of the directors who are not interested persons) determining to restore the right of redemption; (ii) 30 calendar days elapsing; or (iii) the money market fund investing 30 percent or more of its total assets in weekly liquid assets.²⁰ The money market fund may not suspend the right of redemption for more than 30 days in any 90-day period. Unlike the liquidity fee, the gate is purely discretionary as determined by the fund’s board.²¹

A Combined Approach

The SEC acknowledges the potential shortcomings of each of the two approaches. As the SEC explained, while a floating NAV for some money market funds, for instance, helps to address the problem of the incentives for shareholders to redeem during market stress and provides more transparency as to the risks of investing in a money market fund, the floating NAV does not address incentives for investors to redeem during more severe times of stress; this risk is meant to be addressed through liquidity fees and gates. The liquidity fees and gates approach, however, does not address the risk of investors redeeming shares at a stable NAV when the fund’s shadow price actually falls below a dollar. As a result, the SEC seeks comments relating to combinations of some or all aspects of the two approaches, as well as the possibility of adopting both approaches and requiring money market funds to choose to comply with one or the

other.²²

Enhanced Diversification Requirements

The SEC proposed amendments to Rule 2a-7 relating to diversification out of concern that the current diversification limitations do not sufficiently limit money market fund exposure.²³ As a result, the proposed amendments would provide the following diversification enhancements:

1. *Aggregate Affiliate Exposure.* A money market fund would be required to aggregate its exposure to certain entities that are affiliated with each other as a single issuer for purposes of applying the 5 percent issuer diversification requirement under Rule 2a-7.

2. *Asset-Backed Securities.* Rule 2a-7 would be amended to require a money market fund, subject to the exception below, to treat the sponsor of a special purpose entity issuing asset-backed securities (“ABS”) as a guarantor of the ABS subject to the diversification limits of Rule 2a-7 applicable to guarantors and demand feature providers.²⁴ Thus, a money market fund could not purchase additional ABS, if immediately after its investment the fund would have exposure of more than 10 percent of its assets in securities issued by or subject to demand feature or guarantees from an ABS sponsor. If a money market fund’s board determines, however, that the fund does not rely on the sponsor’s guarantee or the ABS demand feature, then the fund would be excepted from this limitation.

3. *Removal of 25 Percent Basket.* Proposed amendments to Rule 2a-7 would eliminate the 25 percent basket, which permits up to 25 percent of the value of the securities in a fund’s portfolio to be subject to guarantees or demand features from a single institution. The amendments are designed to reduce the risk that a money market fund assumes when it relies heavily on a single guarantor or demand feature provider.

Enhanced Stress Testing

As part of the 2010 money market fund reforms, fund boards for the first time became required to adopt procedures for periodic stress testing of fund assets. The SEC has monitored the effectiveness of various procedures since that time and has determined through staff examination that additional enhancements to the procedures are warranted.²⁵ The SEC has pro-

posed that the following reforms²⁶ apply under either approach (except that floating NAV funds would not have to test against preserving a stable NAV).

1. *Floating NAV.* Each money market fund subject to a floating NAV would stress test its ability to maintain weekly liquid assets of at least 15 percent of total fund assets. A money market fund that is exempt from the floating NAV requirement would be required under the Proposal to stress test for its ability to (i) maintain weekly liquid assets of at least 15 percent of total fund assets and (ii) maintain a stable NAV.

2. *Liquidity Fees and Gates.* Similar to the floating NAV approach, under the second approach standing alone, a money market fund would be required to stress test its ability to (i) maintain weekly liquid assets of at least 15 percent of total fund assets and (ii) maintain a stable NAV.

Amendments To Disclosure Requirements

The SEC also proposed amendments to Rule 2a-7 and Form N-1A that would provide greater transparency to allow investors to more fully understand the risk of money market fund investing, while also allowing the SEC to obtain additional information to administer regulatory programs. These amendments, if adopted, would require the following:

1. *Sponsor and/or Affiliate Support.* A money market fund would provide, in its statement of additional information, information about any type of financial support²⁷ provided by the fund's sponsor or an affiliated person of the fund within the last 10 years. The fund would describe the nature, amount, and date of the support provided, the security supported and its value on the date the support was initiated (if applicable), the reason for the support, the term of the support (if applicable), and any contractual restrictions relating to the support.²⁸ A money market fund would also be required for one year to "post prominently on its website" substantially the same information, on the same business day, that the fund is required to report on Form N-CR regarding financial support to the fund.²⁹

2. *Website Disclosure of Daily and Weekly Liquidity Levels and Current NAV Per Share.* The Proposal would require a money market fund to "disclose prominently" on its website the percentage of

fund assets invested in daily and weekly liquid assets, and net inflows and outflows as of the end of the previous business day. Additionally, the Proposal would require a money market fund to "disclose prominently" on its website the fund's current NAV per share, rounded to the fourth decimal place in the case of a fund with 1.0000 share prices, or an equivalent level of accuracy for a fund with different share price (e.g., 100.00), at the end of each business day. Each money market fund would also be required to maintain a schedule, chart, graph, or other depiction on its website showing historical information about investments in daily and weekly liquid assets, historical NAV information, along with fund inflows and outflows, for a rolling six-month period at the end of each business day.³⁰

3. *Advertisement and Sales Material Disclosure.* Proposed amendments to Rule 2a-7 would require specific bulleted disclosure in any advertisement or sales material (including websites) of particular risks associated with investing in a floating NAV money market fund or with investing in a money market fund that may impose liquidity fees or redemption restrictions.³¹ Substantially similar bulleted disclosure would be required in any summary prospectus or summary section of the fund's statutory prospectus. Additionally, proposed amendments to Rule 482 and Form N-1A would require a fund that relies on the government money market fund exemption from the liquidity fees or gate requirement to include specific bulleted disclosure on the fund's advertisements and sales materials, and in the fund's statutory prospectus (including the summary prospectus) pertaining to the risks of investing in money market funds generally.

4. *Harmonization of Rule 2a-7 and Form N-MFP.* The Proposal would change, among other things, the categories of portfolio investments, portfolio maturity dates used to calculate dollar-weighted average life maturity, and the market-based value of portfolio securities. The amended rules would also remove the current 60-day delay in public availability of Form N-MFP information. As a result, the amendments propose that the market-based value of a fund be disclosed on the fund's website at the same time this information becomes available on Form N-MFP.

New Form N-CR

New Form N-CR³² would require a money market fund to report to the SEC certain events one business day after the event occurs. The report would be made public on EDGAR immediately upon filing. Under either proposed approach, Form N-CR would require disclosure of: (1) portfolio security default or insolvency; (2) all instances of sponsor financial support; (3) instances of a significant deviation in a money market fund's share price below its intended stable NAV;³³ and (4) a money market fund reaching the threshold triggering board consideration of a liquidity fee or redemption gate and the lifting of the fee or the resumption of the redemption of fund shares.

Amendments To Form N-MFP Reporting Requirements

The SEC proposed to amend Form N-MFP, which is used to report money market monthly portfolio holdings and certain other information. Each money market fund must currently file Form N-MFP within five business days after the end of each month, but the information is only made publicly available 60 days after the end of the month for which it is filed. The amendment would remove the 60-day delay in public availability (i.e., Form N-MFP would be publicly available immediately upon filing).

Under both the floating NAV and the liquidity fees and redemption gate approach, the SEC has proposed to adopt the following amendments:

1. *Portfolio Securities Value.* Items that reference "amortized cost" would be replaced with the requirement for a money market fund to disclose the "value" of its portfolio securities. As a result, there would be no shadow price to disclose, and this disclosure item would be eliminated.

2. *Weekly Reporting of NAV.* While a money market fund would continue to file reports monthly, certain limited information in those reports, such as NAV per share, would be reported on a weekly basis.

3. *New Reporting Requirements.* A money market fund would be required to disclose the following new information with respect to each holding: security identifiers; fair value hierarchy category (i.e., level 1, level 2 or level 3); purchase date; price and yield at purchase date; principal amount; yield; dollar-weighted

average portfolio maturity; dollar-weighted average life maturity ("WAL"); and final maturity. A money market fund would also have to disclose the amount of cash it holds, the fund's daily and weekly liquid assets, whether each security is considered a daily or weekly liquid asset, and whether any person paid for or waived all or part of the fund's operating expenses of management fees. A money market fund would be required to disclose the total percentage of shares outstanding held by the 20 largest shareholders of record. Additionally, a money market fund would also be required to disclose additional information about securities in the fund, such as the period remaining until the principal amount of a security may be recovered through a demand feature and whether a security demand feature is conditional.

Amendments To Form PF Reporting Requirements

The SEC also proposed to amend Form PF, which is the form used by certain investment advisers to private funds to report information regarding the private fund(s) they manage, including "liquidity funds," which are private funds that seek to maintain a stable NAV akin to money market funds registered under the 1940 Act.³⁴ The proposed amendments would apply to "large" liquidity fund advisers, which are SEC-registered investment advisers that advise at least one liquidity fund and manage, collectively with their related persons, at least \$1 billion in combined liquidity fund and money market fund assets. These amendments will help FSOC monitor and access systemic risk in financial markets. The proposed amendments would require, for each liquidity fund it manages, a large liquidity fund adviser to provide certain information (e.g., category of investment, credit rating, maturity date and value) with respect to each portfolio security for each month of the reporting period.³⁵

Clarifying Amendments

The SEC proposed a number of amendments to help clarify the operations of certain provisions since the 2010 amendments.³⁶

1. *Daily and Weekly Liquid Assets.* First, the amendments propose that a money market fund cannot use the maturity-shortening provisions in current paragraph (d) of Rule 2a-7 regarding

interest rate readjustments when determining whether a security satisfies the maturity requirements of a daily liquid asset or a weekly liquid asset.³⁷ Second, an agency discount note with a remaining maturity of 60 days or less qualifies as a weekly liquid asset only if the note is issued without an obligation to pay interest on the principal amount. In addition, the definitions of daily and weekly liquid assets would include amounts receivable that are due unconditionally within one business day or five business days, respectively, on pending sales of portfolio securities.³⁸

2. *Demand Feature.* The SEC proposed to amend the definition of demand feature in Rule 2a-7 to mean a feature permitting the holder of a security to sell the security at an exercise price equal to the approximate amortized cost of the security plus accrued interest, if any, at the time of exercise, paid within 397 calendar days of exercise.³⁹ The proposed amendment would eliminate the requirement that a demand feature be exercisable at any time on no more than 30 calendar days' notice.

3. *Short-Term Floating Rate Securities.* The SEC proposed that for purposes of determining the WAL, a short-term floating rate security shall be deemed to have a maturity equal to the period remaining until the principal amount can be recovered through demand.

4. *Second-Tier Securities.* The 2010 amendments to Rule 2a-7 limited money market funds to acquire second-tier securities with remaining maturities of 45 days or less. The proposed amendments attempt to clarify this limitation, explaining that the 45-day limit applicable to second-tier securities must be determined without reference to the maturity-shortening provisions in Rule 2a-7 for interest rate readjustments.

Comments And Compliance Dates

The SEC proposed a compliance date of two years after the effective date of the amended rules for the proposed floating NAV approach, one year for the liquidity fee and redemption gate approach, and nine months for the other proposed amendments not specifically related to the two approaches. Comments are due September 17, 2013, 90 days after the Proposal was published in the Federal Register.

1 *Money Market Fund Reform; Amendments to Form PF*, Investment Company Act Release No. 30,551 (June 5, 2013) ("Proposing Release"), available at <http://www.sec.gov/rules/proposed/2013/33-9408.pdf>. References to amendments to Rule 2a-7 under the floating NAV approach will be labeled "Proposed (Floating NAV) Rule" and references under the liquidity fees and gate approach will be labeled "Proposed (Fees & Gates) Rule."

2 Under current Rule 2a-7, a money market fund calculates its NAV using the amortized cost method, subject to certain conditions. Under the Proposal, a money market fund generally would only be able to use amortized cost valuation if the fund's board of directors determines, in good faith, that the fair value of debt securities with remaining maturities of 60 days or less is its amortized cost, unless the particular circumstances warrant otherwise.

3 Proposing Release at 52.

4 The SEC acknowledged that incentives other than those created by a money market fund's stable share price exist for money market fund shareholders to redeem in times of stress, including avoidance of loss and the tendency of investors to engage in flights to quality, liquidity, and transparency. Proposing Release at 52, n.140.

5 Proposed (Floating NAV) Rule 2a-7(c)(1). The proposed rule provides for a relatively long compliance date of two years to provide enough time for money market funds to update their systems to account for a floating NAV and also to allow shareholders enough time to understand the implications of a change from a stable NAV to a floating NAV. See Proposing Release at 49-50, 62-63.

6 Proposed (Floating NAV) Rule 2a-7(c)(2)-(3).

7 Proposing Release at 66-67.

8 Proposed (Floating NAV) Rule 2a-7(c)(2). A government security is defined as a security issued or guaranteed as to principal or interest by the United States, or by a person controlled or supervised by and acting as an instrumentality of the government of the United States pursuant to authority granted by the Congress of the United States; or any certificate of deposit for any of the foregoing. Rule 2(a)(16) of the 1940 Act. Securities issued by government-sponsored entities, such as the Federal Home Loan Banks, fall under this definition.

9 Proposing Release at 68-69.

10 See Proposed (Floating NAV) Rule 2a-7(c)(3)(iii), which states that "[a] money market fund is exempt from the requirements of sections 18(f)(1) and 22(e) of the [1940 Act] to the extent necessary to permit the money market fund to limit redemptions in excess of \$1,000,000 of redeemable securities on any one business day as provided in paragraphs (c)(3)(i) and (ii) of this section."

11 Proposing Release at 80.

12 Proposing Release at 77.

13 An "omnibus account holder" is defined as a broker, dealer, bank, or other person that holds securities issued by the money market fund in nominee name. Proposed (Floating NAV) Rule 2a-7(c)(3)(ii).

14 Proposing Release at 92.

15 Proposed (Fees & Gates) Rule 2a-7(c).

16 "Weekly liquid assets" is defined as cash, direct obligations of the U.S. government, certain other government securities with remaining maturities of 60 days or less, securities that will mature or are subject to a demand feature that is exercisable and payable within five business days, and amounts receivable and due unconditionally within five business days. See Proposed Rule (Fees & Gates) 2a-7(a)(31).

17 Proposed (Fees & Gates) Rule 2a-7(c)(2)(i)(A)-(B).

18 See Proposing Release at 191.

19 It should also be noted that a government money

market fund or a retail money market fund would be able to suspend redemptions in accordance with Rule 22e-3 under the 1940 Act if the fund's board of directors, including a majority of directors who are not interested persons of the fund, determined that the fund is about to "break the buck."

20 Proposed (Fees & Gates) Rule 2a-7(c)(2)(ii).

21 Proposed (Fees & Gates) Rule 2a-7(c)(2)(iii). The SEC believes that liquidity fees would require redeeming shareholders to bear at least some of the liquidity costs of their redemption and might lessen both the frequency and effect of shareholder redemptions during times of fund and market stress. The SEC also believes that gates might stop redemptions long enough to: (i) allow fund managers time to assess the appropriate strategy to meet redemptions; (ii) allow liquidity buffers to grow organically as securities mature, and (iii) allow shareholders to assess the level of liquidity in the fund and for any shareholder panic to subside. Proposing Release at 159-60.

22 See Proposing Release at 235-45.

23 As explained in the Proposing Release: "Generally, money market funds must limit their investments in the securities of any one issuer of a first tier security (other than government securities) to no more than 5% of fund assets. They must also generally limit their investments in securities subject to a demand feature or a guarantee to no more than 10% of fund assets from any one provider, except that the rule provides a so-called 'twenty-five percent basket,' under which as much as 25% of the value of securities held in a fund's portfolio may be subject to guarantees or demand features from a single institution." Proposing Release at 403.

24 Proposed (Floating NAV and Fees & Gates) Rule 2a-7(a)(16)(ii).

25 "We have observed disparities in the quality and comprehensiveness of stress tests, the types of hypothetical circumstances tested, and the effectiveness of materials produced by the fund's manager to explain the stress testing results to the board." Proposing Release at 470.

26 See Proposed (Floating NAV) Rule 2a-7(g)(7)(i);

Proposed (Fees & Gates) Rule 2a-7(g)(9)(i).

27 The term "financial support" would include, but not be limited to: (i) any capital contribution, (ii) purchase of a security from the fund in reliance on Rule 17a-9, (iii) purchase of any defaulted or devalued security at par, (iv) purchase of fund shares, (v) execution of a letter of credit or letter of indemnity, (vi) capital support agreement (whether or not the fund ultimately received support), (vii) performance guarantee, or (viii) any other similar action to increase the value of the fund's portfolio or otherwise support the fund during times of stress. Instruction 1 to Proposed (Floating NAV) Item 16(g) of Form N-1A; Instruction 2 to Proposed (Fees & Gates) Item 16(g)(2) of Form N-1A. The proposed instructions also state that if the fund has participated in a merger with another investment company during the previous 10 years, the fund must provide the required disclosure with respect to the other investment company. *Id.*

28 Proposed (Floating NAV) Item 16(g) of Form N-1A; Proposed (Fees & Gates) Item 16(g)(2) of Form N-1A.

29 See Proposed (Floating NAV) Rule 2a-7(h)(10)(v); Proposed (Fees & Gates) Rule 2a-7(h)(10)(v); Proposed (Floating NAV) Form N-CR Part C; Proposed (Fees & Gates) Form N-CR Part C.

30 Proposed (Floating NAV) Rule 2a-7(h)(10)(ii)-(iii); Proposed (Fees & Gates) Rule 2a-7(h)(10)(ii)-(iii).

31 Proposing Release at 209; 137. Proposed disclosure requirements are amendments to Rule 482 under the Securities Act of 1933.

32 Proposed Rule 30b1-8.

33 The SEC staff explained that a "deviation of 1/4 of 1 percent" would be sufficiently significant to require disclosure. See Proposing Release at 358.

34 For purposes of Form PF, a "liquidity fund" is any private fund that seeks to generate income by investing in a portfolio of short-term obligations in order to maintain a stable net asset value per unit or minimize principal volatility for investors. See Glossary of Terms to Form PF.

35 As Commissioner Aguilar explained, "the proposed amendments address the concern that registered

money market fund assets could migrate to an opaque and unregulated market. This issue is now discussed at length in the release, and the staff has designed a surgical amendment to Form PF to provide transparency on the possible outflows of monies to unregulated private funds that essentially operate like registered money market funds." Commissioner Luis A. Aguilar, Striving to Restructure Money Market Funds to Address Potential Systemic Risk (June 5, 2013), available at <http://www.sec.gov/news/speech/2013/spch060513laa.htm>.

36 Proposed (Floating NAV and Fees & Gates) Rule 2a-7(a)(9), (i)(4), and (d)(2)(ii).

37 Rule 2a-7(a)(8) currently defines "daily liquid assets" to include: (i) cash, (ii) direct obligations of the U.S. government, or (iii) securities that will mature or are subject to a demand feature that is exercisable and payable within one business day. Rule 2a-7(a)(32) currently defines "weekly liquid assets" to include: (i) cash; (ii) direct obligations of the U.S. government; (iii) securities that will mature or are subject to a demand feature that is exercisable and payable within five business days; or (iv) Government securities (as defined in section 2(a)(16) of the 1940 Act) that are issued by a person controlled or supervised by and acting as an instrumentality of the U.S. government that are issued at a discount to the principal amount to be repaid at maturity and have a remaining maturity date of 60 days or less.

38 Proposed (Floating NAV and Fees & Gates) Rule 2a-7(a)(8)(iv); Proposed (Floating NAV and Fees & Gates) Rule 2a-7(a)(31)(v).

39 A demand feature is currently defined to mean: (i) a feature permitting the holder of a security to sell the security at an exercise price equal to the approximate amortized cost of the security plus accrued interest, if any, at the time of exercise. A demand feature must be exercisable either: (a) at any time on no more than 30 calendar days' notice; or (b) at specified intervals not exceeding 397 calendar days and upon no more than 30 calendar days' notice; or (ii) a feature permitting the holder of an ABS unconditionally to receive principal and interest within 397 calendar days of making demand. See Rule 2a-7(a)(9).