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Via Electronic Mail

January 18, 2013

Financial Stability Oversight Council
Attention: Mr. Amias Gerety
1500 Pennsylvania Avenue, NW
Washington, DC 20220

Re: Proposed Recommendations Regarding Money Market Mutual Fund Reform
77 *Federal Register* 69455 (November 19, 2012)

Dear Mr. Gerety:

The American Bankers Association[1] (ABA) appreciates the opportunity to comment on the Financial Stability Oversight Council's (Council) proposed recommendations to the Securities and Exchange Commission (Commission) for additional regulation of money market mutual funds (MMF or fund). As stated in the release, the Council is conducting this exercise because of concerns that "the conduct and nature of the activities and practices of MMFs … leave them susceptible to destabilizing runs; the size, scale, and concentration of MMFs and the important role they play in the financial markets; and the interconnectedness between MMFs, the financial system and the broader economy … act as a channel for the transmission of risk and contagion and curtail the availability of liquidity and short-term credit."[2]

ABA's member institutions interact with MMFs in numerous ways. Over 1500 banks and trust companies use MMFs as a critical source for investments on behalf of their institutional and personal trust clients. Through these trust departments, as of December 31, 2011, banks have invested over $121 billion in MMFs on behalf of fiduciary accounts. In addition, many of our member institutions that offer corporate trust and securities processing services use MMFs to hold cash in connection with the issuance of both municipal and corporate bonds. Many of our members also use MMFs as investments for sweep accounts. Moreover, a significant number of our members sponsor and advise MMFs. Because of these many ways that banks and trust companies interact with MMFs, our members are keenly interested in the Council's proposed recommendations.

[1]ABA represents banks of all sizes and charters and is the voice for the nation's $14 trillion banking industry and its two million employees.
[2] Council Release, 77 *Fed. Reg*. 69455 at 69456.

Accordingly, ABA offers the following general comments on the Council's proposed recommendations:

- First, there is very strong support for retaining a stable net asset value (NAV) MMF, as this product is preferred by trust departments and corporate trustees as a timely and economical way to invest short-term customer cash.

- Second, any regulatory action must avoid creating the perception that investments in MMFs are equivalent to insured bank deposit accounts in terms of federal supervision or backing.

- Third, the Council should carefully consider the sufficiency of the SEC's 2010 reforms and give them adequate weight, as many bankers are convinced that further reforms are not needed.

In their examination of this issue, policymakers should carefully evaluate issues regarding the liquidity and credit quality of MMF portfolios, noting the differences between federal government instruments and those that are not backed by the full faith and credit of the federal government.

Background

Noting the 2008 run on the Reserve Primary Fund and other concerns about the effect of vulnerable MMFs on the financial system, the Council has proposed three alternative recommendations for amending MMF regulation. The Council has stated that these alternatives are not mutually exclusive, and any combination may be included in any formal recommendation to the Commission. The three alternatives are:

- Alternative One: Floating Net Asset Value. Require MMFs to have a floating NAV per share. Instead of being fixed at $1.00, the value of MMFs' shares would "float" and reflect the actual market value of the underlying portfolio holdings, consistent with the requirements that apply to other mutual funds.

- Alternative Two: Stable NAV with NAV Buffer and "Minimum Balance at Risk." Allow a stable NAV but require MMFs to have a capital buffer to absorb day-to-day fluctuations in the value of their investments. MMFs would also be required to delay for 30 days the redemption of 3% of a shareholder's highest account value in excess of $100,000 during the previous 30 days – a minimum balance at risk (MBR). If an MMF suffered losses that exceed the NAV buffer, losses would be borne first by the MBRs of shareholders who have recently redeemed. These requirements would not apply to Treasury MMFs.

- Alternative Three: Stable NAV with NAV Buffer and Other Measures. Allow a stable NAV, but require MMFs to have a capital buffer of 3 percent. In addition, require more stringent investment diversification requirements, increased minimum liquidity levels, and more robust disclosure requirements.

Discussion

1. Critical Importance of Stable NAV Funds

Some of the first MMFs established in the 1970s were created specifically for bank trust departments to provide administratively convenient, conservatively managed funds for the investment of trust account cash. Although MMFs are now popular with both retail and institutional investors alike, trust departments in banks of all sizes still make large investments in MMFs to meet their fiduciary obligation to make trust assets productive. An essential aspect that makes these funds so appealing to trustees and other investors is that they maintain a stable NAV. It is highly likely that bank trust departments will no longer invest in MMFs if they are not able to maintain a stable NAV.

A floating NAV would seriously undermine the MMF product as a popular and efficient way to invest short-term cash whether through trust departments or bank sweep accounts. A floating NAV would have significant tax consequences for banks investing on behalf of trust customers, because, unlike the case with a stable NAV, each purchase and sale transaction—which for many investors typically happens daily—would be a taxable event with consequent tax reporting obligations. For bank trust departments, their fiduciary duty to invest prudently may oblige them to find alternative investments for short-term cash that are stable (unlikely to experience market fluctuations), do not have the complicated tax reporting implications, and balance the interests of all beneficiaries. In particular, the reporting of gains and losses with a floating NAV would be operationally complex and very costly. Additional record keeping would be required to comply with the IRS's wash sales rules.[3] Banks do not currently have the systems necessary to undertake the recordkeeping that would be required for the frequency of transactions they make in MMFs. Indeed, such complexity and costs would make the product unattractive to bank trust departments. With respect to investment of municipal bond proceeds, several states specifically provide in their statutes governing permissible investments that investments are permitted only in MMFs with stable NAVs.

2. No Perception of Bank-Like Regulation

ABA members believe it imperative that, in regard to the regulation and supervision of MMFs, it be abundantly clear that accounts at MMFs are neither regulated nor guaranteed like deposit accounts in banks. A consistent theme of reform supporters has been that MMF investors believe that, because their shares can be redeemed at any time, their accounts are just like FDIC-insured bank accounts, despite clear disclosures to the contrary. It is critical that investors not be

[3] A wash sale occurs when you sell or trade stock or securities at a loss and within 30 days before or after the sale you:

1. Buy substantially identical stock or securities,
2. Acquire substantially identical stock or securities in a fully taxable trade,
3. Acquire a contract or option to buy substantially identical stock or securities, or
4. Acquire substantially identical stock for your individual retirement account (IRA) or Roth IRA.

misled into thinking that MMFs are regulated and supervised in a manner equivalent to banks or that MMF accounts are somehow supported by the federal government.

3. 2010 Reforms

The Association strongly believes that the Council should carefully weigh the adequacy of the Commission's 2010 amendments to Rule 2a-7 and assess fully their impact before imposing additional reforms. The 2010 amendments made substantial improvements to the quality, maturity, and liquidity of permissible MMF investments. Indeed, many of our members believe that the 2010 changes have adequately addressed the systemic concerns and other issues that gave rise to these reforms. These reforms were not minor:

- Such investments are limited to short-term securities rated in one of the top two short-term debt ratings by national recognized statistical rating organizations or, if unrated, are of comparable quality.[4]

- Investments in second-tier assets must be limited to no more than three percent of the fund's total assets, with no more than 0.5 percent in any one issuer.[5]

- The amendments further established stringent quality, diversification, and concentration limits, and mandated that the portfolio have a weighted average maturity of 60 days or less and a weighted average length of 120 days or less.[6]

- Illiquid assets in MMF portfolios must be limited to no more than five percent of the portfolio.[7]

- A taxable MMF must have at least ten percent of its assets in "daily liquid assets", i.e., assets that may be converted into cash in one business day. Thirty percent of MMF assets must be invested in "weekly liquid assets," i.e., assets that may be converted into cash within five business days. Finally, MMFs must "know their customers" and must hold sufficiently liquid assets to meet reasonably foreseeable shareholder redemptions.

4. Focus on Sufficiency of Liquidity and Credit Quality

ABA members believe that policymakers should in their deliberations give high priority to careful evaluation of the liquidity and credit quality of MMF portfolios. In this context, the differences between government MMFs and prime MMFs should be given appropriate weight. As stated above, ABA members strongly believe that the Council and the Commission should hold in abeyance any additional revisions to MMF regulation until the effectiveness of the 2010 reforms can be appropriately assessed.

[4] 17 CFR 270.2a-7(a)(10).
[5] 17 CFR 270-2a-7(c)(4)(i)(C).
[6] 17 CFR 270-2a-7(c)(2)(ii)-(iii).
[7] 17 CFR 270-2a-7(c)(5)(i).

5. Least Risk of Harm

As with medicine, the first rule of the regulatory practitioner is to do no harm. We believe that of the three options for additional regulation offered by the FSOC for public comment, the least risk of damaging the value of MMFs to investors—working from the foundation of a continued stable NAV regime— is to be found in regulatory consideration of reforms involving questions of capital to support potential losses, adequate liquidity, prudent diversification, and useful disclosures.

Conclusion

In conclusion, ABA strongly supports the continued use of a stable NAV. To eliminate this critical feature of MMFs would severely undermine the usefulness of the product to bank trust departments and corporate trustees, as well as to other bank investors. We further caution that underlying the regulatory and supervisory program for MMFs must be the exercise of meticulous care that there be no perception that MMFs are regulated in a manner comparable to bank deposit accounts or that they are backed by the federal government. Moreover, many ABA members remain unconvinced that the Commission's 2010 reforms have not resolved the systemic risk concerns, and in any event careful evaluation of the effectiveness of those reforms is warranted. In its deliberations, the Council should continue to give close attention to issues regarding the liquidity and asset quality of MMFs. In terms of further reforms, regulators should be careful to do no harm, beginning with preservation of a stable NAV regime, with attention to issues involving capital, liquidity, diversification, and disclosures presenting the least regulatory risk of damaging the value of MMFs for investors. If you have any questions about the foregoing, please do not hesitate to contact the undersigned.

Sincerely,

Cecelia A. Calaby
Senior Vice President