October 14, 2014

Mr. Kevin M. O'Neill
Deputy Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: Removal of Certain References to Credit Ratings and Amendments to the Issuer Diversification Requirement in the Money Market Fund Rule; File No. S7-07-11

Dear Mr. O'Neill:

Better Markets, Inc.[1] appreciates the opportunity to comment on the above-captioned re-proposed rule ("Re-Proposed Rule") of the Securities and Exchange Commission ("Commission" or "SEC"). The Re-Proposed Rule would remove references to credit ratings in Rule 2a-7 and Form N-MFP under the Investment Company Act ("ICA"), and it would substitute alternative standards of credit-worthiness to be used in place of credit ratings. The Commission has issued this element of the Re-Proposed Rule in accordance with the requirements of Section 939A of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the "Dodd-Frank Act"). In addition to removing credit rating references, the Re-proposed Rule would also eliminate an exclusion from the issuer diversification requirement for money market funds ("MMFs") in Rule 2a-7.[2]

The Re-Proposed Rule includes some important enhancements in the Commission's approach to the removal of credit rating references from its rules and to the portfolio diversification requirements of Rule 2a-7. We commend the SEC for moving in that direction. However, the Re-Proposed Rule also has weaknesses, and as detailed below, it should it be strengthened before final adoption.

INTRODUCTION

The removal of credit rating references from the SEC's rules is one important component of an overall set of reforms in the Dodd-Frank Act aimed at increasing the

---

1 Better Markets, Inc. is a nonprofit organization that promotes the public interest in the capital and commodity markets, including in particular the rulemaking process associated with the Dodd-Frank Act.

2 Securities and Exchange Commission, Money Market Fund Reform, Amendments to Form PF, 78 Fed. Reg. 36834 (June 19, 2013).

1825 K Street, NW, Suite 1080, Washington, DC 20006 TELEPHONE (1) 202.618-6464 FAX (1) 202.618.6465 WEBSITE bettermarkets.com

oversight and accountability of credit rating agencies while reducing reliance on credit ratings by market participants and regulators.

Although credit ratings can serve as important tools in our financial markets, they have also contributed to some of our most spectacular financial crises, including the collapse of Enron and the financial collapse and economic catastrophe that began in 2008. For years, the ratings industry has been fraught with conflicts of interest and anti-competitive behaviors.

One reason for the widespread and potentially harmful impact of credit ratings is their widespread use not only by market participants but also by regulatory agencies. Credit ratings became extremely important fixture in our capital markets, and were embedded in our securities laws and regulations as shorthand standards of credit-worthiness. As stated in the Dodd-Frank Act, "credit rating agencies are central to capital formation, investor confidence, and the efficient performance of the United States economy."[3]

The Dodd-Frank Act represents a Congressional mandate to institute regulatory measures that will finally and effectively address the decades-old challenges posed by credit ratings. The statute includes three fundamentally important reforms.[4]

First, it builds on the regulatory requirements that were implemented in the Credit Rating Agency Reform Act of 2006 by adding provisions relating to the registration process, corporate governance, compliance examinations, conflicts of interest, and public disclosure of ratings and methodologies.

Second, the Dodd-Frank Act seeks to substantially increase the accountability of NRSROs by increasing their exposure not only to enforcement remedies, such as monetary fines, but also, importantly, to liability in private actions.

Finally, in Section 939A, the Dodd-Frank Act seeks to reduce reliance upon credit ratings by requiring the Commission and other federal agencies to review their regulations, to remove any references to, or requirement of reliance on, credit ratings in those regulations, and to substitute appropriate standards of credit-worthiness in place of credit ratings.

The Congressional determination to reduce reliance on credit ratings is justified on several grounds. First, the reliability of credit ratings is inherently suspect. Regardless of how much regulation is brought to bear on the credit rating agencies, the quality of their ratings will remain subject to serious and legitimate questions due to the multiple material conflicts of interest they face.

Second, regulatory reliance upon credit ratings heightens systemic risk. Incorporating ratings into regulatory standards inevitably magnifies the impact of

[3] Dodd-Frank Act § 931(1).
[4] *See generally* Dodd-Frank Act §§ 931-939H.

erroneous or fraudulent ratings, since market participants subject to those regulatory standards rely on the same flawed ratings.

Finally, the use of credit ratings as regulatory benchmarks undermines thorough and independent credit analysis and due diligence by market participants. The incorporation of credit ratings into statutory and regulatory provisions is perceived as a governmental endorsement or seal of approval. This, in turn, induces an excessive reliance and a sense among market participants that independent credit analysis and due diligence are unnecessary. The Commission recognized all of these concerns prior to the enactment of the Dodd-Frank Act, and for that reason, in 2008, it began the process of removing references to credit ratings from its rules.[5]

In 2011, in accordance with Section 939A of the Dodd-Frank Act, the Commission issued its original proposed rule ("Original Proposed Rule"), addressing the removal of references to credit ratings from its MMF regulations and proposing alternative standards of creditworthiness.[6] Better Markets commented on that release.[7] However, after further consideration of the mandate in Section 939A of the Dodd-Frank Act; in light of the comments received on the Original Proposed Rule; and in light of the other major MMF reforms recently finalized,[8] the SEC decided to issue the Re-Proposed Rule.[9]

The Re-Proposed Rule is significant not only as a credit rating agency reform, but also as an MMF reform. The shadow banking industry in general, and MMFs specifically, have appropriately become the focus of increased scrutiny as potential sources of systemic risk in our financial system, particularly given their incendiary role in igniting and spreading the 2008 financial crash. The Re-Proposed Rule will have a direct impact on the types of securities in which MMFs may invest, which largely determines the ability of MMFs to remain stable in times of market stress, and to withstand runs should they occur. The Commission must strive to make every facet of its reforms governing MMFs and credit ratings as strong and clear as possible, and it should therefore strengthen the Re-Proposed Rule as set forth below.

SUMMARY OF COMMENTS

The Re-Proposed Rule would remove references to credit ratings in Rule 2a-7 under the ICA. The Re-Proposed Rules would additionally amend Form N-MFP, which currently requires credit ratings to be included in reports describing a fund's portfolio holdings. Finally, the Re-Proposed Rule would eliminate an exemption that potentially allows a fund

---

[5] *See* Securities and Exchange Commission, References to Ratings of Nationally Recognized Statistical Rating Organizations, Release No. IC-28327 (July 1, 2008), 73 Fed. Reg. 40124 (July 11, 2008).

[6] Securities and Exchange Commission, References to Credit Ratings in Certain Investment Company Act Rules and Forms, 76 Fed. Reg. 12896 (Mar. 9, 2011), *henceforth* "2011 Release."

[7] Better Markets Comment Letter, "References to Credit Ratings in Certain Investment Company Act Rules and Forms; File No. S7-07-11 (April, 25, 2011), http://www.sec.gov/comments/s7-07-11/s70711-12.pdf.

[8] Securities and Exchange Commission, Money Market Fund Reform; Amendments to Form PF, 79 Fed. Reg. 47736 (Aug. 14, 2014).

[9] Re-Proposed Release at 47987.

to ignore the five percent diversification requirement for issuers of portfolio securities if certain guarantee thresholds are met.

The Commission must address certain weaknesses in the Re-Proposed Rule in accordance with the following principals and recommendations:

- As we noted in our original comment letter,[10] replacing regulatory reliance on credit ratings without providing adequate alternatives will only undermine effective regulation of our capital markets and put investors at greater risk, not less. Therefore, the alternative standards of creditworthiness must be strong and, to prevent evasion by market participants, they must also be clear and concrete.
- The Re-Proposed Rule must establish mandatory factors that MMFs must consider in the credit analysis of securities, and in the ongoing monitoring of creditworthiness, and those factors must be more detailed and set forth in the text of the rule itself, rather than simply in the Federal Register release.
- The Re-Proposed Rule must retain the distinction between first and second tier securities, and must retain the three percent limit on second tier securities.
- The Re-Proposed Rule must explicitly address the extent to which MMFs may continue to rely on credit ratings.
- The Re-Proposed Rule must be amended to require disclosure in Form N-MFP of the factors and analysis funds considered in determining the creditworthiness of portfolio securities.
- The Re-Proposed Rule must limit exposure to any one guarantor to, at a maximum, five percent of the fund's total assets.

OVERVIEW OF THE RE-PROPOSED RULES

A. Re-Proposed Rule 2a-7: Permitted Portfolio Holdings.

Rule 2a-7 under the ICA is the core provision that limits the types of securities that an MMF may hold. It contains several references to credit ratings that the Original Proposed Rule and Re-Proposed Rule would remove and replace with alternative standards of credit-worthiness.

"Eligible" Securities. Under current Rule 2a-7, an MMF's portfolio investments are limited to securities that meet two tests: They must be determined by the fund's board of directors ("Board") to "present minimal credit risks," and they must be "eligible securities." To be an "eligible security," an investment must have received a rating from an NRSRO "in one of the two highest short-term rating categories." These eligible securities are divided into two categories: "first tier" and "second tier." First tier securities are defined to include

[10] Better Markets Comment Letter, *supra* n.7, at 2.

those that have received a rating from an NRSRO in the "highest short-term rating category." Second tier securities are defined as "any eligible security that is not a first tier security." The distinction is important, since, for example, a fund may only hold up to three percent of its portfolio in second tier securities.

The Original Proposed Rule would have replaced references to NRSRO ratings with a Board determination that first tier securities have "the highest capacity to meet its short-term financial obligations."[11] It would have left the definition of second tier securities intact, and it would have retained the requirement that the Board determine the securities "present minimal credit risks, which determination must be based on factors pertaining to credit quality and the issuer's ability to meet its short-term financial obligations."[12]

The Re-Proposed Rule redefines eligible securities as those where the Board has determined the "security's issuer has an exceptionally strong capacity to meet its short-term financial obligations."[13] The Re-Proposed Rule also **eliminates** the concepts of first and second tier securities.

Downgrades and Monitoring. Under current Rule 2a-7, when a security is downgraded by an NRSRO, the Board must promptly assess whether the security continues to present "minimal credit risk" and take appropriate action. The Re-Proposed Rule requires funds to adopt written procedures requiring advisers "to provide ongoing review of whether each security . . . continues to present minimal credit risks," based, at a minimum, on financial data.[14]

B. Re-Proposed Form N-MFP: Monthly Schedule of Portfolio Holdings of MMFs.

The Commission requires MMFs to complete Form N-MFP with detailed information about fund security holdings. Form N-MFP currently requires funds to provide credit ratings from each designated NRSRO. The Re-Proposed Rule would require identification of all NRSROs to which the fund adviser subscribes, as well as any NRSRO ratings the fund considered in its credit worthiness determinations.

C. Re-Proposed Exclusion from the Issuer Diversification Requirement.

Rule 2a-7 currently restricts any security by a single issuer to no more than five percent of a fund's total assets. However, the Rule provides an exclusion for securities subject to a third-party guarantee, provided that no more than ten percent of the securities is guaranteed by a single guarantor. The Re-Proposed Rule removes the exclusion and limits security holdings to five percent per issuer *and* ten percent per guarantor.

COMMENTS ON THE RE-PROPOSED RULES

---

11 2011 Release, at 914.

12 2011 Release, at 12898.

13 Securities and Exchange Commission, Removal of Certain References to Credit Ratings and Amendment to the Issuer Diversification Requirement in the Money Market Fund Rule, 79 Fed. Reg. 47986, 013 (Aug. 14, 2014), *henceforth* "Re-Proposed Release."

14 Re-Proposed Rule 2a-7(g)(3).

A. *The Re-Proposed Rule 2a-7 Must (1) Establish Mandatory Factors for the Credit Analysis of Eligible Securities; (2) Retain the Distinction Between First and Second Tier Securities; (3) Fully Eliminate Continued Reliance on Credit Ratings in that Determination; and (4) Strengthen Credit Risk Monitoring by Establishing Mandatory Factors.*

1. Consideration of Factors to Determine Eligible Securities Must Be Mandatory.

First and foremost, the Re-Proposed Rule must be more prescriptive and **require** advisers to consider the list of factors enumerated in the Re-Proposed Release to determine whether a security satisfies the new standard for creditworthiness. Those factors must be set forth in the text of the rule itself, rather than left as suggestions in the Federal Register.[15] This is essential to ensure compliance by MMFs, consistency in approach among MMFs, and enforceability by the Commission.

The Re-Proposed Release cites a variety of informal sources, including informal guidance letters, that appear to guide MMFs: "most of the advisers to these funds evaluate some common factors that bear on the ability of an issuer or guarantor to meet its short-term financial obligations."[16] In addition, "[b]ased on the staff's experience and in consideration of general criteria included in recommendations by an industry money market working group of best practices for making minimal credit risk determinations," the Re-Proposed Release enumerates a list of factors managers **should** consider.[17] However, despite the Commission's assertion "that an assessment . . . generally should include an analysis of" those recommended factors, the Re-Proposed Rule does nothing to ensure fund managers actually follow those recommended factors.[18]

Investors do not need protection from fund managers who follow industry best practices; they need rules to protect them from those who do not. Without an explicit set of factors that MMFs must consider, inattentive, incompetent, or even unscrupulous fund managers will have significantly wider leeway for determining which securities meet the general standard of creditworthiness: that the "security's issuer has an exceptionally strong

---

15 *See* Better Markets Comment Letter, "References to Credit Ratings in Certain Investment Company Act Rules and Forms; File No. S7-07-11 (April, 25, 2011), http://www.sec.gov/comments/s7-07-11/s70711-12.pdf. Specifically, without mandatory guidelines, funds will develop deficient formulae that will inevitably minimize credit risks associated with securities to allow their fund to purchase higher-risk/higher-return assets; the rules will disadvantage any adviser that is inclined to choose a more conservative approach to the assessment of credit risk, triggering a race-to-the-bottom; and a lack of uniformity will expose some investors to significantly greater risks while recognizing that investors cannot be expected to analyze the quality of these methodologies as a basis for differentiating among funds.

16 Re-Proposed Release, at 91.

17 Re-Proposed Release, at 91-93.

18 Re-Proposed Release, at 91.

capacity to meet its short-term financial obligations."[19] That in turn will pose a greater risk for investors and, potentially, a heightened run risk.

The Release confirms that more rigor is necessary in setting standards for credit analysis. It explains that, in connection with the SEC's examinations of funds, "staff has noted **a range** in the quality and breadth of credit risk analyses among the money market funds."[20] This finding strongly supports the conclusion that the SEC must establish a uniform set of factors in the final rule that all MMFs must consider when conducting their credit analysis.

Furthermore, the Commission has recognized that consideration of mandatory factors is necessary in numerous other rulemaking contexts. For example, in its July rulemaking on MMFs, the Commission imposed on MMFs specific factors to consider when conducting stress tests. This followed the 2010 reforms that required stress testing but allowed fund boards to determine which tests to conduct, given that "different tests may be appropriate for different market conditions and different money market funds."[21] Following three years of this implementation and having "observed disparities in the quality and comprehensiveness of stress tests, the types of hypothetical circumstances tested, and the effectiveness of materials produced by fund managers to explain the stress testing results to boards,"[22] the Commission imposed specific market conditions (factors) funds must consider as they conduct stress tests. Simply requiring funds to conduct tests without mandating protocols was unsuccessful.

Similarly, in the Commission's August rulemaking on credit rating agencies, the SEC declared NRSROs "must take into consideration the factors identified" when determining a credit rating agency's internal controls.[23] In its explanation, the Commission wrote:

> Given the importance of the NRSROs' internal control structures, the Commission believes that an NRSRO should be required to consider the factors identified in the proposing release when establishing, maintaining, enforcing, and documenting an effective internal control structure. The exercise of considering these factors will provide the NRSROs with an opportunity to critically evaluate the effectiveness of their existing internal control structures and new registrants a reference point for designing or modifying existing internal control structures to comply with the statutory

---

19 This is the standard for eligible securities. The same rationale applies to conditional demand or guaranteed securities as well, where the standard is the issuer or grantor "has a very strong capacity for payment of its financial commitments." Re-Proposed Release, at 013.

20 Re-Proposed Release, at 91.

21 Securities and Exchange Commission, Money Market Fund Reform, 75 Fed. Reg. 10060, 79 (Mar. 4, 2010).

22 Securities and Exchange Commission, Money Market Fund Reform; Amendments to Form PF, 79 Fed. Reg. 47736, 889 (Aug. 14, 2014) (Voted on in July, published in August).

23 Securities and Exchange Commission, Nationally Recognized Statistical Rating Organizations, 79 Fed. Reg. 55078, 268 (Sept. 15, 2014), *henceforth* "NRSRO Release" (Voted on in August, published in September); Rule 17g-8(d).

1825 K Street, NW, Suite 1080, Washington, DC 20006 TELEPHONE (1) 202.618-6464 FAX (1) 202.618.6465 WEBSITE bettermarkets.com

> requirement. This should improve the overall effectiveness of the internal control structures of the NRSROs.[24]

The Commission came to this conclusion by finding that, while "the internal control structures [should] 'instill confidence in their investors and the public that the companies in fact are achieving the objectives of their internal control rules,'" there existed "[d]eficiencies in the internal control structure" of several NRSROs.[25]

The same rationale applies to the determination of credit risk by MMFs. Mandatory consideration requirements will "instill confidence in investors and the public that [funds] are achieving the objectives of their" risk assessment methodologies.

The specific factors identified in the Release are helpful, and once incorporated into the Re-Proposed Rule as mandatory factors for consideration, will provide a useful and more objective framework for advisers to apply.[26] We commend the Commission for requiring credit risks to be determined, at least in part, on an issuer's financial data. However, the list must be comprehensive, must cover all material considerations that bear on the credit-worthiness of the securities under review, must be non-exclusive, and must allow funds to take into account additional, appropriate factors.

2. The Distinction Between First and Second Tier Securities Must Be Retained.

The Re-Proposed Rule must retain a differentiation between first and second tier qualifying securities. Removing this distinction will inevitably result in a dilution in the credit quality of the securities held by MMFs as funds seek higher yields.

Currently, Rule 2a-7 places private securities into three categories: first tier, second tier, and unqualified. A fund may currently purchase first tier securities at any time, but may only purchase second tier securities if the maturities are within 45 calendar days, and if second tier securities comprise no more than **three percent** of the fund's total assets.[27] This rule exists to prevent dilution of the fund's assets into lower-quality securities, thus helping to keep the fund solvent.

The Re-Proposed Rule will eliminate this distinction. The Re-Proposed Rule creates two categories of securities: those from an issuer which "has an exceptionally strong capacity to meet its short-term financial obligations," and all others. While the SEC asserts that this standard will "preserve the current degree of risk limitation in rule 2a-7 without reference to credit ratings," it is actually a lower standard.[28] As the Release acknowledges, "[b]y eliminating the rule's current limitations on investments in second tier securities,

---

24 NRSRO Release, at 098.
25 NRSRO Release, at 098, *citing* CFA II Letter.
26 List includes those mentioned on pages 91-93 of the Re-Proposed Release.
27 Rule 2a-7(d)(2)(ii), 17 C.F.R. 270.2a-7(d)(2)(ii).
28 Re-Proposed Release, at 90.

funds theoretically could invest in second tier securities to a greater extent than they do today."[29]

There is no reason to believe that funds will shy away from what are currently classified as second-tier securities, regardless of whether they comprise more than three percent of a portfolio. Rather, the Re-Proposed Rule values first- and second- tier securities equally, and would remove the limit on holding second-tier securities. Without that limit, those second-tier, riskier assets will inevitably comprise a greater percentage of a fund's holdings as competing advisers reach for yield, market share, and profits. Indeed, that is exactly what the Re-Proposed Rule allows and will, in fact, encourage.

The Commission's Original Proposed Rule, which held that issuers of first tier securities must maintain "the highest capacity to meet its short-term financial obligations,"[30] was stronger, more effective, and more in line with the current Rule 2a-7 than this Re-Proposed Rule. Further, the Original Proposed Rule was stronger in that it limited those securities which "present minimal credit risks" but are not first tier to three percent of a fund's assets. The Re-Proposed Rule similarly must maintain the distinction between first and second tier securities, with the accompanying limit on the percentage of second tier securities that a fund may hold.

3. The Re-Proposed Rules Should Clarify and Limit the Extent to Which Funds May Continue to Rely on Credit Ratings.

In the Release, the Commission states that under the Re-Proposed Rule, funds may still consider third party credit ratings when making credit risk determinations. For example, the Release explains that, when evaluating "whether a security presents minimal credit risks, a fund adviser could take into account credit quality determinations prepared by outside sources, including NRSRO ratings, that the adviser considers are reliable."[31] In addition, the Release notes that nothing in the Re-Proposed Rules would prohibit a fund from continuing to rely on its own policies and procedures that incorporate credit ratings,[32] or even require disclosure of relied upon NRSROs, noting, "nor would fund boards have to disclose designated NRSROs."[33]

Allowing funds to incorporate credit ratings into their standards undermines one of the core objectives of Section 939A of the Dodd-Frank Act. Simply removing references to credit ratings from the Commission's regulations helps accomplish one goal of the statute, which is to eliminate the governmental imprimatur on credit ratings. But Congress also sought to promote another policy objective, namely reducing actual reliance on credit ratings and encouraging independent due diligence and credit analysis. It therefore

[29] Re-Proposed Release, 90.

[30] 2011 Release, at 98

[31] Re-Proposed Release, at 90.

[32] Re-Proposed Release, at 001 ("we anticipate that many funds are likely to retain their investment policies as currently required under rule 2a-7, which incorporate NRSRO ratings and which would be permitted under the reproposed rule amendments.").

[33] Re-Proposed Release, at 89.

required the Commission to establish new standards that market participants would have to apply in making independent judgments about credit-worthiness. Establishing such new standards, while at the same time allowing market participants to continue their traditional reliance on credit ratings, would do nothing to accomplish this second Congressional objective. That approach simply would not reduce reliance on credit ratings or promote independent credit analysis.[34]

Therefore, the Re-Proposed Rules should explicitly address the extent to which and how market participants may continue to use credit ratings. It may not be possible or even desirable to prohibit market participants from considering credit ratings as they conduct their own credit analysis.[35] For example, a significant discrepancy between a fund's credit analysis and the applicable credit rating might serve as a useful signal to the fund's board that anomalies or flaws may exist in their credit analysis. This would presumably have the positive effect of causing the fund board to reexamine its credit analysis and make necessary corrections or at least understand the reasons for the differences.

However, the Re-Proposed Rules must make clear that funds may not **rely** on credit ratings, and that credit risk determinations under the Commission's new standards must be justifiable entirely on the basis of those new standards, without regard to credit ratings.

4. Strengthen Risk Monitoring by Establishing Mandatory Factors.

Re-Proposed Rule 2a-7 must, as the Commission has proposed, require MMFs to adopt written policies and procedures requiring the fund adviser to conduct ongoing review of each portfolio security to ensure that it continues to satisfy the new standard of creditworthiness.[36] However, the rule must require the ongoing monitoring to occur on a specified periodic basis so that the process occurs with a minimum frequency.

Furthermore, the monitoring requirements must specify, at a minimum, which factors a fund must consider, as with conducting the initial risk evaluation. The Release notes that the "review would typically update the information that was used to make the initial minimal credit risk determination and would have to be based on, among other things, financial data of the issuer or provider of the guarantee or demand feature."[37] This is positive, but insufficient, as this requirement must be included in the text of the rule, rather than merely set forth in the accompanying explanation of the rule in the Federal Register.

---

[34] It should also be noted that one of the Financial Stability Board's promulgated principles on credit rating agencies is that "Banks, market participants and institutional investors should be expected to make their own credit assessments, and not rely solely or mechanistically on CRA ratings." Financial Stability Board, Principles for Reducing Reliance on CRA Ratings (Oct. 27, 2010), *available at* http://www.financialstabilityboard.org/publications/r_101027.pdf.

[35] The Financial Stability Board again suggests that firms "may use CRA ratings as an input to their risk managements, but should not mechanistically rely on CRA ratings."

[36] Re-Proposed Release at 94-96.

[37] Re-Proposed Release at 95.

Finally, the Re-Proposed Rule does not require an adviser to notify the Board when a security may no longer be held by the fund due to a negative credit risk evaluation. While the Release states that the Commission "**would expect** that a fund board generally should establish procedures for the adviser to notify the board in such circumstances,"[38] notification to the Board should be required in the final rule.

B. The Re-Proposed Form N-MFP Must Require Detailed Reasoning for the Selection of Each Security.

The Re-Proposed Rule would require each fund to disclose in its monthly filing of Form N-MFP all NRSRO ratings to which it subscribes for each portfolio security, as well as any other NRSRO rating that the fund considered in making its minimal credit risk determination.[39] Provided that all credit analysis performed by a fund can be justified on the basis of the factors discussed above, and independently of any rating, having this information may prove helpful to the Commission in understanding the extent to which funds consider ratings.

However, the reporting requirements should be expanded to ensure that regulators and investors can gain a "better understanding of risks in money market fund portfolios."[40] The Re-Proposed Rule should require each fund to describe in the Form the factors they used in their credit analysis and a description of how they arrived at their creditworthiness determination. These enhancements to the reporting requirements are necessary to help ensure that each fund applies the new standards of credit-worthiness correctly and without regard to credit ratings.

C. The Re-Proposed Rule 2a-7 Exclusion Must Limit Exposure to Any One Guarantor to Five Percent.

Rule 2a-7 attempts to ensure that no fund is reliant on a single issuer for a substantial share of its assets. However, as explained in the Release, the rule as currently written could allow a fund to hold only securities from a single issuer, if those securities were covered by guarantees and no single guarantor was backing more than ten percent of the portfolio holdings.[41]

This is plainly unacceptable. As the Release acknowledges, this approach effectively ignores "a fund's exposure to the issuer," something fundamentally at odds with the goal of ensuring the diversification and stability of a fund.[42]

The Re-Proposed Rule would close this loophole, and this is a positive step. However, the Re-Proposed Rule would continue to allow a single guarantor to guarantee up

---

38 Re-Proposed Release, at 96.
39 Re-Proposed Release, at 97.
40 Securities and Exchange Commission, Money Market Fund Reform, 75 Fed. Reg. 10060, 84 (Mar. 4, 2010).
41 Re-Proposed Release, at 99.
42 *Id.*

to ten percent of a fund's assets.[43] There is no persuasive rationale for setting a more generous limit for guarantors of the securities in a fund than for issuers of the securities in a fund. Accordingly, the Commission should strengthen the diversification requirements by preventing any one guarantor from guaranteeing more than five percent of a fund's assets, as opposed to the ten percent threshold in the Re-Proposed Rule.

CONCLUSION

We hope these comments are helpful in your consideration of the Re-Proposed Rule.

Sincerely,

Dennis M. Kelleher
President & CEO

Stephen W. Hall
Securities Specialist

Todd Phillips
Attorney (Bar Application Pending)

Better Markets, Inc.
1825 K Street, NW
Suite 1080
Washington, DC 20006
(202) 618-6464

dkelleher@bettermarkets.com
shall@bettermarkets.com
tphillips@bettermarkets.com

www.bettermarkets.com

43 "[U]nder today's proposed amendment, each money market fund that invests in securities subject to a guarantee (whether or not the guarantor is a non-controlled person) would have to comply with both the 10 percent diversification requirement for the guarantor as well as the 5 percent diversification requirement for the issuer." Re-Proposed Release, at 99.