Dreyfus

THE DREYFUS CORPORATION

J. Charles Cardona
President

October 14, 2014

VIA EMAIL TO RULE-COMMENTS@SEC.GOV

Mr. Kevin M. O'Neill
Deputy Secretary
U.S. 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 (the "Release")

Dear Mr. O'Neill:

The Dreyfus Corporation ("Dreyfus") appreciates the opportunity to comment on the Securities and Exchange Commission's (the "Commission") (a) re-proposed amendments to remove references to credit ratings of nationally recognized statistical ratings organizations ("NRSROs") from Rule 2a-7 and to modify provisions in Form N-MFP that reference credit ratings, in consideration of the Commission's Dodd-Frank Act section 939A mandate and (b) proposed amendments to Rule 2a-7 that would eliminate an exclusion from the Rule's issuer diversification requirements for securities subject to a guarantee issued by a non-controlled person (collectively, the "Proposals").

Dreyfus is registered with the Commission as an investment adviser and is a subsidiary of The Bank of New York Mellon Corporation, a global financial services provider with approximately $1.6 trillion in assets under management and approximately $28.5 trillion in assets under custody and/or administration. Dreyfus currently manages approximately $270 billion in mutual fund and related stable net asset value cash management investment vehicles, including approximately $160 billion in 39 domestic money market fund portfolios that are structured within the confines of Rule 2a-7.

We will discuss the following comments in this letter.

1. ***The Proposed Definition of "Eligible Security."*** ***We recommend that the Commission limit the creditworthiness finding under the definition of "Eligible Security" to the established "minimal credit risk" determination, without qualifying it with any specific finding that must be made that is based on a descriptive or subjective reference about an issuer's capacity to meet its debt service obligations.***

2. ***Conform the Other Aspects of the Proposal to Reflect the Minimal Credit Risk Determination Only.*** ***Consistent with the foregoing, we believe that in each other part of the Proposal that requires the minimal credit risk determination, the Commission should remove the associated qualifying, subjective finding that is proposed.***

3. ***5% Issuer Diversification.*** ***We do not support the proposal to require each money market fund (and, particularly, tax exempt money market funds), that invests in securities subject to unconditional credit support to have to comply with both a 10% guarantor diversification test and a 5% issuer diversification test under Rule 2a-7.***

1. The Proposed Definition of "Eligible Security."

Background. Currently, Rule 2a-7 provides that a money market fund only can invest in an "Eligible Security," which includes securities that have received one of the two highest short-term NRSRO credit ratings (or the unrated equivalent as determined by the board or its delegate). Further, Rule 2a-7 currently limits money market funds to investing in securities determined to present "minimal credit risk," which determination includes factors pertaining to credit quality and any ratings assigned to such security by an NRSRO. Together, these current requirements define the universe of securities from which the minimal credit risk determination can be applied. Importantly, in our view, Rule 2a-7 currently does not require as part of the minimal credit risk determination any specific, subjective finding of creditworthiness.

The Proposal would revise the definition of "Eligible Security" by specifying that the minimal credit risk determination *"must include a finding that the security's issuer has an exceptionally strong capacity to meet its short-term financial obligations"* (the "ESC Finding"). This compares with the Commission's proposals in 2011, which would have defined an Eligible Security by the minimal credit risk determination and substitute, subjective standards of credit quality (that sought to correspond with related NRSRO ratings descriptors) for the definitions of "First Tier" and "Second Tier" under the Rule. We opposed this approach in 2011, mainly because of the subjectivity required in making the first and second tier distinctions as well as the apparent inequality in the proposed descriptors relative to the NRSRO descriptions used to define top tier rated securities (the 2011 proposals seemed overly limiting relative to permissible First and Second Tier investments).

The Proposal takes the approach of consolidating the two criteria proposed in 2011 and requiring a single, uniform, very high standard of quality (an approach supported by a number of commenters in 2011). Dreyfus did not support that approach in 2011 and while we firmly support very high standards of credit quality in money fund portfolios, for similar reasons we also do not support the Proposals. Our views have evolved to where we believe that the minimal credit risk determination, by itself, should be relied on rather than any substitute standard of creditworthiness that is based on making subjective findings. We believe it is the most appropriate approach to take, providing flexibility and a standard that managers have applied for years, uncluttered with a subjectivity that creates conflict for funds and their boards and managers.

Our Rationale for Supporting for the Minimal Credit Risk Determination Only.

A. Adopting the ESC Finding appears unnecessary in order to achieve the Dodd-Frank Section 939A objective. The "minimal credit risk" determination already provides the framework for making a definitive finding of creditworthiness for money market funds. Moreover, it provides a flexible framework uncluttered with the conflict that arises from substituting a subjective standard for an objective standard. The objective standard (First Tier and Second Tier) facilitates a level playing field. The subjective standard (as proposed) will not.

Correspondingly, we believe the proposed credit quality standard will create confusion and conflict in implementation for fund boards and managers. To illustrate, on one hand, the commentary in the Release suggests that removing the credit rating references from Rule 2a-7 may expand the universe of securities that managers may determine present minimal credit risk.

> *"By eliminating the rule's current limitations on investments in second tier securities, funds theoretically could invest in second tier securities to a greater extent than permitted today."*

On the other hand, in a number of places the commentary in the Release seeks to qualify the terms of the Proposal with statements suggesting that the "credit profile" of money market funds will not change. For example:

> *"The re-proposed standard, however, is designed to preserve the current degree of risk limitation in Rule 2a-7 without reference to the credit rating by requiring a fund's board (or its delegate) to determine that the issuer of a portfolio security has an exceptionally strong capacity to meet its short-term obligations, a finding that some boards or fund advisers my determine can be met by second tier rated securities (but only of the highest quality)."*

Ultimately, we are concerned that fund boards and managers will face conflict and confusion about the quality of an Eligible Security and how the rule will be interpreted and administered by the Staff and the Commission over time. For example, contrary to the statement in the Release, we would not interpret the Proposal to say that eliminating the First Tier/Second Tier limitations "theoretically" changes the potential universe of eligible investments for money funds. We believe it definitely changes it and so we are very concerned with how to interpret the substance of the Proposal with the associated commentary in the Release.

More specifically, we are concerned about the number of places in the Release where the commentary appears to set rules to qualify the proposed rule text. We believe that many of the qualifying statements in the Proposal may go beyond the scope of commentary or "guidance." For example, and without arguing the merits, in several places in the commentary it is suggested that third tier securities should not satisfy a finding of "exceptionally strong capacity." We believe this is a function of credit analysis and brings into question whether ratings criteria are being reinserted in the Proposal through commentary rather than through the Rule. We note other commentary with respect to conditional demand features (e.g., with respect to a single ratings downgrade) and monitoring for credit risks (again, related to the Commission's "expectations" in the event of a downgrade) that we believe raise similar concerns. Accordingly, we respectfully urge the Commission to consider how it represents the nature of this Proposal and the potential conflict that is posed in crafting a final rule and any associated commentary that might read more like rulemaking.

B. The foregoing comments reflect our view that we do not see a necessity in adopting a more specific "substitute" creditworthiness standard in order to remove credit rating references from Rule 2a-7 (because of the minimal credit risk determination requirement). However, to the extent the

Commission remains committed to this approach, as in 2011, we believe that the Proposal to substitute the ESC Finding may not be suitable because it still may be too restrictive relative to Rule 2a-7's current permissible quality requirements. Importantly, the ESC Finding does not account for variances in NRSRO ratings descriptions and in gradations in ratings.

To illustrate, here are the highest short-term ratings and ratings descriptors of the three leading NRSROs (for taxable securities):

S&P	A-1:	Highest category; strong capacity
	A-1+:	Highest category; extremely strong capacity
	A-2:	Satisfactory capacity
Moody's	P-1:	Superior ability
	P-2:	Strong ability
Fitch	F-1:	Strongest intrinsic capacity
	F-1+	Exceptionally strong capacity
	F-2:	Good intrinsic capacity

Because the ESC Finding corresponds with a "Fitch-1+" rating only, we respectfully urge the Commission to reconsider if the proposed "exceptionally strong" creditworthiness finding is representative of the quality of money market fund portfolios currently and whether the Proposal will preserve current quality parameters. Notwithstanding, we believe any substitute measure of creditworthiness proposed should not raise such questions and we respectfully ask the Commission consider if the Proposal is inclusive enough to accomplish the Commission's goal of preserving the current levels of creditworthiness.

2. <u>Conform the Rule Proposal to Reflect the Minimal Credit Risk Determination only</u>.

<u>Conditional Demand Features</u>.

Under Rule 2a-7 currently, a long-term security subject to a conditional demand feature may be determined to be an Eligible Security (or a First Tier security) if (a) the conditional demand feature is an Eligible Security or a First Tier security and (b) the underlying security has received either a short-term or long-term rating within the two highest NRSRO ratings categories, or comparable unrated securities.

As proposed, a fund would have to determine the conditional demand feature is an Eligible Security (as proposed to be defined) and the fund's board (or its delegate) would have to evaluate the long-term risk of the underlying security and determine that it has *"a <u>very strong</u> capacity for payment of financial commitments."*

Based on our earlier comments, we believe the rule should provide that *"the board or its delegate would have to evaluate the long-term risk of the underlying security and determine that it presents minimal credit risk."* As noted above, we believe that this minimal credit risk determination would be applied without any qualifying, subjective descriptor or finding (e.g., a specific finding of a "very strong" capacity, e.g.)), as proposed.

Monitoring Minimal Credit Risks.

Under Rule 2a-7 currently, a fund's board (or its delegate) must (a) promptly reassess whether a security that has been downgraded by an NRSRO continues to present minimal credit risks; (b) take such action as it determines is in the best interests of the fund; and (c) undertake an ongoing review of the minimal credit risks associated with securities for which maturity is determined by reference to a demand feature.

As proposed, each fund will be required to adopt written procedures that require the fund's adviser to provide ongoing review of the credit quality of each portfolio security, eliminating the need for re-assessing credit risk of an issuer when a security is downgraded by an NRSRO. Under this proposal, the review must determine that each security continues to present minimal credit risks (i.e., that the issuer or provider of the guarantee or demand feature continues to meet the "exceptionally strong" standard).

Based on our earlier comments, we support this reassessment requiring a minimal credit risk determination pursuant to written procedures as proposed, but without any qualifying, subjective descriptor or finding (e.g., a specific finding of "exceptionally strong" capacity), also as proposed.

3. The 5% Issuer Diversification Proposal.

Currently, for securities subject to unconditional credit support, only the 10% guarantor diversification test applies to that security. We believe that focus is appropriate and, contrary to the thinking underlying the Proposal, should be maintained as currently provided for under Rule 2a-7. In our view, the credit support provider assumes the credit risks associated with a particular issue, so it is appropriate to direct, and continue to direct, the minimal credit risk determination to that entity. The Proposal, to the contrary, seeks to re-focus the analysis on issuer concentration risk.

We believe a sharp reduction in market supply will ensue (particularly in the tax exempt market) if this Proposal is adopted. We further believe that any perceived benefit from enhancing issuer concentration with this proposed rule is far outweighed by the portfolio management challenges that will be raised. Many of the largest issuers of variable rate demand notes issue with unconditional guarantees from several different tier one, credit support providers (and which get tested under Rule 2a-7's 25%/15% basket). A 5% issuer diversification overlay will be severely limiting, particularly for tax exempt money market funds (and mainly, for state-specific tax-exempt funds) in terms of eligible supply. In fact, we are unsure how a 5% issuer diversification test could reasonably be accommodated by a state-specific fund.

Moreover, we note that the supporting economic analysis is based on a one-month sample of data from the Form N-MFP, for which we question both whether it is representative and, in our experience, accurately depicts the particularly negative impact we anticipate adopting this Proposal will have on tax exempt funds. We also note that the economic analysis focuses on forecasting a number of positions that might have to be managed within a portfolio in order to bring it into compliance with the Proposal. We think this focus is misplaced because we view the long-term supply concerns for tax-exempt money funds as a much more serious concern from eliminating this exclusion than we do a few portfolio holdings changes.

To summarize, we think the negative impact on money market funds far outweighs any diversification benefits that might arise from adopting this Proposal. Accordingly, we believe the Commission should not adopt this Proposal. In the alternative, we respectfully urge the Commission to consider not adopting this Proposal as to tax-exempt money market funds, where to detrimental impact will be strongest.

We thank the Commission again for the chance to comment on these important Proposals. We would be pleased to discuss any of these comments further, at your convenience.

Very truly yours,

J. Charles Cardona

J. Charles Cardona, President

<u>With copies to</u>:

The Honorable Mary Jo White, Chair
The Honorable Luis A. Aguilar, Commissioner
The Honorable Daniel M. Gallagher, Commissioner
The Honorable Kara M. Stein, Commissioner
The Honorable Michael S. Piwowar, Commissioner
Norman B. Champ, III, Director, Division of Investment Management