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January 23, 2013

Financial Stability Oversight Council
Attn: Amias Gerety
1500 Pennsylvania Avenue, NW
Washington, DC 20220

RE: Proposed Recommendations to the Securities and Exchange Commission under Section 120 of the Dodd-Frank Act Regarding Money Market Mutual Funds; Docket Number FSOC-2012-0003

Dear Mr. Gerety:

The U.S. Chamber of Commerce ("Chamber") is the world's largest business federation, representing more than three million businesses and organizations of every size, sector and region. The Chamber created the Center for Capital Markets Competitiveness ("CCMC") to promote a modern and effective regulatory system for the capital markets to promote economic growth and job creation. The CCMC appreciates the opportunity to comment on the Proposed Recommendations Regarding Money Market Mutual Fund Reform ("Proposed Recommendations") to be issued under section 120 of the Dodd-Frank Wall Street Reform and Consumer Protection Act ("DFA" or "Dodd-Frank") by the Financial Stability Oversight Council ("Council") and published in the *Federal Register* on November 19, 2012 ("Proposal").

The Chamber's members are both investors in money market mutual funds ("MMMFs") and borrowers of these funds through their commercial paper programs. Accordingly, we supported, and continue to support, regulations that strengthen MMMFs, such as the amendments to Rule 2a-7 promulgated by the Securities and Exchange Commission ("SEC") in 2010. The continued vitality and preservation of this important cash management tool remains our primary concern. The alternatives proposed by the Council, however, will fundamentally alter the structure and nature of MMMFs, extinguishing their utility as a critical source of investing and short-term financing for the business community.

As noted in the CCMC's November 5, 2012 letter to Treasury Secretary Timothy Geithner, we are deeply concerned by the Council's actions in issuing proposed recommendations for money market mutual fund reform through its authority under Section 120 of the DFA. Such action could create uncertainty, weaken financial regulation, harm investors, and damage the capital formation process needed for businesses to grow and create jobs. We continue to believe that the SEC, the primary regulator with expertise on MMMFs, should be allowed to proceed with its deliberative process in evaluating options for additional changes to Rule 2a-7 without interference from the Council. The Council has indicated that it may not seek to issue a final recommendation to the SEC if the SEC moves forward with meaningful structural reforms of MMMFs. Based on several SEC Commissioners' public statements[1] and the recent release of the staff's study on MMMF questions posed by SEC Commissioners Aguilar, Paredes, and Gallagher[2], there is little doubt that the SEC is working toward strengthening the regulation of MMMFs while preserving the utility of this product as an efficient cash management and short-term financing tool for businesses. Accordingly, the CCMC believes that the Council should allow the SEC to move forward with its work on MMMF without undue influence from the Council.

Nevertheless, the CCMC remains concerned about the actions of the Council and the recommendations put forth. Our comments are divided into two sections. The first section articulates the specific concerns of the CCMC as to the three recommendations made by the Council. The second section states the CCMC's concerns regarding an inadequate process and the dubious legal authority the Council asserts for invoking Section 120 of the DFA. Clearly, if the Council acts beyond the scope of its statutory authority or fails to comply with its procedural rulemaking obligations, then the recommendations themselves cannot be implemented. Specifically, we believe that:

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[1] *See* August 23, 2012 Statement Regarding Money Market Funds by Commissioner Luis A. Aguilar and August 28, 2012 Statement on Regulation of Money Market Funds by Commissioner Daniel M. Gallagher and Commissioner Troy A. Paredes.

[2] *See* November 30, 2012 Response to Questions Posed by Commissioners Aguilar, Paredes, and Gallagher available at http://www.sec.gov/news/studies/2012/money-market-funds-memo-2012.pdf.

- The Proposal's recommended alternatives will create adverse operational and economic issues for businesses and wreak havoc on time-tested, stable and efficient cash management and short-term financing options used by businesses. In effect, the proposed recommendations would destroy the utility of MMMFs and precipitate the very run on funds by corporate investors that the Proposal is intended to prevent.

- The Council has not demonstrated that MMMFs pose a threat to financial stability, a requirement that needs to be satisfied for the Council to take action under section 120 of DFA. Additionally, the Council has also violated prescribed processes because it does not have the current authority to treat MMMFs as nonbank financial companies. Moreover, it has failed to appropriately consult with the SEC or provide the appropriate cost benefit analysis required by Section 120.

Our concerns are discussed in more detail below.

I. Background

MMMFs play a critical role in the U.S. economy because they provide two essential services for American businesses and local governments. First, MMMFs are an essential short-term investment vehicle and cash management tool. Corporate treasurers rely on MMMFs to efficiently and affordably manage cash. Cash balances for companies fluctuate on a daily basis, and depending on the nature of the business, companies' cash levels can swing widely from hundreds of dollars to hundreds of millions of dollars.

Corporate treasurers' main priority is to ensure the safety and liquidity of their companies' cash. As such, MMMFs' stable price per share and easy investment and redemption features make them an attractive and preferred investment choice. Investments can be made and redeemed on a daily basis without fees, penalties, or tax implications. Moreover, MMMFs offer corporate treasurers diversified and expertly-managed short-term investment of their cash. Quite simply, it is more efficient and economical to pay the management fee for a MMMF than to hire internal staff to manage the investment of cash.

It is important to note that corporate treasurers understand the risk of investing in MMMFs. They are professional stewards of their companies' funds and take their responsibilities seriously. Because MMMFs include significant disclosures in their public filings and other investor resources, corporate treasurers are able to easily ascertain what investments are in each MMMF and the degree of risk associated with each of the funds. Contrast this with the need to understand a bank's creditworthiness when making a deposit. Corporate treasurers have seen that even the largest and most respected money-center banks are prone to surprises and a succession of potentially damaging disclosures.

The second crucial role that MMMFs play in the operation of American business is as a source of liquidity for their short-term financing needs. MMMFs represent a major source of funding to the commercial paper market in the U.S., purchasing 36 percent of all outstanding commercial paper as of November 2012.[3] This source of funding is vital to companies across America as commercial paper is an efficient, affordable means to obtain short-term financing on a moment's notice. These proposed recommended changes to MMMFs will have both direct and indirect adverse implications for the larger U.S. economy and occur at the same time that American companies and institutions will be confronted by the effects of the Volcker Rule, Basel III capital requirements, and expanded derivatives regulation—all of which will impair companies' ability to hedge risk and obtain capital necessary to grow and create jobs.

In general, corporate treasurers receive a daily cash report indicating the anticipated cash inflows and cash outflows for that day. If there is an anticipated cash shortfall, a company can issue commercial paper and have the funds available later that same day. This "just-in-time" financing not only affords corporate treasurers the flexibility to borrow cash when needed, it also grants them the flexibility to borrow for the duration needed—and at much more affordable rates. For example, currently in the United States, a company rated at Tier II (A2/P2) can issue overnight

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[3] According to data from Investment Company Institute and Federal Reserve Board.

commercial paper at approximately 41 basis points. In contrast, drawing on a bank line of credit with same day notice for a short duration will cost prime (approximately 325 basis points). This represents an 8-fold increase in financing costs. Many companies, including many small or start-up companies, will be unable to arrange lines of credit on such terms. For them, the only alternative will be to slowly build up reserves of idle cash. This will hamper the growth of these companies, limit their ability to take advantage of new business opportunities, slow product development, and ultimately impede job growth.

This is why the CCMC supports prudent regulations, like the SEC's 2010 amendments to Rule 2a-7, that make MMMFs better able to withstand short-term liquidity swings, and that strengthen the utility and vibrancy of MMMFs. These funds are a result of over 40 years of financial evolution. This evolutionary process was driven by the needs of corporate and municipal America, and the 2010 amendments were consistent with this prudent evolution. The Proposal, however, would make fundamental structural changes to this important cash management tool that would render it useless for investors and the business and municipal communities. The significance of the changes in each of the three proposed alternatives cannot be understated, as MMMFs provide investors, businesses, and state and municipal governments with the flexibility needed to meet short-term funding obligations and deploy reasonable cash management strategies that support their everyday operations. MMMFs play a critical role in sound financial management. No alternatives with the same multiple benefits are available to replace money market mutual funds.

II. Comments on the Council's Recommendations

1. Comments Regarding Alternative One

The CCMC has consulted broadly with the corporate treasurers of its members regarding the Council's Proposal. This process illustrated significant concerns across the corporate treasurer community about the operational impacts of proposed Alternative One on American business financing and on the capital markets and the U.S. economy more generally. Accordingly, we cannot support the implementation of a floating NAV for MMMFs, as proposed by the Council, regardless of whether

accounting and tax relief is made administratively available. We discuss these serious concerns in more detail below.

1.1. $100 Per Share Pricing

Under Alternative One the Council proposes that MMMFs would re-price their shares at $100 per share. According to the Council, a $100 share price is more likely to result in regular fluctuations in NAV.[4] The Council apparently sees this as beneficial. While we agree that moving from a $1.00 share price to a $100 share price will likely result in regular fluctuations in NAV, we do not share the perspective that the increased price volatility is beneficial. Moving to a $100 per share price will create a multitude of very small short-term capital gains or losses that previously would not have occurred and that would not occur if Alternative One did not require the use of a $100 per share price. This would create an additional unnecessary burden for MMMF shareholders that will deter many of them from investing.

1.2. Tax Considerations

The Proposal suggests that the Department of the Treasury and the Internal Revenue Service ("IRS") will consider administrative relief for both shareholders and fund sponsors.[5] We note that even if the IRS agrees to grant administrative relief for *de minimis* gains and losses on wash sales of MMMF shares, investors would still have to keep track of gains and losses to determine if they are *de minimis*.

For businesses that frequently move money in and out of numerous MMMFs on a daily or weekly basis, having to keep track of these gains and losses without human error will be challenging. For example, for a corporate treasurer with a portfolio of a dozen MMMFs with $10 million in each, if on Monday he redeems $2 million from one fund at $99.99 per share, and continuing with the same fund on Tuesday invests $1.5 million at $100.01 and on Wednesday invests $1 million at $99.98, and on Thursday redeems $4 million at $100.002 and on Friday redeems $2.1

[4] 77 Fed. Reg. 69455, 69466 (Nov. 19, 2012) ("Proposal").
[5] *Id*. at 69467.

million at $99.99, even with consistently applying the LIFO or FIFO approach, accounting can get confusing. Multiply this complexity and detail across a dozen different funds at different NAVs and it gets complicated quickly.

The burden associated with tracking these transactions requires fundamental changes to treasury systems that will take months to test and complete. Moreover, these changes would have to take their place after prioritization with other business needs the IT department must meet. In this interim, corporate treasurers would have to forgo making investment in MMMFs. This outflow of funds could well force fund managers to wind down their offerings, reducing the diversification advantages funds bring as outlined in more detail below.

1.3. Operational and Systems Issues

The complications that would arise from the move to a floating NAV as envisioned in Alternative One will impose an enormous burden on both investors, particularly businesses, and MMMF sponsors. Presently, corporate accounting systems and treasury workstations are not programmed to accept a floating NAV for MMMFs. A move to floating NAV will be a complicated, lengthy, and expensive process. As a first step, the MMMF industry will need to develop a reporting format for a floating NAV MMMF and update its systems accordingly. Only when this is accomplished will investors, particularly corporate treasurers, be able to make the necessary adjustments to their accounting and treasury systems and work with their software vendors to determine how those modifications will need to be made—both in terms of software development and software implementation and testing.

MMMF related systems changes may involve significant capital expenditures. Because technology innovation is dynamic, the capital outlay for these system changes will have to be incorporated and prioritized among a pre-existing pipeline of corporate information technology projects and other major corporate capital expenditures. Financial and resource constraints may result in a long lead time to develop and implement systems that will allow corporate treasurers to deal with MMMFs with floating NAVs.

Discussions with corporate treasurers suggest the following general parameters for the timing of a transition from stable NAV to floating NAV for fund sponsors and investors.

Phase 1—fund industry modifies reporting and systems: 12 to 24 months
Phase 2—software vendors and corporate investors develop necessary software upgrades, corporate investors get approval for capital expenditures on software systems: 6 to 12 months after Phase 1.

Phase 3—implementation and testing of upgraded treasury workstations and accounting software: 18 to 24 months after Phase 2.

In addition, not only do the systems not exist to accommodate a floating NAV, but the standard protocol to transmit that data from the MMMFs does not currently exist. Every aspect of the data transmission would have to be developed from the ground up. In developing this protocol, much uncertainty lingers: Is American National Standards Institute the preferred standard oversight organization to embrace these standards or is the National Institute of Standards and Technology under the U.S. Department of Commerce? If these standards have world-wide implications, then would the International Organization for Standardization be better for oversight and promulgation? Is there going to be a clearinghouse or exchange for the daily floating NAV? Or do investors have to communicate with each MMMF individually to get a daily value?

Any implementation of Alternative One must take into consideration the time and resources needed for the foregoing systems changes in order for a floating NAV system to be put into place without major disruptions. Allowing an inadequate amount of time for a transition will force corporate treasurers—and other investors with similar operational issues—to withdraw from investments in MMMFs. In making its recommendations, the Council should take care that it does not trigger such a destabilization of the MMMF industry by imposing regulations it asserts are intended to prevent just such a run on MMMFs.

1.4. Accounting Treatment

The Council acknowledges that there would be an accounting issue as to whether a floating NAV would meet the characteristics of a cash equivalent under relevant accounting guidance.[6] If the Financial Accounting Standards Board and its international counterparts are unable to set accounting standards that allow a floating NAV MMMF to be deemed a cash equivalent, corporate treasurers will be forced to withdraw investments from MMMFs. Companies have an obligation to present accurate financial statements to their shareholders and potential investors. Accordingly, if investments in MMMFs can no longer be categorized as cash equivalents, investment by corporate treasurers is certain to decrease substantially, and the Proposal will result in exactly the type of exodus the Council claims it wants to prevent. The Council should make certain that domestic and international accounting standard setting bodies make the necessary regulatory and policy changes prior to moving forward with any substantive steps to impose a floating NAV.

Importantly, it should also be noted that these accounting standards need to be in place before any vendor software changes can be made and implemented.

1.5. Proposed Removal of Rule 22e-3

The CCMC believes that the Council is being similarly short-sighted by taking the position that if Alternative One is adopted, and MMMFs will no longer need to maintain a stable NAV, the SEC should remove Rule 22e-3, which allows an MMMF to suspend redemptions and commence a liquidation of the MMMF if the MMMF has broken the buck or is about to break the buck. According to the Council, with a floating NAV in place, the need for such actions should be significantly reduced except under the most extreme circumstances.[7]

We disagree with the Council's reasoning. Regardless of whether an MMMF's NAV is stable or floats, the ability to suspend redemptions under Rule 22e-3 is necessary for investor protection and an orderly liquidation of a MMMF. Investors who are aware that the redemption suspension option is no longer available are much more likely to "run" from the funds and redeem their shares in response to slight

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[6] *Id.*

[7] *Id.* at 69466.

fluctuations. The removal of this rule would be an accelerant for fund runs and provide no investor benefit whatsoever.

1.6. Proposed Removal of Rule 17a-9

The CCMC also takes issue with the Council's view that conversion to floating NAVs would obviate the need to permit affiliate support through the purchase of MMMF portfolio securities.[8] Removing the possibility of affiliate support would do nothing to promote fund stability, while depriving funds of a crucial source of ad hoc liquidity, subject to regulatory scrutiny. In fact, removing the availability of support under Rule 17a-9 would seem counter-productive in a world in which MMMFs are no longer able to suspend redemptions. Again, if a goal of the Proposal is to mitigate risk to our financial system that might result from a run on funds, it would seem counterintuitive to remove tools that fund sponsors can use as a support mechanism. MMMF managers are uniquely qualified to assess the liquidity and credit risks facing a MMMF, and they should not be denied the ability to create a cooling-off period in order to allow investors to assess matters deliberately instead of reflexively in a race for the door.

1.7. Investment Policies

The ultimate decision of a company's investment policies rests with its Board of Directors. These policies are set with an appropriate degree of care and with the best interest of the company and shareholders in mind. The Board has a fiduciary obligation to ensure that a company's available cash is invested in investment vehicles with appropriate liquidity risk and credit risk. As such, boards generally allow investment of cash only in stable value products where there is low degree of risk of loss as funds intended for liquidity purposes are the lifeblood of any company. In fact, most corporate investment policies prohibit investment vehicles that have a NAV less than $1.00. Given the fiduciary responsibilities of corporate boards, it is unlikely that that they will allow cash investments in a floating NAV product, even if

[8] *Id.*

the appropriate investor protections are in place and tax and accounting issues have been accommodated by regulators. In the case of many state and local governments the consequences of a floating NAV could not be clearer. Many state and local governments are subject to statutory prohibitions against investing in products that do not have stable NAVs. Therefore, should Alternative One be adopted and a floating NAV is implemented, these investors will have no choice but to withdraw their funds from MMMFs.

1.8. Commercial Paper Implications

MMMFs are significant investors in the commercial paper issuances that Corporate America depends on to provide short-term financing for operations. Any changes to the regulatory scheme that makes MMMFs a less attractive investment will impact the overall costs for issuers in the commercial paper market resulting from a reduced demand for commercial paper

As many investors are not able to tolerate or invest in a product without a stable value, MMMFs will no doubt see a reduction in investments. A recent survey by the Association of Financial Professionals indicates that up to 77 percent of organizations would be less willing to invest in MMMFs and/or would reduce or eliminate their holdings of MMMFs currently in their short-term investment portfolio as a result of allowing NAVs to float.[9] Accordingly, the diminished demand for commercial paper will put pressure on corporate issuers to increase yields to attract new investors, driving up financing costs or force them to move to other, less-efficient means to raise capital—all of which will increase financing costs.

Higher financing costs will have negative consequences. As commercial paper financing becomes more expensive, companies will have to extract cost savings from elsewhere within the firm. For instance, labor, product development or operations costs will have to be cut to make up the difference. This re-prioritization of spending within businesses hinders their productivity and adversely impacts hiring, GDP, and the economy as a whole.

[9] 2012 AFP Liquidity Survey available at http://www.afponline.org/liquidity/.

2. Comments Regarding Alternatives Two and Three

Under Alternatives Two and Three the Council proposes to mandate that most MMMFs maintain a NAV buffer, which would be a tailored amount of up to between 1 percent and 3 percent. The lower 1 percent NAV buffer would be coupled with a requirement that 3 percent of any shareholder's highest account value in excess of $100,000 during the previous 30 days (Minimum Balance at Risk or "MBR") be available for redemption with a 30-day delay.

The CCMC believes that Alternatives Two and Three present significant operational and economic challenges that will precipitate significant and potentially permanent redemptions by corporate investors. Because our views regarding the NAV buffer under both Alternatives Two and Three are similar, we have combined those comments in section 2.1 and provided separate comments for the MBR in section 2.2.

2.1 NAV Buffer

2.1.1 Additional Costs and Loss of Yield for Investors

A NAV Buffer, whether 1 percent or up to 3 percent, will have to be funded by the fund sponsor, a subordinated class of shareholders, or through retained earnings. Regardless of the source, the implementation of a NAV buffer will be costly. Significant costs will be passed down to investors either in the form of reduced yield or additional fees. These will, in turn, deter investors from investing in MMMFs.

2.1.2 Math Doesn't Work

The economics of a NAV buffer are questionable under any circumstance. However, in the current near-zero interest rate environment, a NAV buffer is not economically feasible. Federal Reserve Chairman Ben Bernanke has indicated that

interest rates will remain low until 2014. In fact, the average yield for prime MMMFs in 2012, was 4 bps.[10] Given such low yields, the additional costs associated with building up a NAV buffer through retained earnings will result in a negative yield for investors. The math simply does not work. No investors will put their money into MMMFs where returns are not available.

Until interest rates revert to a profitable level, the only way funds can amass 1 percent or 3 percent capital is if the fund sponsor provides it. This option discriminates against non-bank sponsors that may not have the additional resources to fund a NAV buffer. The likely result is industry consolidation that reduces competition and investor choice, while concentrating risk in a smaller number of funds. Such result should be contrary to goals of financial regulators.

Moreover, a NAV buffer is likely to incentivize sponsors to reach for yield. MMMF reforms should not give rise to conditions that may distort sponsors' behavior to purchase anything other than low risk investments.

2.1.3 Impact on Commercial Paper Issuers

The Council also proposes to implement a three-tiered approach with the NAV buffer, exempting investments in U.S. Treasury securities and repos from being subject to a buffer while other assets, including corporate commercial paper, would be subject to a buffer of as much as 1 percent to 3 percent. This tiered approach could disincentivize MMMFs from purchasing commercial paper because it would be subject to a higher buffer. This could force issuers to offer higher yields in order to attract MMMF investors or find less efficient financing alternatives, since the funds would need increased yield to offset the costs of building the buffer associated with holding commercial paper.

The increased interest costs borne by issuers would result in cost-cutting elsewhere in companies that could hinder hiring, productivity, and growth in the overall economy. If it becomes too expensive to access the commercial paper market,

[10] According to data from iMoneyNet.

companies will have to transition to inefficient means of ensuring short-term financing, such as hoarding cash, which will also harm the larger economy. Either outcome will result in companies that are less efficient and unable to react quickly to changing business realities.

2.2 Minimum Balance at Risk (MBR)

The Council takes the position that an MBR will eliminate a "first mover advantage" by spreading any losses incurred by a MMMF among all investors with balances greater than $100,000 and redemptions within the last 30 days. This proposal would do grave harm to MMMFs, by diminishing one of the attributes of MMMFs that attracts investors—the ability to redeem holdings at any time. While the intent is to create a disincentive for redemptions, we have serious concerns regarding the reality that the implementation of an MBR will result in significant shift away from MMMF investments run by corporate investors. As noted below, there are many complications involved with an MBR.

2.2.1 Illiquidity and Complexity

The MBR concept requires that 3 percent of any redemptions for balances in excess of $100,000 be held back, rendering that amount illiquid. Again, immediate liquidity is one of the features of MMMFs that attract investors. The MBR would be highly problematic for corporate treasurers as it runs counter to their priority of ensuring liquidity in their companies' coffers. If corporate treasurers cannot get access to cash investments, they would be forced to seek alternative resources to meet working capital needs. This includes issuing debt or drawing on credit facilities, incurring additional costs and eliminating resources that may be deployed more efficiently elsewhere. It is imprudent and illogical for corporate treasurers to take this course of action.

The operational complexity of an MBR would also deter investment from corporate treasurers. Consider a company whose cash position fluctuates several times a month from having excess cash, which it invests, to having deficits met with short-term borrowings. Each time the company liquidates investments when it goes into a deficit, it must leave behind a significant MBR. The more times this fluctuation

occurs, the more of these idle balances the MBR has tied up, potentially amounting to a significant proportion of the company's average cash balance. For companies with large cash balances and significant daily swings, investing under an MBR is complicated and undesirable.

2.2.2. Accounting Issues

Currently, under generally accepted accounting principles (GAAP), MMMF investments are considered cash equivalents and rolled into the cash balance on a company's balance sheet. However, under an MBR concept, the portion of that investment held back or restricted may not be considered a cash equivalent because it is illiquid. In addition, it is possible that accountants will require companies to value the illiquid portion of the asset at a value below par. As such there is an inherent loss created by regulators with the implementation of the restrictions of an MBR.

In the aggregate, the complications associated with an MBR will deter corporate investment in MMMFs. If corporate treasurers cannot have immediate access to 100 percent of their cash investments, they will not invest in MMMFs. If the accounting becomes too onerous, corporate treasurers will not invest. If an immediate loss is taken with an MBR in place, corporate treasurers will immediately take cash elsewhere. In all, the MMMF industry could lose approximately $427 billion in assets from nonfinancial corporate investors.[11] An MBR is inherently destabilizing and promotes rather than prevents the collapse of MMMFs.

III. The Proposed Recommendations Do Not Satisfy the Requirements of Section 120 of Dodd-Frank or Basic Procedural Requirements

Section 120 of the DFA provides that the Council may issue recommendations to primary financial regulatory agencies for the application of new or heightened standards and safeguards for financial activities or practices conducted by bank holding companies or nonbank financial companies.

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[11] Derived from Federal Reserve Board Flow of Funds Accounts.

In order to be valid such recommendations must satisfy the conditions established by section 120. Recommendations may only apply to the conduct of a financial activity or practice by either bank holding companies or nonbank financial companies. The Council must:

1. only issue recommendations with respect to bank holding companies and companies that qualify as a nonbank financial companies; [12]

2. determine that the conduct, scope, nature, size, scale, concentration, or interconnectedness of the activity or practice could create or increase the risk of significant liquidity, credit, or other problems spreading among bank holding companies and nonbank financial companies, U.S. financial markets or low-income, minority or under-served communities;[13]

3. consult with the primary financial regulatory agency to which the proposed recommendations are to be directed;[14]

4. take costs to long-term economic growth into account, *i.e.*, conduct a cost benefit analysis;[15] and

5. provide notice to the public and an opportunity for comment.[16]

Under section 120(c), the primary financial regulatory agency must impose standards recommended by the Council, or similar standards deemed acceptable by the Council, or explain to the Council in writing within 90 days after the Council issues the recommendation why the agency has determined not to follow the recommendation of the Council.

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[12] DFA §120(a).
[13] *Id.*
[14] DFA §120(b)(1).
[15] DFA. §120(b)(2)(A).
[16] DFA. §120(b)(1).

As discussed below, the Proposed Recommendations fail to satisfy these requirements on several counts, and for that reason, if issued in their present form to the SEC they would not require the SEC to take any of the actions mandated by section 120(c).

1. The Proposed Recommendations Are Not Legally Valid Because the Council Does Not Currently Have the Authority to Treat MMMFs as Nonbank Financial Companies

Simply put, the Council does not have the authority to make recommendations under section 120 in regard to nonbank financial companies **unless and until** the Board of Governors of the Federal Reserve System ("Board") issues regulations that establish the requirements for a company to be determined to be predominantly engaged in financial activities ("Financial Activities Rule") and thus be treated as a nonbank financial company. The Congress made the issuance of a final Financial Activities Rule the **essential precondition** for the Council to purport to issue a recommendation in regard to a category of "nonbank financial companies."

The Board has proposed a Financial Activities Rule but has not yet issued final regulations. Thus, under the structure of Title I of the DFA as designed by Congress, the Council has no authority to identify any category of companies, including MMMFs, as nonbank financial companies for purposes of recommendations under section 120.

1.1. A Final Financial Activities Rule by the Board Has Not Been Adopted

Although the Council's authority to make recommendations under section 120 is limited to entities that qualify as nonbank financial companies (as determined by Board rules that have not been adopted) and bank holding companies, it has issued the Proposed Recommendations in regard to MMMFs on the basis that it "believes" that they are "nonbank financial companies."[17]

[17] Proposal, 77 Fed. Reg. at 69460.

The term "nonbank financial companies" in section 120 is subject to the definition contained in section 102(a)(4) of the DFA.[18] The critical element of that definition is the definition of the term "predominantly engaged in financial activities" which is contained in section 102(a)(6) of the DFA.[19]

As noted above, the definition of the term "predominantly engaged in financial activities" is not self-effectuating. Accordingly, Congress issued the following mandate to the Board in section 102(b) of the DFA:

> (b) DEFINITIONAL CRITERIA.—The Board of Governors **shall establish, by regulation**, the requirements for determining if a company is predominantly engaged in financial activities, as defined in subsection (a)(6). (emphasis added).

It is logical for Congress to have required the Board to promulgate these regulations because the Board has the authority in regard to the application and implementation of the Bank Holding Company Act, including financial activities that are permissible under section 4(k) of the BHCA.[20]

The Board responded to Congress's directive in section 102(b) by publishing a proposed Financial Activities Rule in February 2011.[21] It issued a supplemental

[18] A "U.S. nonbank financial company" is generally defined as a company that is (i) incorporated under the laws of the United States or any State, and (ii) is predominantly engaged in financial activities, as defined in section 102(a)(6).

[19] Section 102(a)(6) provides:

> (6) PREDOMINANTLY ENGAGED.—A company is "predominantly engaged in financial activities" if –
> (A) the annual gross revenues derived by the company and all of its subsidiaries from activities that are financial in nature (as define defined in section 4(k) of the Bank Holding Company Act of 1956) and, if applicable, from the ownership of or control of one or more depository institutions, represents 85 percent or more of the consolidated annual gross revenues of the company; or
> (B) the consolidated assets of the company and all its subsidiaries related to activities that are financial in nature (as defined in section 4(k) of the Bank Holding Company Act of 1956) and, if applicable, related to the ownership or control of one or more insured depository institutions, represent 85 percent of the consolidated assets of the company.

[20] 12 U.S.C. §1844(b).

[21] 76 Fed. Reg. 7731 (Feb. 11, 2011) ("Board Proposal").

proposed Financial Activities Rule in April 2012.[22] Commenters, including the CCMC, have raised a range of objections to the proposed Financial Activities Rule.

The Board recognizes that the Council's ability to take actions with respect to "nonbank financial companies" is **contingent upon** the Board's issuance of the Financial Activities Rule.[23] The plain language of Title I provides that the Council does not have the authority to issue recommendations for nonbank financial companies under section 120 or to designate a company as a SIFI until the Board issues the final Financial Activities Rule. Only after the final Financial Activities Rule is issued will the Council be able to apply the requirements established by the Board to determine whether particular companies do or do not qualify as nonbank financial companies.

By enacting sections 102(a)(6) and 102(b) of the DFA, Congress mandated a thoughtful, transparent process to establish the requirements for determining whether a company is predominantly engaged in financial activities. This requires the Board to comply with the requirements of the Administrative Procedure Act ("APA") and to issue and explain a proposed rule, to solicit public comment on the proposal, to

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[22] 77 Fed. Reg. 21494 (April 10, 2012) ("Board Supplemental Proposal").

[23] In its initial Financial Activities Rule proposal the Board made the following statement regarding the relationship between the Board's rule defining the term "predominantly engaged in financial activities" and the Council's ability to designate a company for supervision by the Board (a systemically important financial institution or "SIFI"):

> The Dodd-Frank Act requires the Board to issue regulations that *establish the requirements for determining if a company is "predominantly engaged in financial activities" for purposes of Title I of the Act* . . . Accordingly, the Board is requesting comment on a proposed rule that would establish these criteria and define these terms. The Board is requesting comment on the proposed rule at this time because the proposals *are relevant to the authority of the Council to designate nonbank financial companies* ***for supervision by the Board under section 113 of the Dodd-Frank Act.*** . . . The Board believes soliciting comment on the proposed rule at this time should facilitate public understanding of, and comment on, the Council's proposal, and allow the Council to consider potential designations of nonbank bank financial companies under section 113 promptly after the Council's rule is finalized.

Board Proposal, 76 Fed. Reg. at 7733 (emphasis added).

In its supplemental proposal the Board again acknowledged that "[t]he Dodd-Frank Act *requires the Board to establish the requirements for determining whether a company is 'predominantly engaged in financial activities'*", and noted that the Council is authorized to designate a company that is predominantly engaged in financial activities and that otherwise qualifies as a nonbank financial company if it meets certain requirements regarding its potential impact on financial stability. Board Supplemental Proposal, 77 Fed. Reg. at 21494-5 (emphasis added).

consider public comments and to issue a final rule. All of this must occur in accordance with the principles developed in court decisions under the APA.

Not a word in Title I of the DFA authorizes the Council to leapfrog the process mandated by Congress in section 102(b).[24] The Council's approach is all the more remarkable in that it would completely evade the APA rulemaking process required by Congress by declaring MMMFs to be nonbank financial companies without any attempt to establish the requirements for a company to be deemed to be predominantly engaged in financial activities in accordance with APA rulemaking requirements. The Council appears to believe that it has the authority to bypass the express will of Congress and completely ignore the process that Congress mandated for determining whether a company is predominantly engaged in financial activities.

For the reasons described above, we believe that the Council lacks the authority to issue section 120 recommendations with regard to any purported nonbank financial companies. The Council cannot do so ***unless and until*** a final and effective Financial Activities Rule is issued that supports a determination that a company or category of companies qualify as "predominantly engaged" in financial activities.[25]

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[24] *See e.g.*, *Portland Cement Ass'n v EPA*, 665 F.3d 177, 185-188 (D.C. Cir. 2011) (holding that it was arbitrary and capricious for the EPA to issue a pollution standard without first completing a rulemaking proceeding defining a relevant term that the EPA acknowledged could significantly affect the application of the pollution standard).

[25] The Council has not engaged in a rulemaking proceeding in regard to the process for issuing recommendations under section 120. The Council did engage in a rulemaking proceeding in regard to the process for designating companies as SIFIs. In the Council's final SIFI designation rule, the Council in fact recognized the essential role played by the Board's Financial Activities Rule in the SIFI designation process. It defines the term "U.S. nonbank financial company" to generally include a company that is (i) incorporated or organized under the laws of the U.S.; and

> (ii) "Predominantly engaged in financial activities," as that term is defined in section 102(a)(6) of the Dodd-Frank Act (12 U.S.C. 5311(a)(6)), *and pursuant to any requirements for determining if a company is predominantly engaged in financial activities as established by regulation of the Board of Governors pursuant to section 102(b) of the Dodd-Frank Act* (12 U.S.C. 5311(b)).

77 Fed. Reg. 21637, 21653 (April 11, 2012) (to be codified at 12 C.F.R. §1310.2) (emphasis added). Notwithstanding the plain language of the rule, the Council in the preamble to the final rule stated without explanation that it had the statutory authority to proceed with determinations under section 113 of the DFA prior to the adoption of a number of other rules, including the Financial Activities Rule. *Id.* at 21639. Language in the preamble to a regulation cannot override contrary language in the regulation. *See Wyoming Outdoor Council v. U.S. Forest Serv.*, 165 F.3d 43, 53 (D.C. Cir. 1999) (citing *Jurgensen v. Fairfax County*, 745 F.2d 868, 885 (4th Cir. 1984) (a preamble "does not enlarge or confer powers on administrative agencies or officers)).

1.2. The Council Fails To Support An Assertion That MMMFs Are Predominantly Engaged in Financial Activities

The question of whether being an MMMF is a section 4(k) financial activity is directly at issue in the Board's pending Financial Activities Rule. In the rulemaking proceeding, a commenter has repeatedly pointed out that the Board has never found that being an MMMF is a permissible financial activity under section 4(k) of the BHCA.[26] The Board's Supplemental Proposal contains a proposed appendix that lists activities that the Board considers to be financial in nature under section 4(k) of the BHCA as of April 2, 2012 ("Financial Activities List"), which does not take account of prudential limitations that the Board has imposed on bank holding companies' conduct of such activities.[27] The Financial Activities List does not include being an MMMF as a permissible financial activity under section 4(k) of the BHCA.[28]

Thus, even if the Board's proposed Financial Activities Rule was adopted as a final rule, it would not provide the Council with the authority to treat MMMFs as nonbank financial companies, and the Council would have no authority to issue the Proposed Recommendations to the SEC with respect to MMMFs.

The Council in the preamble to the Proposal devotes **one sentence** to the critical question of whether MMMFs are nonbank financial companies.

> The Council believes that MMMFs are "predominantly engaged in financial activities"[note 21] as defined in section 4(k) of the Bank Holding Company Act of 1956

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[26] *See* Letter to Jennifer J. Johnson, Board of Governors of the Federal Reserve System from John D. Hawke, March 30, 2011 at 7-9 ("Being or controlling a mutual fund has never been an activity permitted under Board interpretations of Section 4(c)(8) or 4(k) of the BHC Act" *Id.* at 9); Letter to Jennifer J. Johnson from John D. Hawke, May 24, 2012 at 4-6 (". . . the Board has not determined that an open-end investment company is a business that is financial in nature under the BHC Act nor has it permitted financial holding companies or their nonbank subsidiaries to own or control an open end investment company." *Id.* at 5 footnote omitted).

[27] Board Supplemental Proposal, 77 Fed. Reg. at 21502-5.

[28] The Board includes certain relationships between a bank holding company and an MMMF as permissible activities – "Organizing, sponsoring, and managing a mutual fund." *Id.* 77 Fed. Reg. at 21505 (Appendix A, clause 29). What it does not do is include actually being an MMMF as a permissible financial activity under section 4(k) of the BHCA.

> [note 22] and thus are "nonbank financial companies"
> [note 23] for purposes of Title I of the Dodd-Frank Act.[29]
> [Note 21] *See* 12 U.S.C. 5311(b).
> [Note 22] *See* sections 4(k)(1), 4(k)(4)(A), 4(k)(4)(D), and 4(k)(4)(H) of the Bank Holding Company Act (12 U.S.C. 1843(k)(1), 1843(k)(4)(A), 1843(k)(4)(D), 1843(k)(4)(H)).
> [Note 23] *See* 12 U.S.C. 5311(a)(4).

Remarkably, the Council in referring to the phrase "engaged in financial activities" cites to section 102(b) of the DFA (codified at 12 U.S.C. §5311(b)). This is the very provision on which Congress mandated that the Board issue regulations establishing the requirements for a company to be deemed to be predominantly engaged in financial activities. The Council ignores the language of Title I of the DFA, including section 102(b) requiring the Board to issue regulations establishing the requirements for a company to be deemed to be predominantly engaged in financial activities. It ignores the fact that the Board has been engaged in an extensive, ongoing, and controversial rulemaking proceeding under section 102(b) of the DFA since February 2011. And it ignores the fact that the Board's proposed Financial Activities Rule cannot treat being an MMMF as a financial activity under section 4(k) of the BHCA.

The Council appears to believe that it has its own independent authority in the absence of a final Board Financial Activities Rule to make *ad hoc* determinations as to whether a particular category of companies qualify as nonbank financial companies. As discussed above, the Council has no such authority.

Even on its own terms, the Council's "belief" that MMMFs are nonbank financial companies is wholly inadequate and without authority. The Council has not explained how it reached a determination that MMMFs meet the revenue or asset tests set forth in section 102(a)(6) of the DFA. Furthermore, the Council's mere unexplained citation to four subsections of section 4(k) of the BHCA does constitute a reasoned or adequate explanation for the Council's purported determination that MMMFs are nonbank financial companies.

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[29] Proposal, 77 Fed. Reg. at 69460.

None of the subsections of section 4(k) of the BHCA cited by the Council support the treatment of MMMFs as being predominantly engaged in financial activities:

- Section 4(k)(1) of the BHCA does not by itself cause any activity to be treated as a financial activity.[30]

- Section 4(k)(4)(A) of BHCA provides that the activities of lending, exchanging, transferring, investing for others or safeguarding money or securities are considered to be financial in nature.[31] The Council does not give any indication of which of the activities listed in this subsection the Council considers to be related to MMMFs.[32]

- Section 4(k)(4)(D) provides that issuing or selling instruments representing interests in pools of assets that a bank is permitted to hold directly is considered to be financial in nature.[33] As the Board has explained in the preamble to its Financial Activities Rule Supplemental Proposal this provision describes the activity of asset securitization.[34] MMMFs do not engage in this activity.

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[30] 12 U.S.C. § 1843(k)(1). Section 4(k)(1) provides that a financial holding company may engage in any activity, and may acquire and retain the shares of any company engaged in any activity, that the Board determines (i) to be financial in nature or incidental to such financial activity or (ii) is complementary to a financial activity and does not pose a substantial risk to the safety or soundness of financial institutions or the financial system generally. This provision does not identify any specific activities, but only incorporates activities that may be enumerated elsewhere. It does not by itself cause any activity to be treated as a financial activity.

[31] 12 U.S.C. § 1843(k)(4)(A).

[32] Commenters should not have to speculate as to which of the authorities listed in section 4(k)(4)(A) the Council might have in mind. Moreover, as the Council notes different types of MMMFs invest in different types of instruments. The Council fails to explain how any of these investments would fall within the scope of section 4(k)(4)(A). In particular, to the extent relevant, the Council fails to demonstrate that the Board has treated investments in government or private sector debt securities and related instruments as lending under section 4(k)(4)(A).

[33] 12 U.S.C. § 1843(k)(4)(D).

[34] Board Supplemental Proposal, 77 Fed. Reg. at 21497. In describing the activities listed in the proposed Financial Activities List, the Board summarized the activities conducted under authority of section 4(k)(4)(D) as "securitizing" and stated that "the [Gramm-Leach-Bliley] Act also imposed the condition that the *assets being securitized* must be permissible for a bank to hold directly." *Id.* (emphasis added).

- Section 4(k)(4)(H) is the merchant banking authority for financial holding companies.[35] The Council provides no explanation how MMMFs satisfy the requirements of that section, including that such shares or ownership interests be acquired as part of a bona fide underwriting or merchant or investment banking activity shares or ownership interests be held by a securities affiliate or an affiliate thereof.[36] Most significantly, the Council makes no suggestion that the Board has ever determined that the merchant banking authority serves as a basis for being an MMMF to be deemed to be a financial activity under section 4(k) of the BHCA.

Simply put, the Council has not satisfied its legal obligation to set forth a rational basis in the Proposal to establish that MMMFs are engaged in any section 4(k) activities justifying the conclusion that MMMFs are predominantly engaged in financial activities. Nor has it made any attempt to show how the volume or extent of any such purported financial activities would meet any applicable revenue or asset tests. The Council's purported treatment of MMMFs as nonbank financial companies is arbitrary, capricious and otherwise not in accordance with law. It is in excess of the Council's statutory jurisdiction and authority and fails to observe procedures required by law.[37]

2. <u>The Council Has Not Adequately Demonstrated That MMMFs Pose A Threat To Financial Stability To Justify Section 120 Recommendation</u>

In order to make recommendations under section 120 the Council must make a determination that the conduct, scope, nature, size, scale, concentration or interconnectedness of such activity or practice could create or increase the risk of significant liquidity, credit or other problems spreading among bank holding companies and nonbank financial companies, financial markets of the U.S., or low-income, minority or underserved communities.

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[35] 12 U.S.C. § 1843(k)(4)(H).

[36] The Council provides no indication as to whether it believes that government debt securities would be among the type of instruments that would fall within the scope of a purported application of the merchant banking authority to MMMFs.

[37] 5 U.S.C. §706.

We do not believe that the Council has satisfied its burden to make the required determinations in relation to either Prime or non-Prime MMMFs. The Council's generalized assertions regarding risks posed by MMMFs are not applicable to non-Prime MMMFs. Furthermore, the Council has not adequately demonstrated that Prime MMMFs are subject to destabilizing runs following the adoption of the SEC's 2010 MMMF Reforms and the Council has not adequately supported its assertion that Prime MMMFs' role in the short-term funding markets justifies the required determination.

2.1. The Four Types of MMMFs Identified By the Council

At a general level the Council makes the following assertion regarding the MMMF sector:

> [T]he conduct and nature of MMMFs' activities and practices makes MMMFs vulnerable to destabilizing runs which may spread quickly among funds, impairing liquidity broadly and curtailing the availability of short-term credit.[38]

In essence the Council argues that MMMFs present three types of threats that warrant a determination that MMMFs pose the types of threats that justify a section 120 recommendation.

> (i) MMMFs are structured in a manner so that they are subject to redemptions runs;
>
> (ii) redemption runs may be so severe that they may spill over into other MMMFs and that investors may have difficulty accessing their funds held in MMMFs; and

[38] Proposal, 77 Fed. Reg. at 69460.

(iii) an industry-wide run on MMMFs can reduce the availability of short-term credit.[39]

In making these assertions about MMMFs, the Council lumps together four separate and distinct types of MMMFs which the Council itself recognizes exist:

Treasury MMMFs—with about $400 billion in assets, which invest primarily in U.S. Treasury obligations and repos collateralized with U.S. Treasury securities.

Government MMMFs—with about $490 billion in assets, which invest primarily in U.S. Treasury obligations and securities issued by entities such as Fannie Mae, Freddie Mac and the Federal Home Loan Banks, as well as in repos collateralized by such securities.

Tax-Exempt MMMFs—with about $280 billion in assets, which invest in short-term municipal securities and pay interest that is generally exempt from state and federal income taxes.

Prime MMMFs—with about $1.7 trillion in assets, which invest more substantially in private debt instruments such as commercial paper and certificates of deposit.[40]

2.2. Any Analysis of the Risk of Significant Liquidity, Credit or Other Problems Must Be Done Individually With Respect to a Particular Category of MMMFs

The Council's own statements in the Proposal show that it is unwarranted and inappropriate to aggregate four types of MMMFs that have significantly different characteristics and histories as if they were a single unitary line of business. We believe that a proper analysis must look at each of the four categories individually and

[39] *Id.*
[40] *Id.* at 69457.

examine whether the Council has made a compelling case that a particular category of MMMFs poses risks that justify recommendations under section 120.

2.2.1. The Proposal Does Not Support An Assertion that Treasury MMMFs, Government MMMFs or Tax-Exempt MMMFs Create or Increase the Risk of Significant Liquidity and Credit Problems Spreading Among Financial Companies and Markets

The Council reviews three factors in reaching the determination that MMMFs generally could create or increase the risk of significant liquidity and credit problems spreading among financial companies and markets. These three factors are (i) the conduct and nature of the practices and activities of MMMFs, their sponsors and investors, (ii) the size, scale and concentration of MMMFs, and (iii) the interconnectedness of MMMFs with financial firms, the financial system and the U.S. economy. In this section we will review the application of these three factors to Treasury MMMFs, Government MMMFs and Tax-Exempt MMMFs.

Conduct and Nature of Practices and Activities. The Council argues that MMMFs are structurally vulnerable because they rely on valuation and rounding methods to maintain a stable NAV per share, which exacerbates investors' incentives to redeem their shares when there is risk that MMMF share prices will fluctuate. In the view of the Council a risk is created where an MMMF performs maturity transformation by offering shares that can be redeemed on demand while also investing in relatively longer-term securities.[41]

The Council's own discussion in this regard demonstrates why Treasury and Government MMMFs do not satisfy this element of the Council's generalized claims against MMMFs.

> MMMFs invest not only in *highly liquid instruments, such as* securities that mature overnight and *Treasury securities*, but also in short-term instruments that are less liquid, including term CP and term repo. In the event of shareholder

[41] *Id.* at 69461.

> redemptions *in excess of an MMMF's availability liquidity*, a fund may be forced to sell less-liquid assets to meet redemptions. In times of stress, *such sales may cause funds to suffer losses* that must be absorbed by the fund's remaining investors, further reinforcing the first mover advantage.[42]

This scenario simply does not apply to Treasury MMMFs.

The text of the Proposal itself notes that the run on MMMFs during 2008 was centered on Prime MMMFs. It concedes that during the week following the Lehman bankruptcy "government MMMFs" did not experience redemption runs.[43] Instead, "government MMMFs" attracted inflows of $192 billion during that period. Thus, the Proposal again demonstrates that general arguments about MMMFs as group do not apply to all categories of MMMFs. An argument about the susceptibility of Prime MMMFs to destabilizing runs cannot be transformed into an indictment against Treasury MMMFs or Government MMMFs where the empirical data for those types of MMMFs is to the contrary.

The Council clearly views the 2008 financial crisis as the critical event that provides strong support for significant reforms to the regulation and structure of the MMMF industry. Yet the Council's analysis of the events of 2008 disregards data that contradicts the grounds for making a recommendation with respect to Treasury MMMFs and Government MMMFs. It states that:

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[42] *Id.* (emphasis added).

[43] The Proposal does not indicate whether the phrase "government MMMFs" in this context is meant to apply only to Government MMMFs as described by the Council in the Proposal, or whether it includes both Treasury MMMFs and Government MMMFs as described by the Council in the Proposal. To the extent the Proposal refers only Government MMMFs, presumably Treasury MMMFs which hold a narrower highly liquid set of investments would have had a similar or better inflow of investment as Government MMMFs, thus making the same point applicable to Treasury MMMFs. Furthermore, the Proposal does not indicate whether the phrase "government MMMFs" in this context is meant to include Tax-Exempt Funds as described by the Council in the Proposal. Since Tax-Exempt MMMFs invest in state and local government securities it is reasonable to assume that the Council includes Tax-Exempt MMMFs within its reference to "government MMMFs." The lack of clarity by the Council on these important points demonstrates the Council's failure to give appropriate consideration of the characteristics of the four types of MMMFs for purposes of determining the Council's authority to issue section 120 recommendations with respect to each type of MMMF.

> Government MMMFs did not face similar vulnerabilities [as Prime MMMFs] at the time because they had significantly different portfolio holdings than the distressed prime funds and many government MMMF investments were appreciating in value.[44]

Rather than admit that it is fundamentally wrong to group Treasury MMMFs and Government MMMFs together with Prime MMMFs—even after acknowledging the dramatic difference between them during the 2008 crisis—the Council makes following assertion:

> Government MMMF *nonetheless may pose the same structural risks*, in that the funds' investors would have an incentive to redeem if they feared even small losses.[45]

Dismissing actual data, and replacing it with unfounded speculation does not amount to a legitimate and rational basis for a government determination to regulate an industry.[46] Furthermore, the Council has not even demonstrated that Prime MMMFs are prone to runs. Other than 2008, there have been no other "runs" caused by a default in a Prime MMMF portfolio.

Size, Scale, and Concentration. The Council argues that the size, scale, and concentration of MMMFs increase both their vulnerability to runs and the damaging impact of runs on short-term credit markets, borrowers and investors. The Council characterizes the MMMF industry as consisting of $2.9 trillion of assets.[47] It does so by including $890 billion of Treasury MMMF assets and Government MMMF assets

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[44] *Id.* at 69464.

[45] *Id.* (emphasis added).

[46] The Proposal goes on to note that during the last three business days of July 2011 outflows from "government MMMFs" totaled 7 percent of assets and exceeded as a percentage of assets outflows from prime funds. *Id.* The Council argues that this information shows that "government MMMFs" can be vulnerable to runs. It does not, however, suggest that "government MMMFs" had difficulty in dealing with the level of redemptions that they experienced. Assuming that "government MMMFs" did not have difficulty in dealing with the July 2011 redemptions, an open-minded governmental decision-making body would consider the implications of this information, which would appear to further undermine a concern that Treasury MMMFs and Government MMMFs are subject to destabilizing runs.

[47] *Id.* at 69462.

in this calculation, as well as $280 billion of Tax-Exempt MMMF assets. Yet as discussed above, by the Council's own statements there are differences in the risk profile of these types of MMMFs as compared to Prime Funds.

Interconnnectedness. The Council asserts that MMMFs' extensive interconnectedness with financial firms, the financial system, and the U.S. economy can create a significant threat to broader financial stability because the shocks from a run on MMMFs can rapidly spread to other entities throughout the financial system.[48] As discussed above, the Council itself is forced to recognize that concerns about destabilizing runs are not directed at Treasury MMMFs and Government MMMFs or presumably Tax-Exempt Funds. In the context of the interconnectedness factor such concerns cannot be a basis to find that any of these three categories of MMMFs should be subject to a determination that they create or increase the risk of significant liquidity and credit problems spreading across financial companies and markets.[49]

2.2.2. The Proposal Does Not Support An Assertion that MMMFs Create or Increase the Risk of Significant Liquidity and Credit Problems Spreading Among Financial Companies and Markets

2.2.2.1. The Council Does Not Adequately Support Its Assertion That MMMFs Structure Justifies A Determination That MMMFs Create or Increase the Risk of Significant Liquidity and Credit Problems Spreading Among Financial Companies and Markets

[48] *Id.* at 69462-3.

[49] In giving examples of the Council's concerns regarding the interconnectedness of MMMFs, the Council, among other things, cited the funding that MMMFs provide to non-governmental entities—which is a reference to Prime MMMFs, rather than to Treasury MMMFs, Government MMMFs or Tax-Exempt MMMFs which do not make such investments. The Council also contended that MMMFs may transmit risk to the broader economy as a result of their cash management role arguing that a widespread run on MMMFs could quickly pose liquidity problems for millions of investors. Again, the Council acknowledges that destabilizing runs are not associated with Treasury MMMFs, Government MMMFs or Tax-Exempt MMMFs. Finally, the Council expresses concerns that MMMFs are themselves highly interconnected because large Prime MMMFs generally provide funding to a relatively small group of firms with high credit quality. *Id.* at 69463. This consideration does not apply to non-Prime MMMFs by virtue of the types of investments they make.

The Council argues that MMMFs are vulnerable to runs principally because the stable $1.00 per share net asset value ("NAV") encourages "first movers" to redeem early when there is a risk that share prices will fluctuate. The Council also argues that MMMFs invest in securities with interest rate and credit risk but lack the capacity to absorb losses. It also states that MMMFs have historically relied on discretionary sponsor support. It further argues that MMMFs have attracted highly risk-adverse investors that are prone to redeem rapidly when losses appear possible.[50]

The Council focuses on the impact of the 2008 financial crisis on the MMMF industry and on the events related to the Reserve Primary Fund.[51] It acknowledges that the SEC's 2010 reforms to Rule 2a-7 ("2010 Reforms") were important and helped make MMMFs more resilient to certain short-term market risks and more transparent. Nevertheless, the Council asserts without any support that these reforms do not address what it considers to be the activities and practices of MMMFs that it believes makes them vulnerable to runs.[52]

The 2010 Reforms were made by the SEC—the agency that has decades of experience in overseeing the MMMF industry. The 2010 Reforms by any standard were broad and comprehensive. They included:

- Enhanced requirements regarding the quality of securities that may be held by MMMFs.
- Limitations on individual security maturity and on portfolio maturities.
- Diversification requirements on securities holdings.
- Liquidity requirements mandating minimum holdings of "daily liquid assets" and "weekly liquid assets" and limitations on holdings of illiquid securities.

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[50] *Id.* at 69461-2.
[51] *Id.* at 69463-4.
[52] *Id.* at 69464.

- Stress testing requirements.

- Enhanced disclosures by MMMFs to the SEC and to the public.
- MMMF board authority to suspend redemptions and liquidate the MMMF, upon notice to the SEC, if the MMMF has broken the buck or is in danger of breaking the buck.[53]

The Council in discussing the 2010 Reforms, among other things, argues that redemptions from many MMMFs during the 2008 crisis exceeded the daily and weekly liquidity requirements included in the 2010 Reforms.[54] This assertion ignores the fact that the 2010 Reforms imposed a general liquidity requirement on MMMFs which provides:

> (5) *Portfolio Liquidity*. The money market fund shall hold securities that are sufficiently liquid to meet reasonably foreseeable shareholder redemptions in light of the fund's obligations under section 22(e) of the Act . . . and any commitments the fund has made to shareholders . . .[55]

The Council speculates that MMMF outflows during the 2008 crisis period would have been considerably larger in the absence of unprecedented government interventions to support MMMFs and short-term funding markets.[56] The Council does not, however, address the potential impact on investor behavior and confidence if the 2010 Reforms had been in place in 2008.

The Council simply fails to demonstrate or in any way support the assertion that the 2010 Reforms did not adequately address concerns regarding MMMFs arising out of the 2008 financial crisis. The Council's observation that institutional Prime

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[53] *Id*. at 69458-9.
[54] *Id*. at 69464.
[55] 12 C.F.R. §270.2a-7(c)(5). Section 22(e) of the Investment Company Act provides that no registered investment company may suspend the right of redemption of any redeemable security for more than seven days, subject to certain exceptions.
[56] Proposal, 77 Fed. Reg. at 69465.

MMMFs experienced "heavy outflows" during the summer of 2011 does not support its conclusion that MMMFs' continue to be vulnerable to runs even after the 2010 reforms."[57]

Such assertion by the Council raises a fundamental issue as to the approach the Council is taking. All types of entities that hold customer funds may experience inflows and outflows of funds. Is the Council really taking the position that the mere outflow of funds is sufficient for it to find that an entity creates or increases the risk of significant liquidity and credit problems spreading among financial companies and markets? If that is the standard the Council is employing, its own Proposed Recommendations do not solve the problem. Nothing about any of the three alternatives proposed by the Council would prevent individual MMMF shareholders from deciding to redeem their shares in a manner or to an extent that the Council might characterize as a "run."

The Council's logic is further deprived of any persuasive force by its admission that in the case of the outflows in the summer of 2011, "MMMFs were able to withstand redemption pressures without further repercussions."[58] Thus, rather than supporting the Council's position regarding the purported threat that MMMFs pose to financial stability, the summer 2011 experience supports the efficacy of the 2010 Reforms and counsels against the need for dramatic new regulations.[59]

2.2.2.2. The Council Does Not Adequately Support Its Assertion That MMMFs' Role In the Short-Term Funding Markets Justifies A Determination That MMMFs Create or Increase the Risk of Significant Liquidity and Credit

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[57] *Id.*
[58] *Id.*
[59] In an indication of the Council's clear disposition against the MMMF industry, the Council characterizes the same summer 2011 outflows in two different ways in order to seek to support its policy objectives. In order to support its argument that the potential for MMMF runs is undiminished, the Council described the redemptions as "heavy outflows" yet in order to address the absence of an adverse impact of the "heavy outflows" the Council immediately downplays them, stating that there was no adverse impact because "the pace of outflows in 2011 was well below that experienced in 2008." Another way to look at the same data is that the implementation of the 2010 Reforms should be credited with the reduction in the level of redemptions between 2008 and 2011.

Problems Spreading Among Financial Companies and Markets

A significant element of the Council's argument that Prime MMMFs create the risk of significant liquidity and credit problems spreading among financial companies and markets is the assertion that problems at MMMFs could adversely impact parties that receive short-term funding from Prime MMMFs.

Size, Scale, and Concentration. The Council describes MMMFs as important providers of short-term funding to financial institutions, nonfinancial firms and governments. It states that MMMFs play a dominant role in some short-term funding markets. The Council states that MMMFs hold 44 percent of the U.S. dollar-denominated financial commercial paper outstanding and about 30 percent of all uninsured dollar-denominated time deposits. The Council also states that MMMFs provide approximately one-third of the lending in the tri-party repo market and also states that they hold significant (but unquantified) portions of the outstanding short-term securities issued by state and local governments, the Treasury and Federal agencies. The Council then states that:

> Given the dominant role of MMMFs in short term funding markets, runs on these funds can therefore have severe implications for the availability of credit and liquidity in those markets.[60]

Taking the Council's statements at face value it is difficult to understand how the Council broadly asserts that MMMFs have a "dominant role" in the short-term funding markets. This is because the Council takes a very different position in its discussion of the impact of the Proposed Recommendations on long-term economic growth ("Cost-Benefit Analysis").

Indeed, in its Cost-Benefit Analysis, the Council finds it useful to downplay the importance of short-term credit markets and the role that MMMFs play in them. Thus, it provides the following analysis:

[60] *Id.* at 69462.

> However, while MMMFs provide such financing through a variety of channels and play a *significant role in a number of credit markets* (as discussed in Section IV), the total credit that they supply is *relatively small* compared to aggregate nonfederal, nonfinancial debt.[61]

This statement puts the Council's results-oriented approach in sharp focus. It also undermines the credibility that any independent third party would ascribe to the strength of its purported determinations regarding MMMFs' potential to create significant liquidity and credit problems.

It appears that the Council sees an advantage to emphasizing the role of MMMFs in demonstrating that they have the capacity to cause significant liquidity and credit problems, describing them as playing a "dominant role" in certain short-term credit markets. In contrast, when the Council sees an advantage to minimizing the impact of MMMFs in the very same short-term credit markets, their "dominant role" suddenly retreats to a merely being a "significant role."

Similarly, in the Cost-Benefit Analysis, the Council ascribes a particular amount to the total direct and indirect credit provided by MMMFs to businesses, households, and state and local governments. It then downplays the importance of this activity by stating that, "[w]hile significant, this amount represented only 5 percent of the total debt outstanding of U.S. businesses, households, and state and local governments . . ."[62]

Moreover, in the Cost-Benefit Analysis, the Council states that there could be larger weighted-average costs of short-term funding if those markets were to become less liquid. However, the Council argues that the impact of an "increase in short-term rates on the weighted-average cost of capital would still be *minimal*, given the *small share of business, household, and state and local government debt that is short-term*."[63]

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[61] *Id.* at 69481. (emphasis added).
[62] *Id.*
[63] *Id.* at 69482.

In the Cost-Benefit Analysis, the Council also appears to suggest that there are readily available alternative sources of short-term financing if the role of MMMFs in such markets were curtailed. In the context of discussing the possibility that the Council's Proposed Recommendations could result in higher short term-borrowing costs, it suggests that such alternatives, without any explanation of what they would be, are available. Thus, the Council states, "[i]f substitution toward other sources of credit were considered, the estimated cost to economic growth likely would be smaller."[64]

Similarly, the Cost-Benefit Analysis states that "[t]o the extent that borrowers substitute away from the short term financing provided by MMMFs, for example, and sell short-term instruments directly to investors or to other types of cash-management vehicles, costs to long-term economic growth could be smaller."[65]

The Council posits a world in which it seeks to raise alarm that destabilizing runs on MMMFs will have dramatic negative consequences for short-term financing when it seeks to support its assertion that MMMFs pose significant liquidity and credit threats. Yet when required to address the impact of recommendations that could significantly decrease the availability of short-term financing from MMMFs, the Council suddenly envisions the presence of range of substitute sources of short-term financing that will provide sufficient amounts of credit at attractive rates.

These inconsistencies suggest deficiencies under the administrative standards required of such an important regulatory action by the Council. The credibility of the Council's various assertions regarding the basis for a determination of significant liquidity and credit risk based on the role played by MMMFs in short-term credit markets must be weighed in light of the Council's simultaneous assurances that such markets are relatively insignificant elements of the overall economy and that, in any event, there are readily available economically acceptable substitutes for the role currently played in such markets by MMMFs.

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[64] *Id.* at 69480.
[65] *Id.* at 69482.

3. **<u>The Council Did Not Satisfy the Requirement That It Consult With the SEC In Regard To the Proposed Recommendations</u>**

The Council has not adopted any regulations or procedures regarding how it will comply with the consultation requirements of section 120(b). The Council purports to have satisfied this requirement with the statement that "the Council has consulted with SEC staff."[66]

We do not believe that a conclusory statement that the Council has consulted with unidentified members of SEC staff without any indication as to the extent or substance of the discussion can be considered to comply with the requirements of section 120(b).

This matter does not arise in a vacuum. As the Council has noted, on August 22, 2012, then SEC Chairman Mary Schapiro announced that the majority of SEC Commissioners would not support seeking public comment on the SEC's staff proposal to reform the structure of MMMFs ("Staff Proposal").[67] On August 23, 2012, Commissioner Aguilar issued a statement regarding information he would want before he would be able to support an MMMF reform proposal. On August 28, 2012, Commissioners Gallagher and Paredes issued a statement in which they commented that the necessary analysis has not been conducted to demonstrate the efficacy of the reforms outlined in the Staff Proposal.

Under these circumstances a number of points are clear. First, the SEC staff is not able to act or speak on behalf of the Commissioners. Second, enough Commissioners were opposed to the Staff Proposal in order to prevent it from being approved for issuance. Third, multiple Commissioners are personally engaged in the complex issues related to potential MMMF reform. Fourth, in order for the SEC to adopt regulations that would implement any final recommendations that might be made by the Council to the SEC, a majority of the Commissioners would have to approve such an action.

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[66] *Id.* at 69457.
[67] *Id.* at 69459.

In view of the foregoing, good faith compliance by the Council with the requirements of section 120(b) would not be confined to consultation with SEC staff members who are not able to act on behalf of the Commission. It can only reasonably be attained by the direct consultation with each of the Commissioners.

4. The Council's Cost Benefit Analysis Does Not Meet the Requirements of Section 120(b)(1) of the DFA

Section 120(b)(1)(A) of the DFA requires the Council to take the costs to long-term economic growth associated with any proposed recommendations into account in developing the recommendations.

As noted above, the Council's Cost-Benefit Analysis is suspect because it conflicts with some of the critical assertions the Council makes to justify its recommendations. In addition, the Cost-Benefit Analysis set forth in the Proposal does not meet the requirements of section 120(b)(1)(A).

4.1. The Cost-Benefit Analysis Is Flawed Because It Does Not Clearly Distinguish As To the Impact on Long-Term Economic Growth Among the Three Distinct Alternatives Identified By the Council

The Council's Cost-Benefit Analysis contained in Section VI of the Proposal is defective because it does not adequately present an independent analysis of each of the three alternatives that the Council is proposing. There are significant differences in the key elements of the analysis of long-term economic impact of the three alternatives proposed by the Council. For example, investor interest in purchasing MMMF shares is likely to be impacted very differently by a move to a floating NAV under Alternative One. Alternative One would present legal, operational and business impediments to continued investor purchases of MMMF shares that would not arise under Alternatives Two and Three, which would not result in a move to a floating NAV.

The Council's Cost-Benefit Analysis mixes the discussion of the impact on long-term economic growth by agglomerating its discussion of different alternatives into an integrated cost-benefit discussion. This makes it difficult, if not impossible,

for commenters to clearly discern the analytical approach that the Council is taking and to evaluate and comment on its strengths and weaknesses. A section 120(b)(1)(A) compliant Cost-Benefit Analysis must clearly and separately present an independent, comprehensive analysis for each of the three alternatives.

4.2. Specific Cost-Benefit Analysis Deficiencies

4.2.1. The Cost-Benefit Analysis Does Not Adequately Address The Potential Decrease in MMMF Assets That Could Result From A Requirement For MMMFs To Use Floating NAV

Alternative One would require MMMFs to move to a floating NAV. In the Council's explanation of this alternative in Section V of the Proposal, it acknowledges the following impacts of such a move that could result in investors limiting or terminating their investments in MMMFs:

- Increasing complexity in tax reporting.[68]
- "Wash sale" rules would limit the extent to which a shareholder could deduct any loss realized on a redemption.[69]
- The possibility that floating NAV would not be treated as a cash equivalent under U.S. generally accepted accounting principles.[70]
- Operational costs for MMMFs to accommodate a floating NAV.[71]
- Loss of operational efficiencies associated with floating NAV.[72]
- Investors may be unwilling or unable to conduct their cash management through a vehicle that does not have a stable value.[73]

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[68] *Id.* at 69467.
[69] *Id.*
[70] *Id.*
[71] *Id.* at 69467-8. Investors that chose to continue to invest in floating-NAV MMMFs would also be subject to operational costs to adjust to a move to floating NAV.
[72] *Id.* at 69468.

- Investors may be prohibited by board guidelines or firm policies from using a vehicle that does not have a stable value.[74]

- Investors may be subject to statutory or regulatory requirements that permit them to invest certain assets only in funds that seek to maintain a stable value.[75]

The Council, taking note of all these factors, observes that they "may reduce overall investor demand for MMMFs, which would diminish the funds' capacity to invest in the short-term securities of financial institutions, businesses, and governments, possibly impacting their costs of funding."[76] The Council then acknowledges that "[e]limination of the stable NAV would be a significant change for a multi-trillion dollar industry in which the stable $1.00 share price has been a core feature."[77] It even suggests that if a transition to a floating NAV regime "prompted investors to redeem suddenly and substantially, the transition itself could create financial instability."[78]

With these critical issues acknowledged by the Council, one would surely expect that the Cost-Benefit Analysis would at a bare minimum present its evaluation of the potential likely reduction in MMMF investment resulting from the factors that the Council itself acknowledges. It would also be expected that the Council would present analysis as to where the funds exiting MMMFs would be invested. It must also address the extent to which investor movement to alternative cash-management vehicles would result in replacement financing being provided, and at what rates, by such alternative cash-management vehicles, particularly for the types of short-term financing discussed above. The Council should also present its evaluation of the impact a reduction in investor holdings of MMMFs would have on investments by MMMFs, particularly in short-term financing for businesses, financial institutions, and

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[73] *Id.*
[74] *Id.*
[75] *Id.* (footnote omitted).
[76] *Id.*
[77] *Id.*
[78] *Id.*

state and local governments. The Council's analysis is also inadequate to the extent it fails to address the extent to which investor movement to alternative cash-management vehicles would result in replacement financing being provided, and at what rates, by such alternative cash-management vehicles, particularly for the types of short-term financing discussed above.

The Council's lack of attention to this critical set of issues is striking. In its Cost-Benefit Analysis the Council states:

> [T]he adoption of Alternative One in isolation and hence a requirement that all MMMFs adopt a floating NAV, could prompt shifts by MMMF shareholders away from MMMFs to alternative *cash-management products that maintain stable NAVs*. Such a shift could reduce the expected benefits if the alternative products were vulnerable to runs.[79]

Similarly, the Council makes the following statements:

> Expected benefits could be diminished if investors switched to *alternative-cash management vehicles* because MMMFs become less attractive. If those *cash-management vehicles* are themselves vulnerable to runs and are also interconnected with other parts of the financial system, the benefits to long-term economic growth that result from mitigating the probability and severity of financial crises could be reduced. Nonetheless, the expected reductions in the probability or severity of crises associated with MMMF reform would imply a sizable net benefit in terms of higher expected economic growth, given the very large costs of financial crises on economic output. Moreover, the Council and its members intend to use their authorities, where appropriate and within their jurisdictions, to reduce or eliminate regulatory gaps to address any risks to financial

[79] *Id.* (emphasis added).

> stability that may arise from dissimilar standards for other *cash-management products* with risks similar to MMMFs.[80]

The Council's sparse Cost-Benefit Analysis discussion regarding Alternative One fails to deal with any of the basic and essential issues noted above.

- It provides no estimate or range of estimates for the expected reduction in size of the MMMF industry.

- It does not provide any indication of the types of cash-management vehicles that it expects would receive funds removed from the MMMF industry, or the relative breakdown of the placement of such transferred funds within cash-management vehicles or other entities.

- It does not provides estimates of the likely reduction in various types of investments by MMMFs, including particular types of short-term investments, that would result from the reduction in MMMF size resulting from investor response to a move to floating NAV.

- It does not provide estimates of the extent to which alternative cash-management vehicles would replace the reduction in the amount of financing provided by MMMFs and the impact that the estimated amount of replacement funds would have on the costs of financing available to businesses, financial institutions, and state and local governments.

In our view, these are obvious and critical issues that any good faith analysis of the long-term economic impact of Alternative One must address. The Council's failure to address and consider them demonstrates that it has not meet its obligation under section 120(b)(1)(A).

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[80] *Id.* (emphasis added).

The Council's statements raise another important issue —what are the alternative cash-management vehicles that the Council is referring to? Does the Council know? If it does, why does its Cost-Benefit Analysis not identify what they are? If it does not know what they are, how can the Council reasonably evaluate the potential for runs on such unspecified cash-management vehicles? Moreover, how can the Council be confident that the run risks associated with unspecified or unknown cash-management vehicles will be less serious than those associated with MMMFs? How can the Council be confident of its members' ability to address risks associated with alternative cash-management vehicles if these vehicles are unspecified or unknown?

This is a wholly inappropriate way of conducting a Cost-Benefit Analysis. The Council is obligated to transparently discuss the logical impact of Alternative One, including the alternative cash-management vehicle structures that it apparently anticipates. Failing to present economic estimates of the direct and collateral impact of the alternative does not meet the statutory requirements of section 120.

4.2.2. The Cost-Benefit Analysis Does Not Adequately Address The Impact Of The Alternatives On Short-Term Financing

The Cost-Benefit Analysis contains a discussion of the impact of Alternatives Two and Three on the rates at which MMMFs would lend to borrowers and consequent effects of higher borrowing costs on investment and other spending by U.S. businesses, households, and governments. The Cost-Benefit Analysis assumes that the establishment of NAV buffers would cause MMMFs to require higher returns on their investments in order to offset additional costs.[81]

The Cost-Benefit Analysis states that "the Council has assumed that borrowers will not shift borrowing away from MMMFs and as a result will be required to fully absorb this higher cost."[82] The Council goes on to comment that if MMMFs are not able to pass through their higher costs, and were forced to absorb some of the costs

[81] *Id.* at 69480.
[82] *Id.*

in the form of reduced profits for sponsors or lower yields for shareholder, the costs to economic growth through the borrowing-cost channel would be lower.

The Council has constructed a one-dimensional world in which its proposals may increase the costs to borrowers but do not decrease the amount of financing available from MMMFs. This discussion occurs in the context of NAV buffers under Alternatives Two and Three. The Council apparently makes the assumption that reduced profits for sponsors will have no impact on the willingness of MMMF sponsors to continue to serve in that role in a low interest rate environment of indeterminate length during which sponsors have experienced very low returns. The Council's analysis ignores the obvious possibility that under Alternatives Two and Three sponsors will no longer be willing to offer MMMFs and that financing will no longer be available at any rate from discontinued MMMFs. The Council's assumption that borrowers will always have funding from MMMFs available is clearly inconsistent with this possibility which should have been addressed in the Cost-Benefit Analysis.

This topic also illustrates the deficiencies related to the failure of the Cost-Benefit Analysis to independently and comprehensively analyze the long-term economic impacts of each of the three alternatives. The Council plainly recognizes that Alternative One could result in reductions in the size of MMMFs, even reductions that could be so significant that the Council suggests they could create financial instability. Yet, the Council's assumption in its Cost-Benefit Analysis is that the Proposed Recommendations will not result in a reduction in the availability of financing from MMMFs. This is plainly at odds with the Council's own view of the potential impact of Alternative One. As a result, a proper Cost-Benefit Analysis would have to include the impact of reduced MMMF size on the availability of financing to businesses, financial institutions and state and local governments, which was not done by the Council.

4.3 The Cost-Benefit Analysis Should Be Conducted Through The Lens Of The Primary Regulator

MMMF regulations lie within the jurisdiction of the SEC and it should be noted that in promulgating rules, the SEC has specific requirements regarding cost-benefit analysis that must be met for a rule to pass legal muster.

Under Section 2(c) of the Investment Company Act ("ICA"), in promulgating rules under the ICA that require consideration of the public interest, the SEC must consider whether the rule will promote efficiency, competition, and capital formation. In discharging these responsibilities, the SEC must "determine as best it can the economic implications of the rule it has proposed,"[83] and subject that analysis to public comment.[84] Blanket statements regarding the consideration of the effects on "efficiency, competition, and capital formation," are insufficient if the SEC fails to provide any estimates of the expected costs resulting from the regulations. As recently confirmed by the D.C. Circuit, this fails to satisfy the applicable legal standard.[85] In *Business Roundtable and U.S. Chamber of Commerce* the court determined that the SEC "failed adequately to quantify the certain costs or to explain why those costs could not be quantified; neglected to support its predictive judgments; . . . and failed to respond to substantial problems raised by commenters."[86]

Any recommendations by the Council to the SEC would, as the Council acknowledges, be expected to require a rulemaking proceeding by the SEC.[87] Accordingly, the proposals must be viewed in light of these special legal requirements that the SEC must follow. A failure to do so will not provide commenters with the information needed to assess a proposal that is constructed to pass legal muster. The Council's proposals should be viewed through the lens of the legal requirements the SEC must follow. Those requirements, however, are not taken into consideration by the Council. As currently drafted, we do not believe that the Council has provided commenters with information needed to assess the costs and benefits of the Proposed Recommendations and by extension could therefore not meet the legal requirements the SEC must meet in promulgating a regulation. The Council should provide stakeholders with an adequate cost-benefit analysis that includes a statement on the impacts of the Proposed Recommendations upon efficiency, competition and capital

[83] *See Chamber of Commerce v. SEC*, 412 F.3d 133, 143 (D.C. Cir. 2005).
[84] *See Chamber of Commerce v. SEC (Chamber II)*, 443 F.3d 890, 905 (D.C. Cir. 2006).
[85] *See Business Roundtable and U.S. Chamber of Commerce v. SEC*, 647 F.3d 1144, 1150 (D.C. Cir. 2011) (vacating SEC regulation because the SEC "did nothing to estimate and quantify the costs it expected companies to incur" under that regulation).
[86] *Id.* at 1148-49.
[87] Proposal, 77 Fed. Reg. at 69479.

formation. A failure to provide this critical information to the public distorts the legitimacy of the process and any rules that may be promulgated there under.

Conclusion

For the foregoing reasons, the CCMC believes that the Council has failed to meet the legal predicates, under Section 120 of DFA, needed to move forward with the recommendations and that the recommendations themselves may create economic and operational harm to business investment and cash managements strategies. In short, the recommendations may cause substantial harm without achieving the Council's desired benefits.

We stand ready to work with regulators on appropriate measures to promote financial stability.

Sincerely,

David Hirschmann

cc: The Honorable Elisse Walter, U.S. Securities and Exchange Commission
The Honorable Troy Paredes, U.S. Securities and Exchange Commission
The Honorable Luis Aguilar, U.S. Securities and Exchange Commission
The Honorable Dan Gallagher, U.S. Securities and Exchange Commission
Mr. Norm Champ, U.S. Securities and Exchange Commission
Dr. Craig Lewis, U.S. Securities and Exchange Commission