Via Electronic Submission

Financial Stability Oversight Council  
Attn: Amias Gerety, Deputy Assistant Secretary  
1500 Pennsylvania Avenue, NW  
Washington, D.C. 20220

RE: Proposed Recommendations Regarding Money Market Mutual Fund Reform  
Docket Number FSOC-2012-0003

Dear Mr. Gerety:

The Dreyfus Corporation ("Dreyfus") appreciates the opportunity to respond to the Financial Stability Oversight Council's (the "Council") recently published "Proposed Recommendations Regarding Money Market Mutual Fund Reform" (the "Proposals").

Established in 1951, Dreyfus is registered with the U.S. Securities and Exchange Commission (the "Commission") as an investment adviser under the Investment Advisers Act of 1940. Dreyfus manages over $270 billion in assets, including over $162 billion in 41 domestic money market mutual fund portfolios that are structured within the confines of Rule 2a-7 under the Investment Company Act of 1940 (the "1940 Act") and over $28 billion in two offshore, dollar-denominated liquidity funds (Irish-domiciled UCITS funds).

Dreyfus is a subsidiary of The Bank of New York Mellon Corporation ("BNY Mellon"). BNY Mellon, a global financial services company operating in 36 countries and serving more than 100 markets, is a leading provider of financial services for institutions, corporations and high-net-worth individuals, offering investment management and investment services worldwide.

Dreyfus appreciates the Council's critical role in monitoring the stability of the U.S. financial system and its corresponding desire to advance the discussion on money market fund regulation by publishing these Proposals. We also respect the Commission's role as the nation's primary securities regulator and we were pleased to learn about the Council's preference for the Commission taking the lead in matters of money market fund regulation. Thus, we hope our comment letter informs both the Council and the Commission in their respective deliberations. We thank the Council for the opportunity to share our views on this important topic.
A. Overview of the Basic Principles Underlying our Views on Additional Money Market Fund Regulation.

1. Systemic Regulation of Money Market Funds Should Be Tailored to Address the General Run on Risk that Defined the 2008 Financial Crisis.

The Council has placed substantial emphasis on the contribution of money market funds to destabilizing the U.S. financial system in 2008 when the evidence, in our view, suggests that the crisis was characterized more broadly by a general “run on risk.” As a result, we believe too much emphasis has been placed on stopping money market fund redemptions to the exclusion of considering how a money market fund’s structure and resiliency determines how it will perform in a time of crisis, and tailoring any further regulations accordingly.

2. Systemic Regulation of Money Market Funds Should Be Narrowly Tailored to Apply Only to the Types of Money Market Funds for which “Destabilizing” Risks Can Be Tangibly Demonstrated.

We believe deliberation over further money market fund regulation should be guided by a fair assessment of historical money market fund shareholder investment and redemption activity and whether or to what extent that activity contributed (or could contribute) to destabilizing the financial system. Thus, we do not believe that government and municipal money market funds should be subject to additional regulation. There is no historical evidence of destabilizing net redemption activity (if any net redemption activity at all) associated with these types of money market funds.

3. Systemic Concerns Can Be Reduced Through Enhanced Credit Risk, Higher Minimum Liquidity, and Daily Portfolio Transparency Requirements for Money Market Funds.

If further regulation is pursued, we believe the risk-limiting conditions under Rule 2a-7 can be enhanced to reduce various kinds of concentration and other credit risks and to increase portfolio liquidity, and we would couple these changes with required daily disclosure of portfolio holdings (“Daily Transparency”). We believe the combination of a lower overall risk profile and Daily Transparency would more effectively match portfolio construction with investor risk tolerance and would result in more stable and predictable investor behavior during a time of crisis characterized by a “flight to quality.”

We are mindful that money market funds with low default risk, low spread risk, and ample liquidity are best positioned to withstand a crisis. We believe that had prime money market funds been structured in September 2008 in the way many prime money market funds are structured today, and in an environment of industry-wide Daily Transparency, prime money market fund net redemptions would have been much lower. Accordingly, we respectfully urge the Council and the Commission to continue to consider the value of improving the resiliency of prime money market funds rather than seeking only to address the perceived “structural vulnerabilities” of money market funds with reform proposals that, in our view, would do more harm than good.

4. The Stable Net Asset Value Money Market Fund Should Be Preserved.

We believe maintenance of the stable $1 net asset value (“NAV”) money market fund is preferable to a shift to a floating NAV money market fund. Such a change would eliminate the
usefulness of the product without providing a disincentive for redemption activity. A floating NAV money market fund would be subject to a different kind of “first mover advantage” that could accelerate redemptions in a time of crisis. If a floating NAV cannot resolve one of the key structural vulnerabilities identified by the Council, then the benefits of preserving stable NAV money market funds should outweigh any benefits from their elimination.

5. **A Floating Net Asset Value and a Minimum Balance at Risk (“MBR”) Requirement Each Would Be Rejected by the Vast Majority of Money Market Fund Investors.**

We believe implementation of either of these alternatives would drive a considerable amount of assets out of money market funds. Surveys of money market fund shareholders and service providers including corporate treasurers, institutions, and cash sweep providers, among others, have indicated that a significant majority of invested assets would migrate away from money market funds to other cash management vehicles if a floating NAV were implemented. Similarly, we do not believe money market fund investors or their service providers (e.g., cash sweep providers) can be expected to support an MBR requirement that both severely hampers ready liquidity and poses prohibitive operational challenges.

6. **The Council Should Support the Commission Moving Forward on Money Market Fund Regulation and Suspend its Section 120 Process at this Time.**

To the extent the Council pursues issuing recommendations to the Commission, we hope the Council’s deliberations will be guided by the views expressed herein. However, the Council has noted (rightly, in our view), that money market fund regulation should be carried out by the Commission. Conflicting mandates can be detrimental to the regulatory process and we believe during the past year an array of conflicts prevented the Commission from effectively addressing money market fund regulatory issues. Thus, we respectfully request that the Council defer issuing recommendations on money market fund reforms to the Commission at this time. If the Council suspends its Section 120 activity at this time, we believe it will provide clarity to the regulatory process for the benefit of the industry and its millions of fund shareholders.

B. **An Alternate View of Run Risk Should Inform the Regulatory Debate.**

The Proposals Generally are Overbroad and Would Have Unintended Consequences. We understand from the text of the release published by the Council (the “Proposing Release”) that the Council has identified money market funds’ (1) lack of a loss absorption capacity and (2) susceptibility to runs due to a perceived, inherent first-mover advantage as “structural vulnerabilities” that pose systemic risks to the financial system. Further, we appreciate how proposals for capital requirements and floating NAVs logically might follow from characterizing money market funds as having these structural vulnerabilities. We also recognize how the ready liquidity intrinsic to open-end mutual funds would give rise to an MBR requirement or other kind of redemption circuit breaker to slow or halt redemption activity.

However, we do not agree with how the Council has advanced the concept of “run risk” in forming these Proposals, and we also believe implementation of these Proposals will have unintended consequences. To one degree or another, adoption of any one of these Proposals would compromise
the current utility of money market funds for millions of investors and ultimately drive considerable amounts of assets out of money market funds into other liquidity vehicles (e.g., bank deposits, offshore or other unregistered liquidity vehicles), the result of which would be to transfer systemic risk to alternate (and perhaps less regulated) venues within the financial system rather than reduce it in the aggregate. We believe there is a different interpretation of the 2008 financial crisis that is supported by evidence and that does not justify the extent to which these Proposals potentially compromise the utility of money market funds. We offer the following discussion in this regard.

The Proposals Reflect Undue Emphasis on Reserve Primary Fund’s Failure. We believe the Council has overemphasized the contribution of Reserve Primary Fund’s failure to the prevailing market and liquidity conditions during the financial crisis of 2008. This emphasis, in our view, has resulted in a regulatory response that is disproportionate to money market funds’ contribution to the financial crisis of 2008. We also believe that the way in which money market funds have been singled out for their role in the crisis has prevented consensus and resolution on additional money market fund regulation.

The Proposing Release detailed some of the events surrounding Reserve’s Primary Fund’s failure but, in our view, neglected also mentioning the most significant prevailing events and conditions in the financial system. The 2008 financial crisis commonly is associated with a subprime mortgage crisis, Lehman's bankruptcy, commercial and investment bank failures and acquisitions, and investment banks converting to bank holding companies under Federal Reserve Board authority. These were the destabilizing aspects of the 2008 financial crisis that coalesced into a historic liquidity crisis. In our view, it is apparent that the 2008 money market fund “run” was into an already illiquid and destabilized market and that the regulatory response should recognize money market funds’ redemption activity was only one of many factors contributing to the crisis.

1 The benefits of money market funds include their value as (a) a savings and cash management vehicle for retail and institutional investors alike and (b) part of the financial system’s capital formation process. As a cash management vehicle, money market funds provide liquidity, diversification, and ease of entry and redemption. They also provide convenience in terms of settlement and custody as well as professional investment management and credit research analysis (compared with direct investment in money market instruments). Money market funds also are an essential tool of capital formation for corporations (due to ease of placement of debt issuance) and short-term financing for federal and state governments.

We also note the significant amount of assets invested in money market funds by investors that require a AAA/Aaa-rated investment. Many money market fund investors are subject to either state law or charter requirements that permit the use of money market funds only for the investment of cash balances only if they carry the highest credit or principal stability rating (as applicable) from a Nationally Recognized Statistical Rating Organization (“NRSRO”). Implementation of a floating NAV or an MBR requirement, we believe, could result in money market funds losing those NRSRO ratings and, as a result, losing the assets invested in those funds that rely on such ratings for eligibility.

2 See infra, note 11.

3 To illustrate, we note passages in the Proposing Release (e.g., those on pages 4 and those on pages 24-25) that describe money market stresses and Reserve Primary Fund’s failure without providing any context other than Lehman’s bankruptcy. We believe such a focus is misplaced. Consider the broader circumstances surrounding Reserve Primary’s failure and, we believe, the seminal events that occurred on the same day Reserve Primary Fund broke the buck: (a) September 7th - the U.S. Government seized control of Fannie Mae and Freddie Mac; (b) September 15th - Lehman filed for bankruptcy, Bank of America agreed to buy Merrill Lynch, New York State authorized AIG using $20 billion from its own insurance subsidiaries to ease a financial crunch, and the DJIA dropped 500 points; (c) September 16th - the Federal Reserve loaned AIG $85 billion in exchange for an 80% ownership interest, Lehman went to bankruptcy court, and Reserve Primary Fund broke the buck; and (d) September 17th - banks stopped lending to one another, LIBOR was wildly volatile, the SEC banned naked short-selling, Washington Mutual was put up for sale, Morgan Stanley and Wachovia entered into merger talks, gold prices jumped 8%, and the DJIA dropped 450 points.
Because of this focus on Reserve Primary, we can understand why the Proposals seek to answer the question “How can a run on money market funds be stopped?” However, we believe the key lesson from 2008 is not that money market funds are susceptible to runs but that the financial markets are vulnerable to flights to quality, as 2008 represented, more than anything else, a historic flight from financial institutions broadly. Thus, the appropriate issue for regulators to address, we believe, is “How will a stable NAV money market fund perform in a time of historic market crisis?” We believe our proposals are appropriately tailored to respond to this issue, by not ignoring the importance of improving their resiliency during times of crisis. We believe more resilient money market funds offer a strong likelihood for reducing systemic concern during times of future crisis, while preserving the essential features of stable NAV money market funds and the benefits they offer to fund investors, to the capital formation process, and to the financial system overall.

C. Narrowing the Regulatory Debate to Appropriate Asset Classes.

Government (including Treasury) and Municipal Money Market Funds Should be Excluded from Consideration for Further Regulation. The Proposals apply to all types of money market funds, recognizing in some cases different applications to government and municipal money market funds (e.g., with respect to capital requirements). However, money market fund net redemption activity during the 2008 financial crisis does not support the Proposals applying to all types of money market funds.

We are aware of the generally higher net redemption volume experienced by institutional prime money market funds in 2008, but shareholders invested in government and municipal money market funds did not demonstrate the same kind of behavior. Dreyfus' institutional prime money market funds experienced net redemption activity in line with industry averages, but its institutional government and institutional treasury funds generally experienced high levels of net inflows and its institutional municipal funds, to the extent they experienced net redemption activity, did so at rates at a fraction of that of prime funds. Dreyfus' retail prime money market funds also experienced stable to marginal net redemption activity while assets in its other retail money market funds generally were stable. These flows also were in line with industry experience. Nevertheless, the Proposals seek to regulate products that did not evidence systemic risk concerns through their net redemption patterns during times of market stress. Accordingly, we do not support pursuing any further money market fund regulation for government or municipal money market funds, and we respectfully urge the Council to consider all data submitted by commenters in this regard when deliberating further on the scope of these Proposals.

Distinguishing Between Institutional and Retail Prime Money Market Funds. We are aware that certain commenters, as well as the Council and the SEC, have raised the notion of regulating institutional and retail money market funds differently. We note that the proposed amendments to Rule 2a-7 in 2009 contemplated different minimum daily and weekly liquidity requirements for retail and institutional money market funds, but most commenters opposed this on the basis that they would have difficulty distinguishing between money market funds within their respective fund families for purposes of the Rule. We wrote in our 2009 comment letter that we thought classifying funds as

---

4 In 2009, the Commission requested comment on higher liquidity percentage requirements applying to institutional money market funds compared with retail money market funds. The proposal provided that fund boards could determine which of the money market funds in their fund family would be classified and thus regulated as institutional or retail. Commenters broadly opposed the proposal, in part, due to the perceived difficulty in distinguishing between the types of funds. The proposal was not adopted, in part, because the Commission could not satisfactorily make this distinction within Rule 2a-7.
“institutional” or “retail” would not be a difficult task, except we noted that “sweep” money market funds are not consistently classified solely as institutional or retail across the industry.

We continue to believe that funds can be classified readily as retail or institutional. However, if regulators pursue divergent regulation of institutional and retail money market funds, we do not support classifying “sweep” assets as “institutional” because they did not experience anything close to the same level of net redemption activity seen with institutional direct assets. There is ample evidence to demonstrate that sweep account investors using prime money market funds behaved much more like retail direct investors during the 2008 financial crisis. The account balances of these investors generally were stable over this time. Net redemption activity, if any, was at a fraction of that experienced in institutional direct investment accounts. The unresolved issue, then, would be how to handle “mixed” funds (that is, those having both institutional direct and cash sweep investment accounts). In this case, we believe that money market fund sponsors (given appropriate lead time) would want to pursue alternatives to segregate these investments, such as reorganizing such “dual purpose” prime money market funds that are constituted with a mix of institutional direct and sweep assets into a master-feeder structure that would accommodate a fixed and a floating NAV feeder option within one “master” portfolio.

Also, while institutional investors can pose different redemption risks than retail investors, institutional and retail prime funds generally have similar credit risk profiles. Within fund families, it is not uncommon for institutional and retail funds to be managed similarly from the perspective of weighted average maturity and credit risk. Thus, while it can be expected that different kinds of prime money market funds may experience different levels of redemption activity, it may not be the case that different kinds of prime money market funds have different credit risk profiles. Accordingly, establishing different regulations for prime money market funds solely on the basis of their respective redemption risk may not be the complete or most direct answer to systemic concerns.

D. **Dreyfus Supports Substantive Amendments to Rule 2a-7 that Would Enhance Money Market Fund Performance During Times of Market Crisis.**

We believe the measures discussed below for enhanced portfolio risk and liquidity management, as well as Daily Transparency, would be effective in preserving money market fund stability during times of market stress. We also recognize that prime money market funds can have very different risk profiles, which are not readily apparent to investors, based on how the adviser executes on its “minimal credit risk” determination. We believe that our proposals could improve investor awareness of the risks associated with prime money market funds that are not readily apparent to the investor from Rule 2a-7 construction or the fund’s prospectus.

---

5 Rule 2a-7(c)(5) provides that a money market fund will hold securities that are sufficiently liquid to meet reasonably foreseeable shareholder redemptions. This “General Liquidity Standard” under Rule 2a-7 and its associated “Know-Your-Customer” (“KYC”) procedural requirement generally work to address the potential for different kinds of funds to experience different levels of redemption activity.

6 Rule 2a-7(c)(3)(i) provides, in pertinent part, that a money market fund must limit its portfolio investments to those that the fund’s board determines present minimal credit risks. The Rule, however, does not provide a definition of the minimal credit risk standard, but rather explains it by reference to what would not satisfy the standard. The application of the minimum credit risk requirement explains, for example, why one money market fund might have (high) exposure to the banks of one country while another may have low or no such exposure.

We believe there is room within Rule 2a-7 for a risk management overlay that further refines the credit and liquidity risk profile of prime money market funds. Such refinements would result in money market funds with more stable asset bases in times of market crisis. We believe this would take the form of new portfolio diversification requirements directed at concentration risks (e.g., in asset-backed securities, or in long-maturity securities, or non-dollar, "sovereign" risk or country risk of the kind experienced during the 2011 Eurozone crisis) that would complement existing issuer diversification requirements. We also support measures designed to lower "spread risk" by, for example, reducing the maximum final maturity on individual securities to something less than 13 months.\(^7\)

Our approach seeks to address the risk factors intrinsic to prime money market funds, such as issuer or geographic diversification and concentration in financial and sovereign issuers. For example, recent events have made clear that concentrations in both sovereign and corporate credits pose special risks to prime money market funds. In 2008, during a run on domestic corporate and financial institutions broadly, prime funds were susceptible to market stresses because of their overall exposures to these entities. The 2008 financial crisis also showed how exposure to longer-maturity investments could create credit and liquidity problems during time of heavy redemption activity, as the spreads on those securities widened dramatically. While the 2010 amendments to Rule 2a-7 shortened weighted average maturity, the amendments did not shorten the maximum time to maturity for single investments, meaning that prime funds are subject to spread risk on individual holdings to the same extent as before 2010. In 2011, prime funds showed their sensitivity to European bank exposures during the Greek/Eurozone crisis, while domestic corporate credits during that time became almost a safe haven from such risk. As a result, it became clearer that sovereign issuers presented risks different from corporate issuers.

We also believe there is room for higher minimum allocations to Daily Liquid Assets and Weekly Liquid Assets under Rule 2a-7 without compromising effective portfolio construction. In our 2009 comment letter on the proposed amendments to Rule 2a-7, Dreyfus was one of the very few fund companies that supported the proposed 10%/30% liquidity percentages. We also believe that higher liquidity equates with higher resiliency to market and economic stresses and that higher resiliency means less systemic impact arising from having to satisfy unusually high net redemption activity during periods of market stress or illiquidity. Similarly, the perceived destabilizing effect of the "first mover advantage" only should be a concern to the extent that money market funds cannot manage the associated redemptions organically with liquid investments and intelligent maturity management. During this time of historically low interest rates, we believe this is of particular importance as money market funds appear to continue to serve the interests of investors as liquidity vehicles.

Prudent management of prime money market funds currently reflects consideration of all of these factors. Money market funds that are more diversified geographically and across financial institutions,\(^8\) that pose lower spread risk, that are sensitive to headline risks, that minimize exposure to

---

\(^7\) We do not support reducing the maximum weighted average maturity or weighted average life to maturity below 60 or 120 days, respectively. We do not believe this is necessary to reduce credit or spread risk in a time of crisis and otherwise could unduly restrict effective portfolio management.

\(^8\) We would note that the analysis of concentration risk among financial institution exposures should distinguish between exposures due to repurchase agreements, bank certificates of deposit, and time deposits, and exposure related to commercial
risks that are more difficult to quantify (e.g., structural risks related to ownership of extendible securities), and that otherwise more conservatively apply their minimal credit risk determination, we believe, can be expected to be safer and more stable investments during a time of crisis. Accordingly, we believe the Council and the Commission should further study ways that these aspects of managing prime money market funds can be reflected in Rule 2a-7.

Dreyfus’ experience in managing prime money market funds through the 2008 financial crisis, the implementation of the 2010 amendments to Rule 2a-7, and the Eurozone crisis of 2011 evidences that the funds can be managed conservatively but effectively for the benefit of investors while offering an overall risk/reward profile that would withstand future market crises. Establishing such an investment approach within Rule 2a-7 should offer sufficient stability to money market funds to answer the Council's concern about their systemic impact.

2. **Dreyfus Supports Amending Rule 2a-7 to Require the Daily Disclosure of a Money Market Fund’s Schedule of Investments.**

Since April 2007, Dreyfus has disclosed on www.dreyfus.com on a daily basis the Schedule of Investments for each Dreyfus money market fund. We decided to disclose portfolio holdings daily for client-servicing purposes to facilitate due diligence inquiries from fund shareholders on portfolio composition issues on a real-time basis in a manner consistent with applicable law. Institutional investors in particular are keenly aware of risk of loss in their money market fund investments. As part of their due diligence, they regularly analyze Dreyfus fund portfolio holdings for credit, issuer, liquidity, and counterparty concerns, among others.

Investor due diligence has become the norm because, despite the objective, risk-limiting conditions provided under Rule 2a-7, prime money market funds can have markedly different credit and liquidity risk profiles. These different risk profiles reflect how the manager makes its minimal credit risk determination under Rule 2a-7. As a result, there are aspects of portfolio construction that are not readily accessible to the money market fund investor. For example, a money market fund can utilize repurchase agreements on a daily basis but the fund’s counterparty risk, which reflects the manager’s credit review process, is not readily apparent to investors without specific disclosure.

Daily Transparency helps reveal a fund’s credit and liquidity risk profile and matches risk tolerance with portfolio construction. While there may be concern that Daily Transparency could precipitate a run in time of crisis, we believe that Daily Transparency funds more likely will have stable and predictable asset base during times of market crisis.

We also believe this practice gave Dreyfus a unique insight into institutional investor redemption activity in September 2008. We became aware that the broad credit concerns overwhelming the market were driving investor redemption activity rather than Reserve Primary Fund’s failure. In fact, we believe that the 2008 financial crisis might have unfolded in much the same way even if Reserve Primary Fund hadn’t broken the buck, because the flight to quality would have continued unabated. We also believe this unique access to institutional customers more effectively facilitates applicable know-your-customer obligations under Rule 2a-7 because institutional customers’ risk tolerance and liquidity needs are more clearly matched with portfolio construction.

---

paper and asset-backed securities holdings. Our views are influenced by the critical supply financial institutions provide for daily liquidity sources for money market funds.
Dreyfus and other money market fund sponsors recently announced that they would disclose their respective funds’ market-based NAVs on a daily basis. We began posting these values on www.dreyfus.com on February 1, 2013. However, we do not believe that disclosure of the market-based NAV, by itself, provides a meaningful representation of portfolio construction. We made the decision to post the market-based NAVs as a complement to our current disclosure of the Schedule of Investments for each Dreyfus money market fund. We recognize, though, that the market-based NAV is a lagging indicator, useful as an after-the-fact measure of portfolio construction and performance in the prevailing environment. More importantly, the market-based NAV does not help to distinguish the potential risks embedded in different money market funds. We believe that if the goal of transparency is to match risk tolerance with portfolio construction, then disclosure of market-based NAVs alone does not achieve that result. Thus, we continue to support daily disclosure of the Schedule of Investments.

E. **Dreyfus Does not Support Floating the Net Asset Value of Money Market Funds.**

We do not support floating the NAV of money market funds for two reasons. First, we do not believe that a floating NAV answers the systemic concern regarding run risk because it would not reduce run risk during times of market stress. To the contrary, we believe a floating NAV only changes the circumstances associated with money market fund redemption activity, because the floating NAV only changes the perceived first mover advantage from one which seeks to avoid redemptions at other than $1 to one that seeks to avoid drained portfolio quality and liquidity and steepening capital losses. In fact, a floating NAV could accelerate the magnitude and length of redemption activity because of the greater loss potential associated with this structure compared with a stable NAV fund. Secondly, we believe the floating NAV option poses the risk of unintended and undesirable systemic consequences.

The First Mover Advantage Associated with Floating NAV Money Market Funds. Within the context of a stable NAV structure, we acknowledge the regulatory concern over the risk of a money market fund breaking the dollar share price initiating destabilizing redemption activity and for “the investor left behind” in a break the buck scenario. We can see how proponents of a floating NAV would think that by eliminating the “dollar put” associated with stable $1 NAV money market funds, the incentive to be a first mover would go away. However, the floating NAV only changes the perceived first mover advantage, because there remains the incentive to redeem from the portfolio before liquidity drains away, credit risk increases, and losses deepen. No different than with a stable NAV money market fund, the floating NAV money market fund would meet redemptions first by selling off its “liquidity,” meaning that in the short-term its “credit risk” becomes a larger percentage of its portfolio. However, with no structural bottom in place, and the fund continuing to transact business, the pace of redemptions could both accelerate and lengthen as portfolio liquidity is drained and the risk of principal loss heightens. Accordingly, a floating NAV should not be expected to relieve market stress during times of illiquidity because investors, in our view, will not be less likely to move out of a cash management investment vehicle under such conditions solely because the “dollar put” no longer exists.

---

9 The redemption activity of variable NAV money market funds in Europe, as well as “enhanced income” funds in the U.S., has been well documented and it should be clear that these kinds of funds are neither shielded from market illiquidity nor significant redemption activity during times of market crisis.

10 A floating NAV also could give investors a false sense of comfort that their redemption order would be processed at their expected NAV (e.g., not accounting for the closing NAV on the day of a redemption order reflecting a significant percentage decline from the prior day’s closing NAV).
If the perceived first mover advantage associated with cash management investing is not exclusive to the stable NAV money market fund, there might be a temptation to attach a liquidity gate to a floating NAV. We would strongly oppose such an approach. The floating NAV has been proposed to address the perceived first mover advantage as described by the Council, but combining it with gating acknowledges that the floating NAV does not resolve such first mover advantage. A floating NAV would have a transformational impact on money market funds (as it would be implemented at the expense of the utility of money market funds as cash management vehicles). Therefore, at minimum, a floating NAV should not be pursued unless regulators are convinced that, by itself, the floating NAV resolves the systemic concern at issue.

Unintended Consequences and the Redistribution of Systemic Risk. We have noted that floating the NAV would compromise the utility of stable value money market funds as a cash management vehicle of choice for millions of investors. If money market funds no longer serve as a cash management vehicle of choice, we believe regulators can expect liquidity, particularly that which is subject to "flights to quality," to find its home elsewhere in the financial system.\footnote{We note the Council's statements in the Proposing Release that it would pursue systemic risk associated with cash management activity across the financial system. However, do not believe that the Council intended to advance the floating NAV proposal with the understanding that it would shift rather than alleviate systemic concerns.} Assets can be expected to migrate promptly to bank deposits, or offshore or to unregulated collective investment vehicles (and even bank deposits would not be insulated from flights to quality if the banking system came under stress). In support of this view, we ask the Council to consider a 2009 Dreyfus survey which concluded that approximately two-thirds of institutional investor assets would leave the Dreyfus money market funds if the funds floated their NAVs.\footnote{In our September 8, 2009 comment letter to the Commission responding to the first round of proposed Rule 2a-7 amendments, we described the results of a survey of our 37 largest institutional money market fund shareholders (at the time, representing approximately $60 billion in money market fund investments) regarding the option of a floating NAV. Among the responses were these: (a) 86% responded that a stable NAV is "very important" to them; (b) 67% responded that they would seek an alternative investment option to a floating NAV money market fund; and (c) 25% responded that they would utilize insured bank deposits as the investment alternative (28% responded they were undecided at the time). The percentages cited reflect shareholder assets meaning, for example, that one could conclude that $40 billion of the $60 billion in assets surveyed would migrate away from Dreyfus money market funds if such funds convert to a floating NAV from a stable NAV.}

The risk of losing fund shareholders is among the highest, for example, in the cash sweep business, which is driven by technology and currently unencumbered by technical tax and accounting issues. The cash sweep function is a critical part of daily liquidity management for retail and institutional investors alike, and the floating NAV money market fund poses severe obstacles to that line of business. As noted elsewhere in this letter, we have also described the utility of stable NAV money market funds for certain kinds of investors (e.g., municipalities subject to state laws or charter requirements, FCMs and DCOs, etc.) that, by charter or regulation, require a rated or otherwise statutorily constructed fund that may no longer meet such requirements under a floating NAV structure.

Amortized Cost is not a Fiction. We also disagree with the view that a floating NAV should be adopted because it reveals the "true value" of a money market fund, while the $1 NAV is somehow a "fiction" that should be abolished. The view that a stable $1 NAV does not reflect true value, which is attributable to money market funds using the amortized cost method to calculate daily net asset values,
is contrary to years of established accounting practice. In this regard, we would refer the Council to the white paper recently published by the U.S. Chamber of Commerce which provides an informative summary of the history of the amortized cost method and its applicability to money market funds. We also question if there would be any investor benefit to having money market fund transactions executed at dollar amounts that reflect tiny fractional deviations from one dollar.

If the floating NAV becomes the regulatory option of choice, we would urge that (a) it apply only to prime money market funds only; (b) to the extent there is a distinction made between institutional and retail money market funds, cash sweep assets be recognized and classified as retail assets; (c) its proposal be preceded by the satisfactory resolution of all applicable tax and accounting issues that would address some of the genuine reasons for investor rejection of floating NAV funds as cash management vehicles; and (d) this alternative be adopted with other alternatives acceptable to the industry and to investors that would preserve the stable NAV. However, to reiterate, we believe a proper vetting of the floating NAV option requires recognition that systemic risk associated with ready liquidity would shift rather than decline.

F. **Dreyfus Does not Support a “Minimum Balance At Risk” Requirement for Money Market Funds.**

We do not support the “minimum balance at risk” (”MBR”) requirement, alone or in combination with any other proposal, as it is unworkable for money market fund sponsors and service providers. If implemented, the MBR would be broadly rejected by money market fund investors and assets would leave money market funds permanently and perhaps to an even greater extent than from implementing a floating NAV.

We believe the MBR would be rejected in principle by money market fund investors because it is antithetical to the notion of ready liquidity and otherwise would require those investors to bear a corresponding loss burden that other investors would not have to bear. Secondly, the MBR poses

---

13 We note the Council’s proposal to set the NAV of a floating NAV money market fund at $100, ostensibly to better illustrate to investors the risk of loss associated with money market funds. If a floating NAV is pursued as a regulatory option, we would strongly oppose setting the NAV initially at $100. A $100 NAV, in our view, would exaggerate the tiny fluctuations “from par” that money market fund typically experience on a daily basis.

14 We refer the Council to the Fall 2012 report entitled “Amortized Cost is “Fair” for Money Market Funds” that was issued by the U.S. Chamber of Commerce’s Center for Capital Markets Competitiveness. In summary, the report concludes as follows:

"This paper shows that the use of amortized cost by money market mutual funds is supported by more than 30 years of regulatory and accounting standard-setting consideration. In addition, its use has been significantly constrained through recent SEC actions that further ensure its appropriate use. Accounting standard setters have accepted this treatment as being in compliance with generally accepted accounting principles (GAAP). Finally, available data indicate that amortized cost does not differ materially from market value for investments industry wide. In short, amortized cost is “fair” for money market funds."

15 We appreciate the Council’s recognition of the fact that an MBR requirement could impact the eligibility of money market funds for investment by derivative clearing organizations and futures commission merchants pursuant to the conditions of CFTC Rule 1.25 that otherwise authorize DCOs and FCMs to investment customer margin in money market funds provided certain conditions are met, including a commitment to 1-day delivery of proceeds (absent certain emergency circumstances). This is another example of the kind of money market fund investor, like those who rely on money market funds because of their AAA/Aaa NRSRO ratings (see note 1 above), whose assets could permanently migrate from money market funds is their utility is compromised or eliminated.
significant technological and operational challenges so burdensome that it likely would cause money market fund sponsors and providers to pursue other options for liquidity management. Thirdly, we have noted the significant role of "sweep funds" in the money market fund industry. These funds are attached to third-party intermediary platforms, thus requiring the intermediary to build and maintain the technology to support a redemption holdback. We cannot expect that intermediaries will build out this capacity, even if vendors introduce applicable software packages, because of the time and cost involved in accommodating this operationally, when more convenient alternatives are available. By comparison, intermediaries generally do not collect otherwise applicable redemption fees on investors' transactions in bond and stock mutual fund shares held in omnibus accounts because intermediaries choose not to bear that operational burden.

There also is valid concern for applicable state law requirements and mutual fund corporate charter provisions that could prohibit the redemption holdback feature of the MBR. Mutual fund corporate charters generally contain provisions that "redemption requests will be honored at net asset value," which means, in the context of an MBR, that a redemption request would not be honored if a holdback was applicable. Corporate charter provisions generally are reflective of applicable state law and likely would require fund shareholder votes to amend to accommodate a holdback, something that cannot be reasonably expected to be obtained. We are aware that other commenters have provided more detailed discussions of this aspect of the MBR proposal and we respectfully urge the Council to take such views into consideration in its deliberations.

To the extent the MBR becomes a regulatory option of choice, we urge regulators to work with the money market fund industry to address the significant legal and operational obstacles posed by this approach and otherwise craft it in a manner that would accommodate money market fund investors and the maintenance of a stable $1 NAV money market fund product. For example, consideration could be given to such ideas as increasing the minimum redemption amount from $100,000 to something more like $10 million (or more) and combining that with application of "frequent trading" principles that would apply some kind of limitation on assets traded within some number of days (e.g., 30 days). We believe it is important for regulators to recognize that a 3% holdback is significant. For example, a $10 million redemption could require a $300,000 holdback - again not an insignificant amount. By comparison, we note that an appropriately structured liquidity gating mechanism (which we discuss below) would be less onerous than an MBR requirement and could achieve a more definite result in a time of crisis.

G. Capital Requirements for Money Market Funds.

Capital requirements preserve some of the essential elements of money market funds, including the stable $1 NAV and ready liquidity. Further, capital buffers generated from sources other than the withholding of dividend income (which we do not support) can be built without reducing the level of current income generated for shareholders. Capital also can provide some loss-absorption capacity, but would have to be significant to absorb defaults.

However, capital requirements can be prohibitive. Capital requirements set at prohibitively high levels (which levels likely would vary from sponsor to sponsor) could constrict the industry, just as we believe the Council's other proposed alternatives have the potential to do. The Proposals contemplate a significant up-front and ongoing capital commitment. For example, using the calculation (including liquidity assumptions) in the Proposing Release, which determines that a 2.51% buffer would be required for the average prime money market fund, a fund sponsor with a $50 billion prime money
market fund family could be obliged to commit $1.25 billion in capital to support the buffer - again, not an insignificant amount. During extended periods of historically low interest rates and current yields, the consistent, cost-effective implementation of capital requirements would be a challenge to maintain. The impact to shareholders and to fund sponsors related to generating $1.25 billion in undistributed dividend income, or in committing $1.25 billion in capital to a subordinated money market fund share class for purposes of creating and maintaining a buffer would be high, particularly in the current low yield environment, and with respect to an investment where the likelihood of default is very low.

Ultimately, capital could be a difficult long-term solution to implement uniformly across the money market fund industry if not established at reasonable, cost-effective levels. Thus, to the extent capital requirements become a regulatory option of choice, we believe they would have to be offered at a more cost effective level than reflected in the Proposals. In our view, establishing capital buffers at such lower levels is not unreasonable given that capital requirements would be combined with other measures designed to promote or preserve stability.

Finally, as a technical matter, and consistent with the Council's position that greater liquidity can reduce capital requirements (as evidenced by the formulas underlying Alternatives Two and Three as proposed), we believe a prime money market fund's allocation to Weekly Liquid Assets, in addition to Daily Liquid Assets, is appropriate to include in the calculation of capital requirements. While money market funds strive to deliver redemption proceeds by the next business day, money market funds (like other kinds of mutual funds) have the ability to deliver redemption proceeds within seven days of the effective date of the redemption order. In addition, money market fund managers monitor allocations to Weekly Liquid Assets as well as to Daily Liquid Assets in furtherance of applicable know-your-customer obligations. Thus, money market fund liquidity on an overall basis is properly considered within a seven-day time horizon and not merely within a one-day time horizon.

H. Dreyfus Would Support Choice in Options Between Floating NAVs and Capital Requirements.

We appreciate the Council recognizing that the Proposals do not have to be considered on a mutually exclusive basis. Thus, if regulators adopt new regulations only from one of the three proposed alternatives, we favor having the flexibility to either implement a floating NAV or a capital buffer (with the corresponding choice of "additional measures" aimed at reducing redemption activity), as determined appropriate by a fund's boards of directors in the exercise of its business judgment. We support in principle the notion that money market fund sponsors and their affiliated fund boards of directors can make the determination to pursue the best approach for their fund shareholders.

I. Liquidity Gating Mechanisms.

With respect to redemption restrictions and/or the imposition of redemption fees, which were raised as measures that could complement capital requirements, we believe that while such measures could increase run risk they merit continued consideration (including as a stand-alone measure) as a

---

16 We note that the Council proposed including Weekly Liquid Assets with respect to municipal funds in its capital buffer formulas. We believe that weekly liquidity is equally significant and valuable for taxable and tax-exempt funds alike. Also, because we favor excluding Government and municipal funds from further regulation, the discussion above with respect to accounting for Weekly Liquid Assets for calculating the level of capital required is limited to prime funds.

17 While we acknowledge the principle underlying combining capital requirements with gating (it would provide the fund with further resiliency before the gate dropped), we reiterate that we would not support combining a floating NAV requirement with
means of stemming redemption activity during market stress. While liquidity gating could trigger higher net redemptions prior to the gate “dropping,” gating ultimately stops redemptions for a short period of time, something which the MBR does not do. To the extent that stopping, and not solely providing a disincentive for, redemptions is the goal of the Council’s recommendations, gating provides a direct response. Effective gating that mitigates destabilizing run risk and that does not compromise the stable NAV could provide a meaningful regulatory approach.

However, we think the potential run risk associated with gating would correlate directly with how quickly investors anticipate the gate coming down. For this reason, liquidity gating, in our view, would be more meaningfully implemented in combination with the Rule 2a-7 amendments we propose herein for prime money market funds. Portfolios that are more liquid and more conservatively structured from a credit standpoint should be able to delay or sustain redemption activity more easily, providing more potential lead time until a liquidity gate comes down. We believe this is an appropriate position to take because, by definition, there is no need to stop redemptions if a fund has sufficient liquidity – gating is only required if the fund does not have sufficient liquidity to meet redemptions.

We understand that some of the current discussion on liquidity gating has centered on the gate dropping when the fund’s Weekly Liquid Assets decline to 15% of total net assets. Starting from a minimum Weekly Liquid Asset requirement of 30%, that amount of liquidity (15%) can drain away quickly with redemptions. We believe this scenario can incentivize sharp and heavy redemption activity because investors would react to the relatively small amount of liquidity available before being gated. Alternatively, a larger liquidity cushion would make funds more resilient and shareholders less likely to be gated. Consider, for example, a 40% Weekly Liquid Assets allocation with gating triggered when that liquidity reaches 10%. In this scenario, we believe the larger liquidity cushion should reduce the incentive for shareholders to redeem. We support further review to determine the most desirable amount of liquidity to support fund resiliency and minimize the risk of gating triggering redemptions.

We acknowledge our proposal might suggest that we support allowing more net redemption activity into the financial system during a time of market stress and thus are compromising the value of gating. In response, we would note that funds would be meeting redemptions primarily with Liquid Assets in a time of crisis, which should have less overall systemic impact; so relying more heavily on liquidity before gating should be reasonable and consistent with responding to systemic concerns. Also, gating is a relatively extreme action which, we think, should require a money market fund to have to use up more than 15% of its liquidity before it is activated. Finally, through Daily Transparency, investors would be aware of the degree of a fund’s liquidity and as a result might have less incentive to redeem at the first sign of market stress. Again, we believe this merits further study.

---

**18** We also note that while the Council discusses the potential run risk associated with gating in the Proposing Release, the Council does not give run risk that same attention in connection with its MBR proposal. We think there is run risk associated with the MBR as well, because while the 30-day holdback is uniformly applied, investors nonetheless would have a first mover advantage in order to avoid being in the subordinated, first-loss position. We ask that the Council consider this aspect of the MBR in its deliberations.

**19** Assuming, as noted, a 30% Weekly Liquid Assets allocation and a 15% quantitative, objective trigger for gating.
Some of the current discussion on gating also has focused on requiring that a fund liquidate if its liquidity levels cannot be restored (or, alternatively, if an impaired $1 NAV subsequently cannot be remedied) within an established number of days (e.g., 30 days). We believe that this aspect of the conversation on gating does not necessarily further the best interest of fund shareholders. The recently implemented "transaction processing" requirement under Rule 2a-7\textsuperscript{20} affords the possibility of a reasonable alternative to liquidation at the end of the gating period (if remedial measures are not successful). We believe money market funds should be afforded the option to either convert to a floating NAV or liquidate at the end of the gating period. This would provide money market fund boards with the flexibility to pursue the best option for shareholders (and, pursuant to applicable "transaction processing" requirements, money market funds already possess the operational capacity to make that transition). For example, a floating NAV still could offer liquidity to an investor within a time horizon that may be more desirable than waiting for the end of the orderly wind-down of a fund in liquidation. While we have voiced our objection to a floating NAV broadly as a reform measure, we can see the potential value of a floating NAV option in this limited circumstance (at the end of a gating period when a fund's liquidity or NAV impairment is not resolved).

Finally, we also support gating in concept because it incorporates the value and importance of mutual fund board decision-making, something which we believe is generally absent from the Proposals. We believe that the adoption in 2010 of Rule 22e-3\textsuperscript{21} under the 1940 Act provided one of the most important remedial measures coming out of the 2008 financial crisis. We supported Rule 22e-3 when it was proposed because it empowered boards to use their independent business judgment to make decisions aimed at protecting shareholder value. We think the board decision-making associated with gating is a critical factor in any further regulation of money market funds and we ask that the Council give it due consideration in its deliberations.

J. The Council Should Suspend its Section 120 Process to Support the Commission Moving Forward with Meaningful Money Market Fund Regulatory Proposals.

The Council indicated at its November 13, 2012 open meeting that publishing the Proposals at this time was intended to provide a basis for the Commission to move forward on a second round of money market fund regulation. The Council also indicated a clear preference for the Commission rather than the Council to pursue money market fund regulation and that if at any point a majority of the Commissioners find support for a set of recommendations to issue for public comment, the Council would suspend its work and let that process go forward.

\textsuperscript{20} Rule 2a-7(c)(13) requires a money market fund (or its transfer agent) to have the capacity to redeem fund shares at a price based on current net asset value per share, including the ability to redeem at prices that do not correspond to a stable net asset value per share. This aspect of Rule 2a-7 provides the alternative to board action under Rule 22e-3. If the board does not suspend and irrevocably elect to liquidate a fund, the fund must honor redemptions at then-current net asset value per share.

\textsuperscript{21} Rule 22e-3 under the 1940 Act permits a money market fund to suspend redemptions and postpone the payment of proceeds pending board-approved liquidation proceedings if: (i) the fund's board of directors, including a majority of disinterested directors, determines pursuant to Rule 2a-7 that the extent of the deviation between the fund's amortized cost price per share and its current net asset value per share calculated using available market quotations (or an appropriate substitute that reflects current market conditions) may result in material dilution or other unfair results to investors or existing shareholders; (ii) the fund's board of directors, including a majority of disinterested directors, irrevocably approves the liquidation of the fund; and (iii) the fund, prior to suspending redemptions, notifies the Commission of its decision to liquidate and suspend redemptions.
We appreciate the Council recognizing the Commission’s primary role in regulating money market funds. Since the time the Council issued the Proposals, we believe circumstances have changed that should allow for the Council to advance its preference for the Commission moving forward with proposals for meaningful structural reform of money market funds. Recent statements from Commissioners have evidenced an intention on their part to have a set of rule proposals on money market fund regulation out for public comment in the near future (perhaps by the end of this calendar quarter). It also has been noted that the Commission’s Chief Economist has completed a comprehensive economic analysis that will inform and help advance the Commission’s independent deliberations.

During the Council’s deliberations on whether to proceed with issuing recommendations under Section 120, we respectfully ask that the Council consider the possibility of disrupting the Commission’s regulatory process if it proceeds with issuing recommendations prior to the Commission publishing a set of meaningful structural reforms for public comment. We have been, and continue to be, concerned that the overlap of systemic oversight and securities regulation has created confusion in the marketplace and stymied consensus and advancement of meaningful structural reforms within the confines of Rule 2a-7 to a satisfactory and balanced resolution. Thus, we believe the Council can provide a degree of regulatory clarity that would be beneficial for all interested parties if the Council allows the Commission’s regulatory process to proceed. The Commission’s history in regulating money market funds, in a manner consistent with the protection of investors and in promoting capital formation, coupled with the Commission’s record of working independently with the money market fund industry to effectively reach beneficial results, should provide sufficient comfort for the Council to at least delay issuing recommendations at this time.

To summarize, for the reasons stated above, we respectfully ask that the Council suspend its Section 120 process at this time and, to the extent the Council re-initiates the Section 120 process after the Commission completes its review of money market fund regulation, consider our proposals for money market fund regulation as reasonable yet effective means for reducing systemic risk associated with money market funds without compromising their utility and popularity as stable NAV cash management vehicles. We have confidence, though, that the Commission’s regulatory process, with the money market fund industry’s active participation, will achieve fair, balanced, and meaningful results.

Once again, we thank the Council for its time and attention to our comments.

Very truly yours,

J. Charles Cardona

J. Charles Cardona
President
With copies to:

Financial Stability Oversight Council.

The Honorable Neal Wolin, Acting Secretary and Deputy Secretary of the Treasury
The Honorable Ben S. Bernanke, Chairman of the Board of Governors of the Federal Reserve System
The Honorable Thomas J. Curry, Comptroller of the Currency
The Honorable Richard Cordray, Director of the Consumer Financial Protection Bureau
The Honorable Elisse B. Walter, Chairman of the Securities and Exchange Commission
The Honorable Martin J. Gruenberg, Chairman of the Federal Deposit Insurance Corporation
The Honorable Gary Gensler, Chairman of the Commodity Futures Trading Commission
The Honorable Edward DeMarco, Acting Director of the Federal Housing Finance Agency
The Honorable Debbie Matz, Chair of the National Credit Union Administration
The Honorable S. Roy Woodall, Jr., Independent Member

U.S. Securities and Exchange Commission

The Honorable Luis A. Aguilar, Commissioner
The Honorable Daniel M. Gallagher, Commissioner
The Honorable Troy A. Paredes, Commissioner
Norman B. Champ, III, Director, Division of Investment Management