

Fund Democracy
Consumer Federation of America
Consumer Action
National Association of Personal Financial Advisors
Financial Planning Association

September 22, 2008

BY FACSIMILE

Ms. Florence Harmon, Acting Secretary
U.S. Securities and Exchange Commission
100 F. Street, N.E.
Washington, DC 20549-1090

Dear Ms. Harmon,

We are writing on behalf of Fund Democracy, Consumer Federation of America, Consumer Action, National Association of Personal Financial Advisors, and Financial Planning Association to request that the Commission act promptly on our rulemaking petition to require that money market funds make nonpublic monthly electronic filings of data regarding their portfolios.¹ In the wake of the first retail money market fund breaking a dollar last week and the continuing turmoil in the money market fund industry,² we believe that it is imperative that the Commission demonstrate its commitment to protecting investors by taking steps to ensure the accurate pricing of money market fund portfolios.

In January, we recommended that the Commission essentially resurrect a proposal that it had made in 1995 to require money market funds to file their portfolios electronically

¹ Letter from Fund Democracy, Consumer Federation of America, Consumer Action, AFL-CIO, Financial Planning Association, and National Association of Personal Financial Advisors, to U.S. Securities and Exchange Commission (Jan. 16, 2008) *available at* <http://www.funddemocracy.com/MMF%20Rulemaking%20Petition.pdf>.

² The implication of these events is underscored by the U.S. Treasury's immediate action last week, moving to guarantee money market funds in order to stabilize the market. <http://www.treas.gov/press/releases/hp1147.htm>. See also Michael Gray, *Almost Armageddon*, New York Post (Sep. 21, 2008) (reporting that \$500 billion in money market fund redemption orders were placed prior to the market's opening on Sep. 18).

with the Commission on a quarterly basis.³ We also recommended that the Commission require the filing of additional data that would enable it to monitor the liquidity of short-term money market instruments and the reliability of the prices at which funds carry these instruments. The reliability of prices for securities for which markets have become illiquid lies at the heart of the current financial crisis, where firms thought to be worth tens of billions of dollars one day turn out to be worth only hundreds of millions (or substantially less) the next. Nowhere is it more imperative that portfolio pricing reflect actual market values than in money market funds,⁴ where investors have an expectation that their principal is safe and where the government historically has not provided any insurance backstop in the event of a default.

We are disappointed that the only proactive steps the Commission has proposed since we filed our petition nine months ago is to eliminate the requirement that a money market fund hold only securities that have received minimum credit quality ratings from a Nationally Recognized Statistical Ratings Organizations (“NRSRO”).⁵ At the same time that it has proposed to lower creditworthiness standards for money market funds, the Commission continues to address money market fund problems primarily on a reactive, *ad hoc* basis, whereby fund managers notify the Commission staff that their funds will break a dollar and ask for a no-action position to permit the purchase of the faulty portfolio securities at par.

The failure of the Primary Fund highlights the weakness of this strategy, which does nothing to protect investors against fund managers who are unwilling or unable to bail out the fund and fails to address the underlying problem of incorrectly valued portfolio securities. We recognize that there will always be unusual circumstances when a case-specific approach may be necessary. However, reports that the Commission has applied this approach for over 20 large funds in the last year alone illustrates that clinging to a finger-in-the-dike approach is inadvisable when systemic solutions are available. Permitting bailouts by fund managers on a routine basis has simply helped to conceal the risks presented by money market funds and strengthen the illusion that they cannot lose principal.

³ See Money Market Fund Quarterly Reporting, Investment Company Act Rel. No. 21217, at Executive Summary (July 19, 1995) (proposing to require quarterly electronic filing of portfolio information, including: “(i) the name of the security and its issuer and any guarantor of the security; (ii) the security’s credit quality; (iii) whether it is illiquid; (iv) its value; (v) the percentage of the portfolio represented by the security and the percentage of the portfolio invested in securities issued by the issuer; (vi) its maturity date; and, in the case of an adjustable rate instrument, (vii) the formula used for adjusting its interest rate.”). Under current rules, money market funds are required to disclose their portfolios only quarterly and provide only the information required on Forms N-CSR and N-Q.

⁴ See Sam Mamudi & Jonathan Burton, *Money Market Fund Breaks a Buck, Freezes Redemptions*, Marketwatch (Sep. 17, 2008) (money market fund that broke a dollar valued Lehman Bros. bonds at \$785 million immediately prior to Lehman’s bankruptcy filing).

⁵ See References to Ratings of Nationally Recognized Statistical Rating Organizations, Investment Company Act Release No. 28327 (July 1, 2008) (“NRSRO Proposal”).

Indeed, we recommend that the Commission consider the practicability and potential benefits of moving toward a requirement that *all* mutual funds provide *daily* electronic streaming of portfolio holdings, prices and recent trades. The problem described above is by no means limited to money market funds. Steep losses incurred by many short-term bond funds also raise the question as to whether the valuation of fund assets was accurate.⁶ If such an electronic filing system were in place, a fund that was carrying securities at inflated values would quickly be exposed by other funds' lower valuations and/or the staleness of the last trades on which those valuations were based.

The Commission also should consider whether this kind of technology application could be used in other scenarios, such as for large financial institutions that hold large pools of complex financial instruments, the value of which, incredibly, seems capable of disappearing overnight. We submit that a system under which fully transparent, current asset-pricing helps to ensure that firms' market values stay true to the actual value of their net assets is superior to a system that permits gaps between market values and actual asset values to grow until a taxpayer-funded bailout is considered the only alternative to a potentially harmful systemic failure.

In an ideal world, markets, not banking regulators, should be the primary risk managers in a capitalist democracy. Moreover, the money market fund historically has demonstrated the viability of a cash management vehicle that depends, not on the type of taxpayer guarantee provided to bank depositors, but on the efficient marriage of free markets and smart regulation. We believe that a failure to address this situation promptly will reflect a betrayal of the free market principles that the Commission is tasked with

⁶ See Prospectus Supplement, Morgan Keegan Select Fund, Inc. (Aug. 13, 2007).

defending and a continued reliance on a flawed regulatory approach that has increasingly led to a socialization of risk in our markets.

Thank you for your consideration of our comments.

Sincerely,

Mercer Bullard
Founder and President
Fund Democracy

Barbara Roper
Director of Investor Protection
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