

SUPPORTING STATEMENT
Rule 2a-7

A. JUSTIFICATION

1. Necessity for the Collection Information

Money market funds are open-end management investment companies that differ from other open-end management investment companies in that they seek to maintain a stable price per share, usually \$1.00. Rule 2a-7 [17 CFR 270.2a-7] under the Investment Company Act of 1940 [15 U.S.C. 80a] (the "Act") exempts money market funds from the valuation requirements of the Act, and, subject to certain risk-limiting conditions, permits money market funds to use the "amortized cost method" of asset valuation or the "penny-rounding method" of share pricing.

Rule 2a-7 also imposes certain recordkeeping and reporting obligations on money market funds. The board of directors of a money market fund, in supervising the fund's operations, must establish written procedures designed to stabilize the fund's net asset value ("NAV"). The board also must adopt guidelines and procedures relating to certain responsibilities it delegates to the fund's investment adviser. These procedures and guidelines typically address various aspects of the fund's operations. The fund must maintain and preserve for six years a written copy of both these procedures and guidelines. The fund also must maintain and preserve for six years a written record of the board's considerations and actions taken in connection with the discharge of its responsibilities, to be included in the board's minutes. In addition, the fund must maintain and preserve for three years written records of certain credit risk analyses, evaluations with respect to securities subject to demand features or guarantees, and determinations with respect to adjustable rate securities and asset backed securities. If the board takes action with respect to defaulted securities, events of insolvency, or deviations in share price, the fund must file with the Commission an exhibit to Form N-SAR describing the nature and circumstances of the action. If

any portfolio security fails to meet certain eligibility standards under the rule, the fund also must identify those securities in an exhibit to Form N-SAR. After certain events of default or insolvency relating to a portfolio security, the fund must notify the Commission of the event and the actions the fund intends to take in response to the situation.

On July 1, 2008, the Commission issued a release proposing to amend rule 2a-7 in four principal ways to: (i) rely on money market fund boards of directors (who usually rely on the funds' advisers) to determine that each portfolio instrument presents minimal credit risks, and whether the security is a "First Tier Security" or a "Second Tier Security;" (ii) add a portfolio liquidity requirement to the rule that would require that money market funds hold securities that are sufficiently liquid to meet reasonably foreseeable shareholder redemptions, and expressly limit their investment in illiquid securities to not more than 10% of their total assets; (iii) in the event the money market fund's investment adviser becomes aware of any new information about a portfolio security (or an issuer of a portfolio security) that may suggest that the security may not continue to present minimal credit risks, the proposal would amend rule 2a-7's downgrade and default provisions to require a money market fund's board of directors to reassess promptly whether the portfolio security continues to present minimal credit risks; and (iv) require a money market fund to notify the Commission of the purchase of a money market fund's portfolio security by an affiliated person in reliance on rule 17a-9 [17 CFR 270.17a-9] under the Act.¹ The proposed amendments also would make conforming amendments to rule 2a-7's record keeping and reporting requirements.² The proposed amendments to rule 2a-7 would impose a new reporting obligation on money market funds.

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

² See proposed rule 2a-7(c)(11).

2. Purpose of the Information Collection

The recordkeeping requirements in rule 2a-7 are designed to enable Commission staff in its examinations of money market funds to determine compliance with the rule, as well as to ensure that money market funds have established procedures for collecting the information necessary to make adequate credit reviews of securities in their portfolios. The reporting requirements of rule 2a-7 are intended to assist Commission staff in overseeing money market funds. The proposed reporting requirement to notify the Commission of the purchase of a money market fund's portfolio securities by an affiliated person in reliance on rule 17a-9 under the Investment Company Act is designed to assist Commission staff in overseeing money market funds' affiliated transactions that are otherwise prohibited.

3. Role of Improved Information Technology

The Commission's Electronic Data Gathering, Analysis and Retrieval System ("EDGAR") is designed to automate the filing, processing and dissemination of full disclosure filings. The system permits publicly-held companies to transmit their filings to the Commission electronically. EDGAR has increased the speed, accuracy and availability of information, generating benefits to investors and financial markets. All funds have been required to use EDGAR for their disclosure filings since November 6, 1995. The exhibit to Form N-SAR required to be filed with the Commission under rule 2a-7 when a money market fund's board takes action with respect to defaults, insolvencies, or share price deviations or when a portfolio security fails to meet certain standards may be filed electronically through EDGAR.

The proposed notification of rule 17a-9 transactions would be required to be transmitted to the Division of Investment Management by electronic mail. We believe this is appropriate in

light of recent changes in telecommunications technology, and because most of the notices of default that we have received in the past year have been transmitted electronically.

4. Efforts to Identify Duplication

The Commission periodically evaluates rule-based reporting and recordkeeping requirements for duplication, and reevaluates them whenever it proposes a rule or form, or a change in either. The recordkeeping required by rule 2a-7 is not duplicated elsewhere.

5. Effect on Small Entities

The recordkeeping and reporting requirements of rule 2a-7 are the same for all money market funds, including those that are small entities. A significant portion of the recordkeeping burden involves organizing information that the funds already collect when initially purchasing securities. In addition, when a money market fund analyzes a security, the analysis need not be presented in any particular format. Money market funds therefore have a choice of methods for maintaining these records that vary in technical sophistication and formality (*e.g.*, handwritten notes, computer disks, etc.).

6. Consequences of Less Frequent Collection

As described above, rule 2a-7 requires the fund's board to adopt written procedures designed to stabilize the fund's NAV and guidelines regarding the delegation of certain responsibilities, and requires the fund to notify the Commission if the board takes certain actions or in certain events of default or insolvency. None of these is a recurring obligation. They are, however, essential to the Commission's ability to determine compliance with the rule.

The rule also requires money market funds to perform periodic analyses of portfolio securities and reviews of the credit risks associated with those securities. The frequency of these

reviews is within the fund's discretion. The reviews are necessary to ensure that securities that remain in a fund's portfolio continue to present minimal credit risks.

7. Inconsistencies with Guidelines in 5 CFR 1320.5(d)(2)

Rule 2a-7 requires money market funds to retain certain written records for more than three years. The fund must maintain and preserve for six years a written copy of the procedures established by the board of directors designed to stabilize the fund's NAV as well as a written record of the board's considerations and actions taken in connection with the discharge of its responsibilities. The long-term retention of these records is necessary for the Commission's inspections program to determine compliance with rule 2a-7.

8. Consultation Outside the Agency

The Commission requested public comment on the collection requirements in the proposed amendments to rule 2a-7. The Commission and the staff of the Division of Investment Management also participate in an ongoing dialogue with representatives of the investment company industry through public conferences, meetings and informal exchanges. These various forums provide the Commission and the staff with a means of ascertaining and acting upon paperwork burdens confronting the industry.

9. Payment or Gift to Respondents

Not applicable.

10. Assurance of Confidentiality

Not applicable.

11. Sensitive Questions

Not applicable.

12. Estimates of Hour Burden

Commission staff estimates that there are 808 money market funds, all of which are subject to rule 2a-7.³ Commission staff estimates that rule 2a-7 contains the following collection of information requirements:

- Record of credit risk analyses, and determinations regarding adjustable rate securities, asset backed securities, and securities subject to a demand feature or guarantee.

162 responses annually for each fund to document these determinations, with the total annual responses per fund, on average, requiring 1,220 burden hours of professional (financial analyst or portfolio manager) time.⁴ Thus, to record credit risk analyses and determinations regarding adjustable rate securities, asset backed securities and securities subject to a demand feature or guarantee, the staff estimates a total burden and cost of approximately 985,760 hours and \$180,394,080.⁵

1 response annually for each of 24 new money market funds to formulate and establish written procedures and guidelines, with each response, on average, requiring:⁶

³ These include registered money market funds and series of registered money market funds. See Investment Company Institute, *Trends in Mutual Fund Investing April 2008*, May 29, 2008. available at http://www.ici.org/stats/latest/trends_04_08.html.

⁴ Estimates of the number of responses prepared annually regarding these analyses are based on conversations with individuals in the mutual fund industry. The actual number of responses prepared may vary significantly depending on the type and number of portfolio securities held by individual funds. For purposes of this Paperwork Reduction Act (“PRA”) submission, Commission staff used the following categories for fund sizes: (i) small – money market funds with \$50 million or less in assets under management; (ii) medium – money market funds with more than \$50 million up to and including \$1 billion in assets under management; and (iii) large – money market funds with more than \$1 billion in assets under management.

⁵ This estimate is based on the following calculations: 808 funds x 1,220 hours = 985,760 hours; 808 funds x 1,220 hours x \$183 per hour = \$180,394,080. The estimated hourly wages used in this PRA analysis were derived from reports prepared by the Securities Industry and Financial Markets Association. See Securities Industry and Financial Markets Association, *Report on Management and Professional Earnings in the Securities Industry – 2007* (2007), modified to account for an 1800-hour work year and multiplied by 5.35 to account for bonuses, firm size, employee benefits and overhead; and Securities Industry and Financial Markets Association, *Office Salaries in the Securities Industry – 2007* (2007), modified to account for an 1800-hour work year and multiplied by 2.93 to account for bonuses, firm size, employee benefits and overhead (“SIFMA Salary Guides”).

21 burden hours: 0.9 hour of the board of directors' time;
9.4 hours professional legal time;
10.75 hours support staff time.⁷

Thus, the staff estimates a total burden and cost of approximately 504 hours and \$126,522 to adopt procedures designed to stabilize the fund's NAV and guidelines regarding the delegation of certain responsibilities to the fund's adviser.⁸

- Board review of procedures and amendment of procedures.

1 response annually for each of 202 money market funds to review and amend written procedures and guidelines, with each response, on average, requiring:

4.5 burden hours: 0.5 hour of the board of directors' time;
4.0 hours professional legal time.⁹

Thus, the staff estimates a total burden and cost of approximately 909 hours and \$440,360 to review and amend written procedures and guidelines.¹⁰

⁶ This estimate is based on information from iMoneyNet's database. During the past three years, an average of 24 new money market funds have been created annually.

⁷ Estimates of the number of responses prepared annually regarding these analyses are based on conversations with individuals in the mutual fund industry.

⁸ This estimate is based on the following calculations: 24 funds x 21 hours = 504 hours; 24 funds x ((.9 hours x \$2,000 per hour) + (9.4 hours x \$295 per hour) + (10.75 hours x \$65 per hour)) = \$126,522. In calculating costs for complying with the information collection requirements of rule 2a-7, the Commission staff estimate that fund boards' hourly rate is \$2,000 per hour.

⁹ Estimates of the number of responses prepared annually regarding these analyses are based on conversations with individuals in the mutual fund industry. For purposes of this PRA analysis we assumed that on average 25% of money market funds would review and update their procedures on an annual basis.

¹⁰ This estimate is based on the following calculations: 202 funds x 4.5 hours = 909 hours; 202 funds x ((.5 hours x \$2,000 per hour) + (4 hours x \$295 per hour)) = \$440,360.

- Written record of board determinations and actions related to failure of a security to meet certain eligibility standards or an event of default or insolvency.¹¹

2 responses annually for 1 fund to record the board of directors' determinations and actions in the board meeting minutes, with each response on average requiring 0.5 burden hours of professional legal time.

- Notice to Commission of an event of default or insolvency.

1 response annually for 1 fund to provide notice to the Commission of an event of default or insolvency, with each response on average requiring 0.5 burden hours of professional legal time. Thus, the staff estimates that one money market fund that experiences a change in certain eligibility standards for portfolio securities or an event of default or insolvency relating to portfolio securities spends a total of 1.5 hours of professional legal time documenting board determinations and notifying the Commission regarding the event, for a total of 1.5 hours and \$443.¹²

- Proposed Commission notice of rule 17a-9 transactions.

1 response annually for 10 funds would provide notice to the Commission of a rule 17a-9 transaction, with each response on average requiring 0.5 burden hours of professional legal time, for a total of 5 hours and \$1,475.¹³

¹¹ A fund's board of directors makes these determinations and takes action when a portfolio security no longer meets eligibility requirements under the rule, or there has been an event of default or insolvency. These events occur infrequently. Although we have assumed an average of approximately 1 occurrence for one fund each year, this number may vary significantly in any particular year. A fund also must provide information regarding these events in an exhibit to Form N-SAR. The burden hours and responses required for filing these exhibits are included in the PRA submission for Form N-SAR. In the event of a default or insolvency with respect to an issuer of a portfolio security, the fund also must notify the Commission.

¹² This estimate is based on the following calculations: 1 fund x ((2 responses x 0.5 hours) + (1 response x 0.5 hours)) = 1.5 hours; 1 fund x (1.5 hours x \$295) = \$442.50.

¹³ This estimate is based on the following calculations: 10 funds x 0.5 hours = 5 hours; 10 funds x (0.5 hours x \$295) = \$1,475.

Thus, the Commission estimates the total annual burden of the rule's information collection requirements are 131,135 responses¹⁴ and 987,180 hours¹⁵ at an annual cost of \$180,962,880.¹⁶

These estimates are made solely for the purposes of the PRA and are not derived from a comprehensive or even representative survey or study of the cost of Commission rules.

13. Estimate of Total Annual Cost Burden

Commission staff estimates that in addition to the costs described above, money market funds will incur costs to preserve records, as required under rule 2a-7.¹⁷ These costs will vary significantly for individual funds, depending on the amount of assets under fund management and whether the fund preserves its records in a storage facility in hard copy or has developed and maintains a computer system to create and preserve compliance records.¹⁸ Commission staff estimates that the amount an individual fund may spend ranges from \$100 per year to \$300,000. Based on a cost of \$0.0000204 per dollar of assets under management for small fund, \$0.0000005 per dollar assets under management for medium funds, and \$0.0000046 per dollar of

¹⁴ This estimate is based on the following calculation: (162 responses x 808 funds) + (1 response x 24 funds) + (1 response x 202 funds) + (2 responses x 1 fund) + (1 response x 1 fund) + (1 response x 10 funds) = 131,135 responses.

¹⁵ This estimate is based on the following calculation: 985,760 hours + 504 hours + 909 hours + 1.5 hours + 5 hours = 987,179.5 hours.

¹⁶ This estimate is based on the following calculation: \$180,394,080 + \$126,522 + \$440,360 + \$443 + \$1,475 = \$180,962,880.

¹⁷ A significant portion of the recordkeeping burden involves organizing information that the funds already collect when initially purchasing securities. In addition, when a money market fund analyzes a security, the analysis need not be presented in any particular format. Money market funds therefore have a choice of methods for maintaining these records that vary in technical sophistication and formality (*e.g.* handwritten notes, computer disks, etc.). Accordingly, the cost of preparing these documents may vary significantly among individual funds. The burden hours associated with filing reports to the Commission as an exhibit to Form N-SAR are included in the PRA burden estimate for that form.

¹⁸ The amount of assets under management in individual money market funds ranges from approximately \$400,000 to \$109 billion.

assets under management for large funds, the staff estimates compliance with rule 2a-7 costs the fund industry approximately \$7.6 million per year.¹⁹ Based on responses from individuals in the money market fund industry, the staff estimates that some of the largest fund complexes have created computer programs for maintaining and preserving compliance records for rule 2a-7. Based on a cost of \$0.0000231 per dollar of assets under management for large funds, the staff estimates that total annualized capital/startup costs range from \$0 for small funds to \$37.5 million for all large funds. Commission staff further estimates that, even absent the requirements of rule 2a-7, money market funds would spend at least half of the amount for capital costs (\$19 million) and for record preservation (\$3.8 million) to establish and maintain these records and the systems for preserving them as a part of sound business practices to ensure diversification and minimal credit risk in a portfolio for a fund that seeks to maintain a stable price per share.

14. Estimate of Cost to the Federal Government

Rule 2a-7 does not impose any costs on the federal government.

15. Explanation of Changes in Burden

The estimated total annual burden is being decreased from 1,034,800 hours to 987,180 hours. This decrease is primarily attributable to the decrease in the number of money market funds. The proposed amendments to rule 2a-7 would account for an increase in hourly burdens of approximately 5 hours. The proposed amendments would not affect the staff's total annual cost estimate.

16. Information Collection Planned for Statistical Purposes

¹⁹ The staff estimated the annual cost of preserving the required books and records by identifying the annual costs incurred by several funds and then relating this total cost to the average net assets of these funds during the year. With a total of \$2.2 billion under management in small funds, \$174.1 billion under management in medium funds and \$1623.8 billion under management in large funds, the costs of preservation were estimated as follows: $((0.0000204 \times \$2.2 \text{ billion}) + (0.0000005 \times \$174.1) + (0.0000046 \times \$1623.8 \text{ billion})) = \7.6 million . See *supra* note Error: Reference source not found regarding sizes of large, medium, and small funds.

Not applicable.

17. Approval to not Display Expiration Date

Not applicable.

18. Exceptions to Certification Statement

Not applicable.

B. COLLECTIONS OF INFORMATION EMPLOYING STATISTICAL METHODS

Not applicable.