

PUBLIC

9 JUN 1994

RESPONSE OF THE OFFICE OF CHIEF COUNSEL
DIVISION OF INVESTMENT MANAGEMENT

Our Ref. No 93-834-CC
CBA Money Fund, et. al
File No. 811-3703

By letter dated December 21, 1993, you request our assurance that we would not recommend enforcement action to the Commission under Rule 22c-1 under the Investment Company Act of 1940 (the "1940 Act") if, as described in your letter, the money market mutual funds advised by Merrill Lynch Asset Management ("MLAM") and its subsidiary, Fund Asset Management, Inc. (collectively, the "Funds"), implement certain automatic redemption procedures.

You state that, at 4:00 p.m. each business day, each Fund declares a dividend in shares and calculates the net asset value (i.e., "dividend/price"). Accordingly, a redeeming shareholder who places a redemption request prior to 4:00 p.m. retains the last dividend paid on that date ("order date"). You state that currently a shareholder who places a redemption request receives redemption proceeds on the next business day following the order date. You further state that currently a Fund shareholder with a securities account with Merrill Lynch, Pierce, Fenner & Smith Incorporated ("MLPF&S") who places a redemption order and requests same-day settlement receives the redemption proceeds that day. 1/ In those instances, MLPF&S or an affiliate, to accommodate its customers, will advance funds on behalf of the customer on the order date but will not receive the proceeds from the redemption of the customer's Fund shares until the business day following the order date. 2/ You further state that, under the proposed automatic redemption procedures, if a shareholder requests same-day settlement, his Fund shares would be transferred to MLPF&S on the basis of the prior business day's share price, which would exclude the dividend declared on the order date. MLPF&S would then redeem the shares at the order date's 4:00 p.m. price for its own account so that MLPF&S would receive the dividend declared immediately prior to the 4:00 p.m. pricing. The redeeming shareholder would receive the dividends only through the business day preceding the order date.

You represent that these procedures would partially compensate MLPF&S for its foregone cost of funds in connection with same-day settlement transactions. You also represent that

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- 1/ You state that a shareholder may require same-day funds to purchase Treasury bills and certain other U.S. Government securities, or to enter into other types of transactions that typically require same-day settlement.
- 2/ You state that, because MLPF&S does not receive Fund redemption proceeds until the next business day in connection with same-day settlement transactions, it loses the overnight interest on the funds advanced on behalf of customers on the order date.

the proposed procedures would apply only to same-day settlement transactions involving money market funds, and that a Fund's use of the proposed procedures would be suspended during any period in which the net asset value of the Fund is not maintained at a constant \$1.00 per share or in the event of a negative dividend. You further represent that the redemption policy would be noted prominently on the shareholder's monthly account statement and would be disclosed in the Funds' prospectuses. 3/ Finally, you represent that, if a Fund's yield exceeds the cost of funds to MLPF&S, the proposed redemption procedures would be suspended for that Fund until MLAM and the Funds were satisfied that MLPF&S would receive no additional benefits beyond recouping the costs of advancing these funds.

Rule 22c-1 prohibits an open-end fund, the fund's principal underwriter, and any dealer from selling or redeeming the fund's securities except at a price based on the next computed net asset value. The Commission adopted Rule 22c-1 to: (i) eliminate dilution of existing shareholders' interests that might arise through the sale of shares at a price below their net asset value, or the redemption or repurchase of shares at a price above their net asset value; and (ii) eliminate speculative trading practices. 4/ You state that because the Funds are designed to maintain a constant net asset value per share, and because the procedures would be suspended if the Funds' net asset value per share deviated from \$1.00, the proposed redemption procedures do not present the potential for the backward pricing abuses that Rule 22c-1 was intended to address.

We would not recommend enforcement action to the Commission under Rule 22c-1 if the Funds implement the automatic redemption procedures as described in your letter. You should note that different facts or representations may require a different conclusion. Further, this response expresses the Division's position on enforcement action only and does not express any legal conclusions on the issues presented.

Janice M. Bishop
Janice M. Bishop
Attorney
by R. Stam

3/ Telephone conversation between Laurin Blumenthal Kleiman and Janice M. Bishop on February 1, 1994.

4/ Investment Company Act Rel. No. 5519 (Oct. 16, 1968).

555 CALIFORNIA STREET
SAN FRANCISCO, CA. 94104-1715
TELEPHONE: 415-398-3909
FACSIMILE: 415-397-4621

10900 WILSHIRE BOULEVARD
LOS ANGELES, CA. 90024-3959
TELEPHONE: 310-443-0200
FACSIMILE: 310-208-5740

SHIROYAMA JT MORI BUILDING, 15TH FLOOR
3-1, TORANOMON 4-CHOME, MINATO-KU
TOKYO 105, JAPAN
TELEPHONE: 03-5472-5360
FACSIMILE: 03-5472-5058

BROWN & WOOD

ONE WORLD TRADE CENTER
NEW YORK, N. Y. 10048-0557

TELEPHONE: 212-839-5300
FACSIMILE: 212-839-5599

815 CONNECTICUT AVENUE, N. W.
WASHINGTON, D. C. 20006-4004
TELEPHONE: 202-973-0600
FACSIMILE: 202-223-0485

172 WEST STATE STREET
TRENTON, N. J. 08608-1104
TELEPHONE: 609-393-0303
FACSIMILE: 609-393-1990

BLACKWELL HOUSE
GUILDHALL YARD
LONDON EC2V 5AB
TELEPHONE: 071-606-1888
FACSIMILE: 071-796-1807

[DUPLICATE]

December 21, 1993

BY FEDERAL EXPRESS

Office of Chief Counsel
Division of Investment Management
Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, D.C. 20549

ACT ICA-40
SECTION _____
RULE 22C-1
PUBLIC
AVAILABILITY 6/9/94

Re: Proposed Automatic Redemption Procedures
for Money Market Funds Advised by Merrill Lynch
Asset Management or Fund Asset Management, Inc.
In Connection With Same-Day Settlement Transactions

Ladies and Gentlemen:

This letter is submitted on behalf of several of the money market mutual funds advised by Merrill Lynch Asset Management¹ and its subsidiary, Fund Asset Management, Inc. (each a "Fund" and, collectively, the "Funds").² On behalf of the Funds, we

¹ The name under which Merrill Lynch Asset Management is incorporated in Delaware is Merrill Lynch Investment Management, Inc. Merrill Lynch Asset Management and Fund Asset Management, Inc. are together referred to herein as "MLAM."

² The Funds are CBA Money Fund, CMA Government Securities Fund, CMA Money Fund, CMA Tax-Exempt Fund, CMA Treasury Fund and the ten series of CMA Multi-State Municipal Series Trust (collectively, the "CMA/CBA Funds"), Merrill Lynch Ready Assets Trust ("Ready Assets Trust"), Merrill Lynch Retirement Reserves Money Fund of Merrill Lynch Retirement Series Trust ("Retirement Reserves Money Fund"), Merrill
(continued...)

hereby request that the staff of the Division of Investment Management (the "Division") of the Securities and Exchange Commission (the "Commission") advise us that it would not recommend enforcement action for violation of Rule 22c-1 ("Rule 22c-1") under the Investment Company Act of 1940, as amended (the "Investment Company Act") if the Funds implement the proposed automatic redemption procedures described below.³

I.

Current Automatic Redemption Procedures

Current procedures for all automatic redemptions. Each Fund is a no-load money market fund registered under the Investment Company Act as an open-end management investment company.⁴ The Funds' current automatic redemption procedures are applicable to shareholders who maintain securities accounts with Merrill Lynch, Pierce, Fenner & Smith Incorporated ("MLPF&S").⁵ Under these procedures, each Fund may redeem a sufficient number of its shares automatically to satisfy amounts due MLPF&S or an affiliate as a result of (a) account fees and expenses due and/or

²(...continued)

Lynch U.S. Treasury Money Fund, Merrill Lynch U.S.A. Government Reserves and Summit Cash Reserves Fund of Financial Institutions Series Trust ("Summit Cash Reserves Fund"). It is requested that the relief sought in this letter extend both to the Funds currently advised by MLAM and to any new Funds advised by MLAM in the future.

³ The proposed procedures originally were discussed by telephone and by letters dated April 27, 1990 and October 31, 1990 from Thomas R. Smith, Jr. of this firm to David L. Wills of the Division staff. These procedures were further discussed by Robert Harris of MLAM by telephone with Thomas S. Harman and Dorothy M. Donohue of the Division staff and by letter to Ms. Donohue dated October 6, 1992. Based on those communications, Ms. Donohue recommended that this formal no-action request be made.

⁴ Most of the Funds finance the distribution of their shares under the terms of a distribution plan pursuant to Rule 12b-1 under the Investment Company Act (a "Rule 12b-1 plan"). Neither the Summit Cash Reserves Fund nor the Retirement Reserves Money Fund have adopted a Rule 12b-1 plan.

⁵ Such accounts generally do not include margin accounts with MLPF&S, except in the case of the CMA/CBA Funds.

(b) purchases of securities or other transactions in the shareholder's securities account.

For all of the Funds except the CMA/CBA Funds, these procedures are conducted on an "opt-out" basis; *i.e.*, unless the shareholder notifies MLPF&S in advance that he or she does not want his or her Fund shares to be subject to the automatic redemption procedures, such shareholder's account will be scanned for debits (a "sweep") each business day prior to 4:00 p.m. New York time, the time at which such Funds are priced. In the case of the CMA/CBA Funds, the sweep is an integral feature of the CMA or CBA programs and takes place on each business day prior to those Funds' 12:00 p.m. pricing. In either case, if a debit exists, a sufficient number of Fund shares are redeemed as of the related Fund's pricing⁶ and the redemption proceeds are received the next business day to satisfy the amount due in the shareholder's account.

II.

Same-Day Settlement Transactions

Automatic redemption procedures are utilized to accommodate shareholders' needs for liquid funds to purchase securities or execute other transactions. The required settlement periods for these transactions range from same-day (in which immediately available funds must be delivered on the order date -- the time the order is placed or the transaction entered into) to five or more business days thereafter. Currently, automatic redemptions are effected on the business day preceding the date the shareholder is obligated to make such payment, and MLPF&S or its affiliate receives the redemption proceeds on the business day following the redemption date. Under the current procedures, shareholders receive all dividends declared and reinvested through the date of redemption. Therefore, for transactions requiring funds one business day or more after the order is placed, the redemption order can be placed on the business day prior to the date funds are needed, and MLPF&S will receive the customer's redemption proceeds on the proper day.

⁶ At each Fund's pricing time each day, the Fund first declares the daily dividend in shares and then determines the net asset value (*i.e.*, "dividends/price"). Accordingly, the redeeming shareholder retains the last dividend paid on such date. Certain other money market funds that are not part of the MLAM complex price first and then declare the dividend (*i.e.*, "price/dividend"), in which event the redeeming shareholder does not receive the daily dividend paid on the redemption date.

Transactions that require execution on a same-day settlement basis, such as the purchase of Treasury bills,⁷ however, cannot be processed in this manner, because Fund redemption proceeds cannot be made available on a same-day basis. In this event, MLPF&S, to accommodate its customers, advances funds on behalf of the customers on the order date but does not receive the proceeds from the redemption of the customer's Fund shares until the business day following the order date. Transactions entered into by Fund shareholders that require same-day settlement for which MLPF&S advances funds against the receipt of Fund redemption proceeds are herein referred to as "same-day settlement transactions."

Because MLPF&S does not receive Fund redemption proceeds until the next business day in connection with same-day settlement transactions, it loses the overnight interest on the funds advanced on behalf of customers on the order date.⁸ Based on its cost of funds, MLPF&S estimates that losses due to same-day settlement transactions aggregated over \$7.0 million in 1990, over \$5.4 million in 1991 and over \$3.4 million in 1992.⁹

⁷ In addition to the purchase of Treasury bills and certain other U.S. Government securities, other types of transactions that typically require same-day settlement include (a) transmission of federal funds by wire; (b) certain securities purchases involving, e.g., options, precious metals, money market securities, customer repurchase agreements and customer agreements pursuant to which cash is advanced collateralized by the customer's own securities; (c) checks issued by MLPF&S branch offices drawn on local banks in immediately available funds; and (d) transfer of funds from one customer account to another to cover debit balances.

⁸ Conversely, the shareholder receives a double return on his or her investment in the Fund for that day, since he or she receives both the benefit of immediately available cost-free funds and the dividend on the shares to be redeemed.

⁹ The decline in the amount of Merrill Lynch's losses in connection with same-day settlement transactions is not attributable to a decline in the number of transactions but is instead a result of the decline in interest rates over the past three years.

III.

Proposed Additional Automatic Redemption Procedures

Proposed procedures. MLPF&S has informed MLAM that it intends to continue its practice of advancing funds in connection with same-day settlement transactions if it can defray, in part, the overnight cost of funds presently incurred in connection with such transactions. In this regard, the Funds seek to implement the additional automatic redemption procedures described below.

Under the proposed automatic redemption procedures, Fund shares would be transferred to MLPF&S prior to the declaration of the daily dividend and the subsequent 4:00 p.m. pricing on the day the order for a same-day settlement transaction is placed.¹⁰ MLPF&S would then redeem the shares at such 4:00 p.m. pricing for its own account so that MLPF&S would receive the daily dividend declared immediately prior to such 4:00 p.m. pricing.

These procedures would partially compensate MLPF&S for the fact that the redemption proceeds would not be received by MLPF&S until the day after the shareholder is obligated to make payment. The proposed automatic redemption procedures would be conducted on the same "opt-out" basis that applies to the current automatic redemption procedures.

Restrictions on proposed procedures. The proposed automatic redemption procedures would apply only to same-day settlement transactions. Moreover, a Fund's use of the proposed procedures would be suspended during any period in which the net asset value of the Fund is not maintained at a constant \$1.00 per share.

Shareholder statement disclosure. To ensure that each shareholder understands that there is a cost associated with same-day settlement transactions, each such transaction would be noted prominently on the shareholder's monthly account statement. Each same-day settlement transaction appearing on the statement would be followed by a symbol. On the reverse side of the statement, that symbol will be included in the section explaining symbols and abbreviations followed by the following explanation:

**Transaction you requested required same-day
payment -- MLPF&S retained last day's
dividend to offset cost of advancing payment
on your behalf.**

¹⁰ The shares will be transferred prior to the daily dividend declaration to avoid any adverse Federal tax consequences to the Fund shareholder on account of the dividend.

MLPF&S cost of funds versus Fund dividend amount. As previously stated herein and discussed with the Division staff, the proposed procedures will only partially compensate MLPF&S for its forgone cost of funds in connection with same-day settlement transactions. Based on an historical comparison of the Funds' yields and MLPF&S's cost of funds, both MLPF&S and the Funds are confident that the aggregate amount represented by dividends recovered by MLPF&S under the proposed procedures will not exceed the aggregate amount expended in borrowing money to cover same-day settlement transactions. For example, set forth in the table below for the last three years is MLPF&S's cost of funds as compared to the yields on MLAM's two largest Funds:

Year Ended December 31,	Average 30-day Fund Yield		MLPF&S Cost of Funds	
	CMA Money Fund	Ready Assets Trust	Short-Term Borrowing	Blended Cost From All Sources ¹¹
1990	7.72%	7.76%	8.51%	9.26%
1991	5.87%	5.85%	6.36%	7.06%
1992	3.37%	3.31%	3.95%	4.67%

On an ongoing basis, MLPF&S will provide MLAM with an average weekly cost of funds to ensure that MLPF&S does not profit from the proposed automatic redemption procedures by obtaining more in dividends than it costs to advance same-day settlement transaction funds. In the unlikely event that a Fund's yield exceeded the cost of funds to MLPF&S, the proposed redemption procedures would be suspended until MLAM and the Funds were satisfied that MLPF&S would receive no additional benefits beyond the recouping of its cost of funds due to the use of the proposed automatic redemption procedures.

IV.

Legal Analysis

Rule 22c-1 provides, in pertinent part, that:

No registered investment company issuing any redeemable security ... and no principal underwriter of, or dealer in, any such security shall sell, redeem, or repurchase any such security except at a price based on the

¹¹ In general, funds advanced in connection with same-day settlement transactions are acquired through both short-term and longer-term borrowings.

current net asset value of such security which is next computed after receipt of a tender of such security for redemption

Rule 22c-1 was adopted to institute "forward pricing" to eliminate or reduce so far as reasonably practicable perceived abuses in connection with the sale, redemption or repurchase of mutual fund shares at prices based on "backward pricing" (*i.e.*, prices based on the last determined net asset value). Investment Company Act Release No. 5519 (October 16, 1968) (adopting release) (the "Release"). The Commission sought to eliminate the practice of selling, redeeming or repurchasing shares for a certain period of time at a previously determined net asset value. According to the Release, such practice enabled investors to take unfair advantage of increases in share value by purchasing shares at prices lower than current net asset value, thus diluting the value of the fund's outstanding shares. The ability to trade fund shares at prices other than current net asset value also invited speculative trading practices by enabling investors to purchase large blocks of shares whose value had increased above the selling price and then redeem them at the higher price after the next valuation. The Release stated that such speculative trading practices could seriously interfere with fund management to the extent that "(i) management may hesitate to invest what it believes to be speculators' money and (ii) management may have to effect untimely liquidations when speculators redeem their securities." Id.

It is submitted that the proposed automatic redemption procedures do not present the potential for the backward pricing abuses that Rule 22c-1 was intended to address. Money market funds invest in high quality, short-term money market instruments, declare daily dividends and maintain a stable \$1.00 net asset value per share. In this context, the types of fluctuations in net asset value that present opportunities for speculation do not exist. Furthermore, the declaration of a "negative dividend" by a Fund (*i.e.*, automatic redemption of shares to cover daily losses) is extremely rare and, in the unlikely event of a negative dividend, the proposed automatic redemption procedures would be suspended. Therefore, the proposed procedures create no risk of dilution. The fact that the automatic procedures will be used only to satisfy a same-day settlement obligation is a further disincentive to speculation.

The Commission staff has in several instances recognized the practical necessity for a liberal interpretation of the technical requirements of Rule 22c-1 in the money market fund context and has allowed money market funds to price on a technically backward basis (*i.e.*, prior to the daily declaration of the dividend). Certain institutional money market funds, such as TempFund, issue

two classes of shares, one of which prices prior to the dividend declaration (*i.e.*, backward pricing) and the other of which prices subsequent to dividend declaration (*i.e.*, forward pricing). [Moreover, due to systems requirements, the Commission staff has allowed the Funds to make a technical deviation from the requirements of Rule 22c-1 by allowing purchase orders placed through MLPF&S to be made effective on the business day following the day the order is placed, in which case the customer receives the next day's price.]

In addition, the Commission staff has in the past officially taken an equitable approach to Rule 22c-1 in other contexts, granting no-action relief in unique circumstances in which the staff has determined that noncompliance with the Rule is justified on grounds of practicality. See, e.g., Baldwin Life Insurance Co., et al. (pub. avail. February 3, 1989); Templeton Global Fund, Inc. (pub. avail. September 7, 1982); Scudder Tax Free Money Fund, et al. (pub. avail. July 16, 1982); Scudder, Stevens & Clark (pub. avail. February 18, 1976).

As a practical matter, unless MLPF&S continues to incur substantial losses in connection with its customers' same-day settlement transactions, a customer would be unable to enter into such transactions using Fund redemption proceeds and would instead be forced either to produce cash in large amounts when placing his or her order or (ii) to wait and have the order effected on the following business day. MLPF&S is willing, however, to continue to advance funds on behalf of its customers if it can reduce its consequent losses by using the proposed automatic redemption procedures with no adverse consequences to a Fund or its shareholders. MLPF&S therefore believes that the Funds and their shareholders would be best served by allowing the automatic redemption procedures to be effected as proposed, and that the proposed procedures are appropriate in the context of Rule 22c-1 and the relevant interpretations discussed above.

V.

Conclusion

In light of the foregoing, we believe that the proposed automatic redemption procedures for same-day settlement transactions are fair and equitable under the circumstances, provide a benefit to Fund shareholders with no negative effect on any Fund or its shareholders and are appropriate and permissible under the Investment Company Act. Accordingly, we hereby request that the staff of the Division of Investment Management advise us that it would not recommend that the Commission take any enforcement action for violation of Rule 22c-1 if the Funds

implement the proposed automatic redemption procedures as described herein.

If you have any questions regarding this matter, please call the undersigned at (212) 839-5525.

Sincerely,

A handwritten signature in black ink, appearing to read "Laurin", with a long horizontal flourish extending to the right.

Laurin Blumenthal Kleiman

cc: Robert Harris, Esq.