

MEMO# 8632

February 14, 1997

MONEY MARKET FUND PORTFOLIO INSURANCE

February 14, 1997 TO: BOARD OF GOVERNORS No. 7-97 PRIMARY CONTACTS - MONEY MARKET FUNDS (MONEY MKT MEMBERS-ONE PER COMPLEX) No. 1-97 PRIMARY CONTACTS - MEMBER COMPLEX (MEMBERS - ONE PER COMPLEX) No. 7-97 RE: MONEY MARKET FUND PORTFOLIO INSURANCE

As many of you know, ICI Mutual Insurance Company, the mutual fund industrys captive insurance company, has been engaged in studies to determine whether to create a facility to offer money market fund portfolio insurance ("MMFI"). The insurance model under study involves defaults of payments of interest or principal on portfolio holdings of money market funds which comply with Rule 2a-7. This memorandum is to report on progress to date and to ask for your assistance in arriving at conclusions with respect to certain issues. ICI Mutual estimates that it can have an insurance facility in operation by June 1 if discussions with reinsurers are successful and there is sufficient member interest. Specific issues under study are: (1) whether money market fund portfolio insurance is economically feasible from an actuarial standpoint, (2) whether such insurance can be reasonably priced from the fund investors standpoint, (3) whether reinsurance support is available at acceptable prices, (4) the development of policy provisions which provide protection against losses but do not reward unsound portfolio practices, and (5) the degree of member interest in this project. The actuarial studies vital to the first two issues above have been completed and indicate that MMFI is a viable insurance product and can be provided at premiums which would not significantly impair yield. Specifically, subject to further study, premiums would probably be one basis point or less. Insurance limits have been tentatively set at \$150 million. Not yet decided is whether coverage should be limited to a default which results in a decline in net asset value per share to 99 cents, and whether the insurance payment would be limited to the amount necessary to restore \$1.00 net asset value per share or for the entire decline in value of the security immediately prior to the default. Also to be decided is the amount of required deductibles, if any. In view of the positive results of studies to date, it appears to be timely to inquire of members whether they would be interested in MMFI within the general parameters described above. Moreover, your input is desired on the questions discussed above and any other matter you deem of interest. The enclosed questionnaire is provided for your convenience. It would be helpful if you would complete and return the questionnaire as quickly as possible but no later than February 28. If there is a significant degree of interest among members, a meeting of interested members will be scheduled to discuss this matter. Matthew P. Fink, President Investment Company Institute David Silver, President ICI Mutual Insurance Company Enclosure

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