

## MONEY MARKET FUNDS IN 2013

### *A Bad Idea: Imposing Capital Requirements on Money Market Funds*

The Financial Stability Oversight Council is considering whether to recommend that the U.S. Securities and Exchange Commission impose capital requirements, also known as capital buffers or NAV buffers, on money market funds. This notion is deeply flawed, as shown by ICI's in-depth analysis on several variations on the capital buffer idea: requiring fund advisers to commit capital, requiring funds to raise capital in the market, or having funds build a capital buffer by retaining fund income (rather than distributing income to fund shareholders).

- See ICI's report, [The Implications of Capital Buffer Proposals for Money Market Funds](#).

#### **Bank-like capital is inappropriate for money market funds.**

- Money market funds are neither banks nor unregulated. They manage risks very differently from banks—money market funds are required to hold diverse portfolios designed to limit risk.
- Capital providers would need to be paid for providing capital to funds, and these payments would have to come from fund assets. Unlike banks, money market fund sponsors cannot unilaterally raise fund fees. In many cases, funds would have to seek shareholder approval, which can be a costly and lengthy process.
- Even if shareholders accepted a fee increase, the necessary increase could be so large as to reduce the net yield on a prime fund below that of a Treasury-only money market fund.
- For more, see ICI's fact sheet, "[Money Market Funds Are Not Banks](#)."

#### **None of the capital buffer options are workable.**

- **Sponsor-provided capital:** Requiring money market fund advisers to commit capital to absorb possible future losses in their funds would alter fundamentally—and detrimentally—the money market fund business model.
  - Mutual funds, including money market funds, are owned by fund shareholders, not by fund sponsors. Fund advisers do not allocate capital to absorb losses because, as with all securities products, investors bear the risks of investing in funds.
- **Market-provided capital:** ICI analysis indicates that market-provided capital could in fact be a source of instability. Investors in subordinated securities could elect not to roll over their positions during periods of financial stress, subjecting funds to the risk of having to find new sources of capital precisely when market participants are reluctant to offer it.
- **Shareholder-provided capital:** A “within-fund” capital buffer could not be accumulated at any appreciable rate in the current near-zero interest rate environment. Funds are already waiving billions of dollars in fees (\$4.8 billion in 2012) to maintain a positive yield. Building capital from

investors' returns is impossible until short-term interest rates return to a more normal level, which, judging from Federal Reserve pronouncements, now appears to be years in the future. Even then, accounting rules would cap this buffer at less than 50 basis points. Further, any income retained by the fund would be subject to corporate income tax.

**In any form, a capital requirement for money market funds would likely push investors to less-regulated products, increase risks in the financial system, and reduce choice and competition.**

- Many advisers may simply liquidate their money market funds and not offer alternative products. Others may refocus their efforts on alternative cash-like products that are less regulated and less transparent, thereby increasing risks in the financial markets.
- The flight of investors from money market funds will disrupt the crucial role these funds play in financing jobs, communities, businesses, and the U.S. economy.

For more information on money market funds, their role in the economy, ICI's efforts to make these funds more resilient in the face of adverse market conditions, and the significant risk of undermining money market funds' value to investors and the economy, please see [www.ici.org/mmfs](http://www.ici.org/mmfs) or [www.PreserveMoneyMarketFunds.org](http://www.PreserveMoneyMarketFunds.org).