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The SEC's Money Market Fund Plans—Scoring a Hat Trick Against Investors and the Economy

By Paul Schott Stevens

The [Wall Street Journal](#) reports today that the Securities and Exchange Commission (SEC) continues to pursue regulatory changes for money market funds that will harm investors, damage financing for businesses and state and local governments, and jeopardize a still-fragile economic recovery. Quite a regulatory hat trick.

The reported changes are not necessary, particularly in light of the SEC's own success in reforming money market funds. In January 2010—six months before the passage of the Dodd-Frank Act—the Commission enacted U.S. regulators' first substantive response to the financial crisis with new amendments to the rules governing money market funds. The changes to Rule 2a-7 made money market funds stronger by raising standards for credit quality, liquidity, and transparency, while reducing risks by shortening the maturity of these funds' portfolios. The fund industry strongly supported these changes.

The first test for these newly strengthened funds came swiftly—and they weathered it well. In the summer of 2011, money market funds faced three challenges: the ongoing European debt calamity, the showdown over the U.S. debt ceiling and subsequent downgrade of government securities, and the long-running punishment of near-zero interest rates, compounded by unlimited insurance for non-interest-bearing checking deposits and payment of interest on business checking for the first time in 80 years.

Under this pressure, some investors took cash out of prime money market funds. About 10 percent of prime funds' assets were redeemed from June to August—some \$170 billion—with nary a hiccup in the money market. U.S. money market funds met the redemptions, maintained liquidity well in excess of the new standards put into place in 2010, and saw no change in the mark-to-market value of their portfolios. Even more remarkably, investors still maintain \$2.6 trillion in money market fund assets—the same level as mid-2007, before the start of the financial crisis—despite yields hovering near zero for the more than 30 months.

In light of the success of the 2010 reforms, we see no need for further regulatory changes. And we are especially concerned that the ideas reported in the *Journal's* story—forcing money market funds to float their value, imposing bank-like capital requirements, and freezing investors' funds when they try to redeem—present the worst of all worlds. These proposals will both drive fund sponsors out the industry, reducing competition and choice for investors, and leave the remaining sponsors with a product that few investors or their financial advisers will use.

The harm to investors and the economy of such changes could be enormous. Scores of organizations representing businesses, state and local governments, nonprofit institutions, and individual investors have told the SEC in no uncertain terms that they prize the stability and liquidity of money market funds. Forcing these funds to abandon their \$1.00 net asset value (NAV) or denying investors full access to their assets will undermine the core features that make money market funds a valued cash-management tool for individuals and institutions alike.

The combination of capital requirements and redemption restrictions may well be the one idea that's worse than forcing funds to float. Compliance with redemption freezes will impose hundreds of millions of dollars in added costs on investors, funds, and financial intermediaries and impair features—like check writing, debit-card access, and sweep accounts—that investors demand.

We have no doubt that these changes will drive investors away from money market funds—because [investors have said so](#). As hundreds of billions of dollars flow out of these funds, the economy will take a hit due to the disruption of vital financing. After all, money market

funds buy more than one-third of commercial paper, which businesses rely upon to fund payrolls and operations; more than one-half of short-term municipal debt, which state and local governments issue to fund public projects such as roads, bridges, airports, and hospitals; and almost one-sixth of short-term Treasury bills. There is no ready source of financing to replace money market funds.

The mutual fund industry is committed to ensuring that money market funds are strong enough to withstand adverse market conditions. Since the summer of 2007, we have worked alongside regulators to propose and examine constructive changes to make these funds more resilient. ICI has marshaled its members' expertise to respond to regulators' requests with extensive analysis and insights into a wide range of reform proposals. But the changes reportedly under consideration are neither constructive nor likely to make financial markets more resilient. The SEC has already made money market funds stronger. It should recognize its own success.

For more on money market funds, visit ICI's [Money Market Fund Resource Center](#).

Paul Schott Stevens was President and CEO of ICI.

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