

ICI VIEWPOINTS

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Preserving Money Market Funds Is Good for Corporate America

By Sean Collins and Mike McNamee

A recent [DealBook](#) column about money market funds distorts the truth and omits essential facts. We'd like to correct the record and review a few key points that the *DealBook* author, law professor Steven M. Davidoff, seems to have missed.

Support for preserving the fundamental characteristics of money market funds is wide and deep. To suggest otherwise is misleading.

Davidoff frames his column in terms of “the money market fund industry’s resistance” to changes in these funds. He neglects to note that the industry was first to respond to effects of the financial crisis on funds, proposing [substantial reforms for money market funds by March 2009](#). The Securities and Exchange Commission (SEC) went even further and adopted tough new regulations for money market funds in early 2010. The SEC’s 2010 reforms benefited investors by raising credit standards, shortening maturities for funds’ portfolios, adding minimum liquidity requirements, increasing transparency of fund holdings, and authorizing an orderly liquidation if a fund risks breaking the dollar.

The industry is opposed to the further proposals the SEC is considering—[floating funds’ net asset value \(NAV\)](#), imposing a “holdback” on redemptions, and [imposing a capital requirement](#)—and we are not alone in our opposition. More than 100 organizations representing an extraordinary array of business, government, financial services, nonprofit, and consumer organizations have voiced their opposition to structural changes under consideration by the SEC. You can find these voices [at PreserveMoneyMarketFunds.org](#).

Let’s look at one example, from Associated Oregon Industries. Last month, that group wrote to the SEC:

“As Oregon’s leading employer organization, representing companies from the largest multinational corporations to small businesses in nearly every community of our state, we are deeply aware of the value that these businesses derive from money market funds. In our view, forcing money market funds to float their NAVs or restrict the ability of investors to retrieve 100 percent of their money would harm businesses, and the broader U.S. economy.”

Investors prize the convenience, stability, and liquidity of money market funds—and they care about whether those qualities are lost.

Davidoff asks, “do [investors] really care whether money market funds are priced at a dollar or have to pay for capital buffers?” The answer: you bet they do.

[Research](#) on the reactions of treasurers, governmental, and institutional investors shows that each of the SEC’s concepts for structural changes would cause a dramatic drop-off both in investors’ use of money market funds and in institutional assets. Surveys of retail investors show [similar results](#).

Far from “ignoring possible compromises,” the fund industry has tirelessly examined the range of ideas floated for reform examined by the [President’s Working Group on Financial Markets](#) and others. The fund industry has been willing to study any proposal and has spent thousands of hours and millions of dollars doing so. But we will remain opposed to any proposal that will fundamentally alter the money market fund product and its benefits to investors. Most ideas proposed have failed this test, including the two-tier system

(floating and non-floating share classes) that Davidoff mentions.

Money market funds are not causing operating companies to be shut out of the commercial paper market.

Davidoff suggests that “corporate America can no longer get the wide array of financing it previously received from money market funds,” and therefore, “corporate entities are now shut out of the market and funds are not willing to purchase their paper.”

But there’s no evidence in the data that corporate issuers are being shut out of the commercial paper market. The chart below, based on Federal Reserve data, shows that nonfinancial commercial paper outstanding is at nearly the peak level seen in mid-to-late 2008.

The fact that commercial paper issuance by nonfinancial firms has not yet exceeded that level probably owes to factors completely unrelated to money market funds. First, with long-term interest rates so low, companies that need financing are more likely to tap the bond market to lock in cheap long-term financing than to issue commercial paper. Second, nonfinancial corporations are flush with cash. Federal Reserve statistics show that as of the first quarter of 2012, nonfinancial firms held more than \$2.3 trillion in cash and other liquid instruments (including more than \$500 billion in money market funds). Given that nonfinancial companies already have plentiful cash on hand, there’s little impetus to raise more cash by issuing commercial paper.

Nonfinancial Commercial Paper Outstanding

Billions of dollars



Source: Federal Reserve Board

A healthy money market fund sector is better for corporate America than no money market funds at all.

Davidoff’s core error is that he ignores the implications of the SEC’s proposed changes. Forcing these funds to float their NAV would drive away millions of investors who cannot or will not invest cash in floating-value products, either for legal reasons or because of the tax and accounting burdens that floating values cause. Capital buffers would impose [high costs](#) on fund sponsors and investors. [Denying investors full access to their money market fund assets](#) would render these funds useless across a wide range of products—including retirement plans and sweep accounts—and drive away even more investors who want their cash to be fully liquid.

The bottom line: if the SEC proposals go through, the money market fund industry would shrink to a shadow of its current size—and then what would happen to what Davidoff calls “the heart of corporate finance”? In our view, it is far better for investors, for corporate America, and for the economy to have money market funds with higher investment standards than no money market funds at all.

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