

MEMO# 33382

March 25, 2021

ICI Draft Comment Letter on PWG MMF Reforms; Comments Due April 5

[33382]

March 25, 2021 TO: Money Market Funds Advisory Committee RE: ICI Draft Comment Letter on PWG MMF Reforms; Comments Due April 5

As you know, the SEC has published a [request](#) for public comment on potential reform measures to improve the resilience of money market funds as highlighted in a December [Report](#) of the President's Working Group on Financial Markets (PWG).^[1] The Report provides background on money market funds, including the SEC's 2010 and 2014 regulatory reforms, and the events in certain short-term funding markets in March 2020. The Report then discusses various measures that policy makers could consider to improve the resilience of US prime and tax-exempt money market funds and broader short-term funding markets.

ICI has prepared a draft comment letter, which is attached and briefly summarized below. Any comments on the draft letter should be in writing and sent to jheinrichs@ici.org by Monday, April 5. Please note we also are sending a word version by email so members can add redline comments.

Our examination of the reform options outlined in the Report and other reform ideas has led us to the same conclusion the PWG apparently reached: namely, that there is no "silver bullet" for safeguarding money market funds against the severest market distress. With this in mind, we have divided the ten reform options into three categories:

1. Reforms that could advance the goals of reforms—specifically, options with the most promise for addressing policymakers' concerns with the least negative impact;
2. Reforms that do not advance the goals of reform and do not preserve the viability of money market funds—specifically, options with significant drawbacks, ranging from potential detrimental impacts on money market funds, their investors, and the market, to complicated regulatory, structural, and operational hurdles; and
3. Reforms that are unlikely to address policymakers' goals of reform.

Reforms that could advance the goals of reform:

- *Removal of tie between money market fund liquidity and fee and gate thresholds:* This reform would remove the tie between the 30 percent and 10 percent weekly liquid asset thresholds and the imposition of fees and gates when doing so is in the

best interest of the fund, without reference to any specific level of liquidity. We agree that the tie between liquidity and fee and gate thresholds made money market funds more susceptible to financial market stress and would likely do so again in future periods of stress. By coupling the option to impose liquidity fees or gates with the 30 percent weekly liquid asset requirement, the SEC's 2014 reforms may have negatively affected the benefits of this substantial liquidity buffer. Indeed, the 30 percent weekly liquid asset buffer became a floor that accelerated shareholder redemptions due to uncertainty about the imposition of liquidity fees or gates. To be a true buffer, it should be an extra source of liquidity in times of stress.

- Although we support delinking fees and gates from liquidity thresholds, we believe that a more nuanced approach to fees should be considered. The industry continues to believe that redemption fees are an appropriate tool for money market funds, but should only be triggered when a fund is facing unusual circumstances, such as a period of heavy redemptions associated with general stress in the financial markets at large, or with an idiosyncratic credit issue. To make this powerful tool even more useful to fund boards (and therefore more likely to advance the goals of reform), we recommend an approach to fees that is separate from, and to be used earlier than, gates. Specifically, we recommend the SEC consider requiring funds to maintain detailed, board-approved policies and procedures that provide the board with a clear framework for *when* to impose redemption fees and *how* to calculate them.
- *Money market fund liquidity management changes:* Our letter suggests that ICI members could support an increase in the weekly liquid asset minimums, provided the tie between the liquidity thresholds and the imposition of fees and gates is removed. We caution regulators, however, that any increase in weekly liquid asset thresholds should not be so high as to materially impact money market funds' ability to serve as direct sources of financing for businesses and financial institutions and indirect financing for households or make it difficult (or impossible) to provide a return that is above that of a Treasury money market fund.

Reforms that do not advance the goals of reform and do not preserve the viability of money market funds

- *Swing pricing:* To provide money market funds a tool to mitigate potential dilution that can result from costs associated with redemption activity and to manage fund liquidity, the Report proposes swing pricing as a possible reform option. Our letter argues that implementing swing pricing would likely strip money market funds of their defining features (such as multiple daily NAV strikes per day and same-day settlement), impose excess costs to overcome unnecessary and complex structural challenges, and cause confusion among investors in periods of stress. Any potential benefits of employing swing pricing—assuming that it could realistically be implemented—are difficult to predict given its novel application to money market funds.
- *Capital buffers:* This reform would require money market funds to provide dedicated resources within or alongside a fund to absorb losses and fluctuations in the value of a fund's portfolio. Our letter reiterates our long-standing position that requiring money market funds or their advisers to maintain capital against money market fund assets is a deeply flawed suggestion. Over the years, ICI has analyzed 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). Each time we have found that its likeliest impact would be to impel money market fund sponsors to exit

the business, thus depriving investors, issuers, and the economy of the benefits these funds provide.

- *Sponsor support requirements*: This reform would establish a regulatory framework governing when a sponsor would be required to provide support that could clarify who bears money market fund risks. We believe this reform option suffers from many of the same drawbacks as imposing capital buffer requirements on fund advisers.
- *Minimum balance at risk (MBR)*: A MBR is a potential reform that would make a portion of each shareholder's recent balances in a money market fund available for redemption only with a time delay to ensure that redeeming investors still remain partially invested in the fund over a certain time period. We believe the MBR also is deeply flawed and will not advance the goals of reform for three primary reasons: investors would not invest in money market funds with these redemption restrictions; an MBR may actually increase the likelihood of a run, and MBR-type restrictions are costly, operationally complex, and difficult to implement. Indeed, the likeliest impact of an MBR requirement would be to drive investors as well as intermediaries away from these money market funds.
- *Liquidity exchange bank membership*: This reform would require prime and tax-exempt money market funds to be members of a private liquidity exchange bank that would provide a liquidity backstop during periods of market stress. Over ten years ago, ICI, with assistance from its members, outside counsel, and consultants, spent about 18 months developing a framework for a liquidity exchange facility (LF), including how it could be structured, capitalized, governed, and operated. At that time, we believed the proposed LF addressed many of the risks and challenges of the 2007-2008 global financial crisis to stable NAV prime money market funds. Ultimately, the LF did not garner regulatory interest. Instead, the SEC adopted different money market fund reforms in 2014, including a floating NAV requirement for all prime and tax-exempt money market funds sold to institutional investors and new fee and gate tools for all prime and tax-exempt money market funds, including retail funds. As a result of those reforms, the prime money market fund industry, including the number of prime fund sponsors, substantially shrunk. Given this smaller asset base and the costs of such a facility, the industry no longer believes, as it once did, that the LF is a viable reform option that would advance the goals of reform. Rather, members have indicated that they would simply stop sponsoring money market funds if membership to an LF was required.

Reforms that are unlikely to advance the goals of reform

- *Floating NAVs for all prime and tax-exempt money market funds*: Retail prime money market funds and retail tax-exempt money market funds currently can sell and redeem shares at a stable share price (e.g., \$1.00). This reform would require that these money market funds sell and redeem their shares at a price that reflects the market value of a fund's portfolio consistent with the current floating NAV requirements for institutional prime and institutional tax-exempt money market funds that the SEC adopted in 2014. The Report suggests that floating the NAV could reduce the likelihood of investors wanting to move away from the money market during these events. We disagree with this suggestion. Institutional prime money market funds had floating NAVs but experienced large redemptions. On the other hand, retail prime money market funds with stable NAVs experienced much more modest redemptions. For these reasons, we remain doubtful that floating the NAV for retail money market funds is necessary and more generally, that it reduces risks in any meaningful way. The letter also notes that floating NAVs could eliminate key benefits to retail investors.

- *Countercyclical weekly liquid asset requirements:* The Report proposes a countercyclical weekly liquid asset requirement that could automatically reduce minimum weekly liquid asset requirements in certain circumstances, such as when net redemptions are large or when the SEC provides temporary relief from weekly liquid asset requirements. Any thresholds linked to a fund's minimum weekly liquid asset requirements (e.g., fees or gate thresholds) also would move with the minimum. The letter notes that current rules do not preclude funds from using weekly liquid assets to meet redemptions or prohibit funds from falling below the 30 percent threshold and that before the 2014 reforms that tied a fund's ability to impose a fee or gate to the weekly liquid asset thresholds, money market funds regularly dipped below the 30 percent threshold. The difficulty in March 2020 was that money market funds could no longer freely use their weekly liquid assets to meet redemptions because investors feared the mere possibility of fees or gates. We therefore do not believe this reform will improve the usability of weekly liquid asset requirements.
- *Reform of conditions for imposing redemption gates:* Based on the experience of certain money market funds last March, the Report expresses concern that rather than making money market funds more resilient, the mere prospect of gates may have caused investors to engage in preemptive runs. In response to this concern, the Report includes a potential reform that would reduce the likelihood that redemption gates may be imposed, by for example, requiring funds to obtain SEC permission, requiring fund boards to consider liquidity fees before gates, or lowering the weekly liquid asset threshold at which gates could be imposed (e.g., 10 percent). Rather than reforming conditions for imposing redemption gates, we believe gates should be limited to extraordinary circumstances that present a significant risk of a run on a fund and potential harm to shareholders, such as those contemplated under Rule 22e-3, which permits a money market fund to suspend redemptions *only* to facilitate an orderly liquidation of the fund. As such, we believe if thresholds for gates remain (even if substantially lower), they could still be focal points for preemptive runs.

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[Attachment](#)

endnotes

[1] The PWG is chaired by the Secretary of the Treasury and includes the Chair of the Board of Governors of the Federal Reserve System, the Chair of the SEC, and the Chair of the CFTC.