

**MEMO# 25193**

May 17, 2011

## **ICI Comment Letter on Federal Reserve Board Proposal to Repeal Regulation Q**

[25193]

May 17, 2011

TO: MONEY MARKET FUNDS ADVISORY COMMITTEE No. 32-11  
MUNICIPAL SECURITIES ADVISORY COMMITTEE No. 27-11  
SEC RULES COMMITTEE No. 48-11 RE: ICI COMMENT LETTER ON FEDERAL RESERVE BOARD PROPOSAL TO REPEAL REGULATION Q

The Investment Company Institute filed a letter with the Federal Reserve Board on its proposed rule that would repeal Regulation Q, which prohibits member banks of the Federal Reserve System from paying interest on demand deposits. [\[1\]](#) The proposed rule, which implements Section 627 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank Act), repeals Section 19(i) of the Federal Reserve Act, the statutory authority under which the Board established Regulation Q. In its rule proposal, the Board asked a series of questions about the repeal of Regulation Q, including whether it would have implications for money market funds. ICI's letter is attached and briefly summarized below.

The letter states that although it is unclear how significant the competitive effect of allowing banks to pay interest on demand deposits will be on investor demand for money market funds, we have deep concerns that the elimination of Regulation Q, coupled with the unlimited deposit insurance on noninterest bearing transaction accounts as required under Section 343 of the Dodd-Frank Act, [\[2\]](#) will effectively extend unlimited insurance to interest-bearing accounts. The letter further states that these changes could dramatically alter the competitive landscape between banks and money market funds and potentially create large outflows from money market funds and into banks either immediately or during a future financial crisis, putting severe pressure on the money markets. Furthermore, the combination of these two changes will significantly increase moral hazard for the banking system, and potentially increase the costs of operating the deposit insurance program for the FDIC and ultimately the U.S. taxpayer. Indeed, the adoption of these two provisions likely will create systemic risks that did not previously exist. The letter ends by recommending that the Board express this view to Congress and the FDIC to ensure that the unlimited insurance, authorized for two years in Section 343, be allowed to expire as contemplated by the Dodd-Frank Act.

Jane G. Heinrichs  
Senior Associate Counsel

[Attachment](#)

**endnotes**

[1] See Prohibition Against Paying of Interest on Demand Deposits, Federal Reserve Board, Docket No. R-1413, RIN No. 7100-AD72 (April 5, 2011), available on the Board's website at <http://edocket.access.gpo.gov/2011/pdf/2011-9002.pdf>.

[2] Pursuant to Section 343 of the Dodd-Frank Act, the FDIC is required to provide unlimited insurance coverage for funds held in noninterest bearing transaction accounts through December 31, 2012. See Deposit Insurance Regulations; Unlimited Coverage for Noninterest Bearing Transaction Accounts, 75 Fed. Reg. 69,577 (November 15, 2010) (to be codified at 12 C.F.R. pt. 330).

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