April 19, 2021

Via Electronic Mail (rule-comments@sec.gov)

Vanessa Countryman, Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: Request for Comment on Potential Money Market Fund Reform Measures in President's Working Group Report, File No. S7-01-21

Dear Ms. Countryman:

The Healthy Markets Association[1] appreciates the opportunity to offer comments in response to the Commission's release of the President's Working Group on Financial Markets, Overview of Recent Events and Potential Reform Options for Money Market Funds ("PWG Report").[2]

We urge the Commission to identify, assess, and address potential causes for systemic risks, and welcome the inquiry into the short term funding markets and investor cash management. However, we are deeply concerned with the limited analysis of what happened in March 2020, as well as the fundamental orientation of the proposals and potential negative impacts on investors, funding markets, and economy overall.

We question the evidentiary basis for those who argue that money market funds should be managed with bank-like regulation, or that past reforms to money market fund regulations were insufficient. Rather, we agree with the PWG Report that some of the redemption activity in March 2020 was in fact *caused by* the SEC's 2014 Reforms. Further, we are befuddled that we are once again debating essentially the same sets of proposed reforms as were discussed a decade ago, without regard to the fundamental changes in the funding markets, including the dramatic shrinking of non-government money market funds and changes in the commercial paper markets, since that time.

We urge the Commission to evaluate the short term funding markets as they currently exist, and consider reforms that will promote the efficient flow of capital to businesses, protect investors, and serve the public interest.

---

[1] To learn about Healthy Markets or our members, please see our website at http://healthymarkets.org.

[2] *Request for Comment on Potential Money Market Fund Reform Measures in President's Working Group Report*, Sec. and Exch. Comm'n, Inv. Co. Act Rel. No. 34188, (Feb. 4, 2021), *available at* https://www.sec.gov/rules/other/2021/ic-34188.pdf ("2020 PWG Report Release").

HEALTHY MARKETS
TRANSPARENCY & TRUST

Regulatory Background

We begin by comparing and contrasting traditional bank funding to money market funds. Both seek to provide cash management for investors who are primarily focused on preservation of capital. Both seek to invest customers' capital, earn safe returns, and then readily and predictably meet redemption or withdrawal requests upon demand at stable prices. Both banking and asset management of money market funds essentially provide liquidity transformation, and as a result, come with some embedded liquidity risk. This liquidity risk can give rise to runs by depositors or investors, if they become concerned that they may lose access to their deposited or invested capital.

In most regards, traditional bank accounts and money market funds are remarkably close substitutes for investors.[3] However, their regulatory regimes are surprisingly different.

Banking regulators have traditionally addressed market and liquidity risks by requiring (1) capital, and (2) limited insurance that is funded by the banks themselves, but ultimately backed by the taxpayers. For a variety of reasons (including that capital requirements are often too low to be effective), these safety nets have had limited success in preventing bank failures and market-wide disruptions.[4]

Notably, banking regulators have generally taken a very permissive approach to the types of assets and liquidity of holdings that insured depository institutions may have, and required extremely limited transparency regarding those holdings' characteristics. For example, the so-called "London Whale" episode that ultimately cost JPMorgan Chase billions of dollars in trading losses and regulatory settlements was essentially a very large, complex bet on credit derivatives that was conducted within an insured depository institution.[5]

In general, a bank enjoys the comparative advantage of having a much larger pool of potential investments (that can pay greater returns), but then has the additional costs of

---

[3] Jonathan R. Macey, *Reducing Systemic Risk: The Role of Money Market Mutual Funds as Substitutes for Federally Insured Bank Deposits*, John M. Olin Center for Studies in Law, Economics, and Public Policy Research Paper No. 422, at 6, 2011, *available at* https://papers.ssrn.com/sol3/papers.cfm?abstract_id=1735008 ("MMFs are a substitute for the checking accounts offered by banks").

[4] For example, since 1980, there have been about 3500 bank failures, costing taxpayers billions of dollars. Further, the Financial Crisis of 2008 was unquestionably a result of high-risk activities by banks and other market participants -- not money market funds.

[5] See generally, *JPMorgan Chase Whale Trades: A Case History of Derivatives Risks and Abuses, Majority and Minority Staff Report of the US Senate Permanent Subcmte on Investigations, Cmte on Homeland Sec. and Gov't Affairs*, 113th Cong. (2013), *available at* https://www.hsgac.senate.gov/imo/media/doc/REPORT%20-%20JPMorgan%20Chase%20Whale%20Trades%20(4-12-13).pdf.

capital and insurance (such as payments to the Deposit Insurance Fund).[6] Despite the ability to invest in riskier, and higher-yielding assets than money market funds, the interest paid on these accounts is often lower than investors' returns from money market funds.[7] Put simply, banks enjoy larger profit margins from deposit accounts.

By contrast, the Commission requires money market fund advisers to manage their market and liquidity risks more directly -- by dramatically limiting the assets that can be held to only short term, high-quality assets.[8] The Commission also requires significant transparency into the characteristics of money market funds' assets.

These rules impose significant competitive disadvantages for money market funds, as these funds are expected to invest in instruments of shorter duration and generally lower risks, which typically means lower expected returns. The comparative advantage of money market funds is that they are able to avoid the burdens of explicit capital requirements or third-party insurance. Interestingly, despite the shorter duration and generally lower-risk holdings of money market funds, the net returns for investors are often somewhat greater than those provided by banks' interest-bearing accounts.

Over the past four decades, these differing approaches to what are essentially similar cash management tools have been prominently tested three times: (1) the Savings and Loan Crisis; (2) the 2008 Financial Crisis; and (3) the Pandemic Shutdown of 2020.

In the Savings and Loan Crisis, the significant flexibility afforded to banks for their investments proved fatal to many. In both of the latter two tests, the federal government engaged in extraordinary interventions to ensure that investors' assets were protected and the borrowers and issuers of financial products purchased by banks and money market funds continued to remain funded. However, the different vehicles have performed differently.[9]

For example, immediately after the 2008 financial crisis, many investor advocates trumpeted the success of the money market fund framework. As longtime investor advocate and prominent securities law professor Mercer Bullard explained to Congress in early 2009,

[6] Federal Deposit Insurance Corporation, *The Deposit Insurance Fund*, *available at* https://www.fdic.gov/deposit/insurance/ (viewed Apr. 8, 2021).

[7] *See, e.g.,* Letter from Paul Stevens, Investment Co. Institute, to Elizabeth Murphy, SEC, Jan. 10, 2011, *available at* https://www.sec.gov/comments/4-619/4619-49.pdf.

[8] We appreciate that the definition of "high quality" assets may be an imprecise exercise, and that ratings from nationally recognized statistical ratings organizations have rapidly deteriorated in times of broader market stress.

[9] See generally, Jonathan R. Macey.

> mutual funds have been a singular success story in the midst of the current financial crisis. Money market funds arguably have been the best illustration of this success.[10]

By contrast, essentially the entire banking system had to be bailed out. As Bullard continued

> As often happens when those who succeed are surrounded by failed competitors, however, some have responded to the failure of a single retail money market fund – the first in history – by demanding that money market funds be converted to and regulated as banks. A former Fed chairman explained this position as follows: "If they are going to talk like a bank and squawk like a bank, they ought to be regulated like a bank." The problem with this argument is that money markets do not fail like banks.[11]

But there was a money market fund that "broke the buck," and was forced to liquidate during that last crisis. As we all know by now, as the 2008 Financial Crisis was beginning to unfold, Lehman Brothers and several other large financial institutions continued to sell commercial paper into the markets, unabated by the Commission or other financial regulators who were increasingly aware of the dire financial challenges facing those firms. Ultimately, one large financial industry commercial paper issuer -- Lehman Brothers -- was not provided financial assistance by taxpayers, and so collapsed. As a result, one money market fund, the Reserve Primary Fund, which was over-exposed to Lehman Brothers debt, "broke the buck," and liquidated.

Less than a year later, the Commission proposed sweeping reforms for money market funds.[12] Then, in January 2010, the Commission adopted rules that, amongst other

---

[10] *Enhancing Investor Protection and the Regulation of Securities Markets Before the U.S. Senate Committee on Banking, Housing, and Urban Affairs*, 111th Cong. (2009) (Testimony of Mercer E. Bullard, Professor, University of Mississippi School of Law), *available at* https://www.banking.senate.gov/imo/media/doc/BullardTestimony31009.pdf.

[11] *Id. See also,* Mercer Bullard, *Money Market Funds on Life Support*, Morningstar Magazine, Oct. 3, 2012, *available at* https://www.morningstar.com/articles/569140/article ("The shoe yet to drop is the systemic risk created by driving MMF cash to banks... Placing additional burdens on MMFs will undoubtedly drive more cash to banks, over 3,000 of which have failed (compared with one retail MMF) since MMFs were first offered. Contrary to popular belief, banks pose risks for savers. Just ask retail depositors in the failed--but "insured"--IndyMac Bank who lost about 50% of their deposits above $100,000. They would have been far better off with a 1% loss in the Reserve Fund--which lost more money than any MMF in history."). *Accord, Oversight of the Mutual Fund Industry: Ensuring Market Stability and Investor Confidence: Hearing Before the Subcomm. on Investor Protection, Entrepreneurship, and Capital Mkts. of the House Fin. Serv. Cmte,* 112th Cong. (June 24, 2011), (Statement of Mercer Bullard), *transcript available at* https://financialservices.house.gov/UploadedFiles/112-42.pdf.

[12] *Money Market Fund Reform*, Sec. and Exch. Comm'n, 74 Fed. Reg. 32688 (July 8, 2009), *available at* https://www.sec.gov/rules/proposed/2009/ic-28807fr.pdf.

things, imposed significant liquidity requirements on money market funds, including that (i) "at least 10 percent of assets must be in cash, U.S. Treasury securities, or securities that convert into cash (e.g., mature) within one day," and "at least 30 percent of assets must be in cash, U.S. Treasury securities, certain other government securities with remaining maturities of 60 days or less, or securities that convert into cash within one week."[13]

Again, at least 30 percent of a money market fund's assets need to be in cash or securities that can turn into cash "within one week." The 2010 Reforms also imposed limits on the overall maturities of a fund's portfolio, including that the maximum weighted average portfolio maturity was shortened from 90 to 60 days, and the weighted average life of the portfolio is limited to 120 days.[14]

Further, the Commission explicitly required funds -- for the first time -- to hold sufficiently liquid securities to meet foreseeable redemptions.[15] Lastly, the 2010 Reforms further imposed minimum credit quality requirements, stress testing requirements, and monthly and other periodic disclosure requirements.[16]

These reforms fundamentally altered the risk profile of money market funds, and their operations. They also limited, to some degree, the potential returns for investors. Those regulatory actions were reasonable and appropriate, and ultimately strengthened an investor-friendly product. Importantly, these reforms put greater limitations on investments and transparency into liquidity on money market funds than are generally imposed upon banks.

One might expect that, having taken such dramatic action, the financial regulators would wait to see how those reforms would be implemented before future changes were proposed. That did not happen.

Instead, in late 2010, a council of leading financial regulators released the President's Working Group Report on Money Market Fund Reform,[17] which expressed support for the 2010 Reforms, but also suggested a number of further changes to the governance and operations of money market funds, including:

- Floating net asset values;
- Private emergency liquidity facility for money market funds;

[13] *Money Market Fund Reform*, Sec. and Exch. Comm'n, 75 Fed. Reg. 10060, 10106 (Mar. 4, 2010), *available at* https://www.sec.gov/rules/final/2010/ic-29132fr.pdf ("2010 Reforms").
[14] 2010 Reforms, at 10070.
[15] 2010 Reforms.
[16] 2010 Reforms.
[17] *President's Working Group Report on Money Market Fund Reform*, Sec. and Exch. Comm'n, Inv. Co. Act Rel. No. 29497, *available at* https://www.sec.gov/rules/other/2010/ic-29497.pdf.

- Mandatory redemptions in kind;
- Insurance for money market funds;
- A two-tiered system for money market funds, with enhanced limits for those with stable NAV;
- A two-tiered system for money market funds, with a stable NAV for only retail money funds;
- Regulating stable NAV money funds as special purpose banks; and
- Constraining less regulated money fund substitutes.[18]

After the enactment of the Dodd-Frank Act, the newly-created Financial Stability Oversight Council began pushing for further reforms to money market mutual funds. In 2012, the FSOC released a 73-page report on Proposed Recommendations Regarding Money Market Mutual Fund Reforms.[19] That report asserts that the FSOC might use its authority under Section 120 of the Dodd-Frank Wall Street Reform and Consumer Protection Act to compel the Commission to implement further reforms.[20] The FSOC sought comment on essentially three alternative recommendations:

1) Floating Net Asset Value;
2) Stable NAV with NAV Buffer and "Minimum Balance at Risk"; and
3) Stable NAV with NAV Buffer and Other Measures.[21]

Facing intense public pressure from the FSOC, a divided Commission adopted more changes to money market funds in 2014.[22]

The 2014 Reforms fundamentally changed the money market fund industry in a number of ways. Most notably, it imposed fees (but permitted a stable share price) for any prime or tax-exempt fund whose shareholders are limited to natural persons; and a floating share price and fees and gates for any prime or tax-exempt fund whose shareholders

[18] *President's Working Group Report on Money Market Fund Reform*, Sec. and Exch. Comm'n, Inv. Co. Act Rel. No. 29497, *available at* https://www.sec.gov/rules/other/2010/ic-29497.pdf.

[19] Financial Stability Oversight Council, *Proposed Recommendations Regarding Money Market Mutual Fund Reforms*, Nov. 2012, *available at* https://www.treasury.gov/initiatives/fsoc/Documents/Proposed%20Recommendations%20Regarding%20Money%20Market%20Mutual%20Fund%20Reform%20-%20November%2013,%202012.pdf.

[20] 2012 FSOC Report, at 5.

[21] 2012 FSOC Report, at 6.

[22] *Money Market Fund Reform; Amendments to Form PF*, Sec. and Exch. Comm'n, 79 Fed. Reg. 47736 (Aug. 14, 2014), *available at* https://www.govinfo.gov/content/pkg/FR-2014-08-14/pdf/2014-17747.pdf ("2014 Reforms").

are not so limited.[23] It essentially left government funds alone. At the time, Democratic Commissioner Kara Stein objected to the 2014 Reforms, in part out of concerns that the gates would likely serve as a new threshold which might itself precipitate destabilizing runs in advance of the potential closing of the gates.[24]

These changes were adopted on July 23, 2014, but did not take effect until October 14, 2016. While money market fund liquidity, stability, and transparency increased dramatically after the 2010 Reforms, the money market fund industry was upended by the 2014 Reforms.

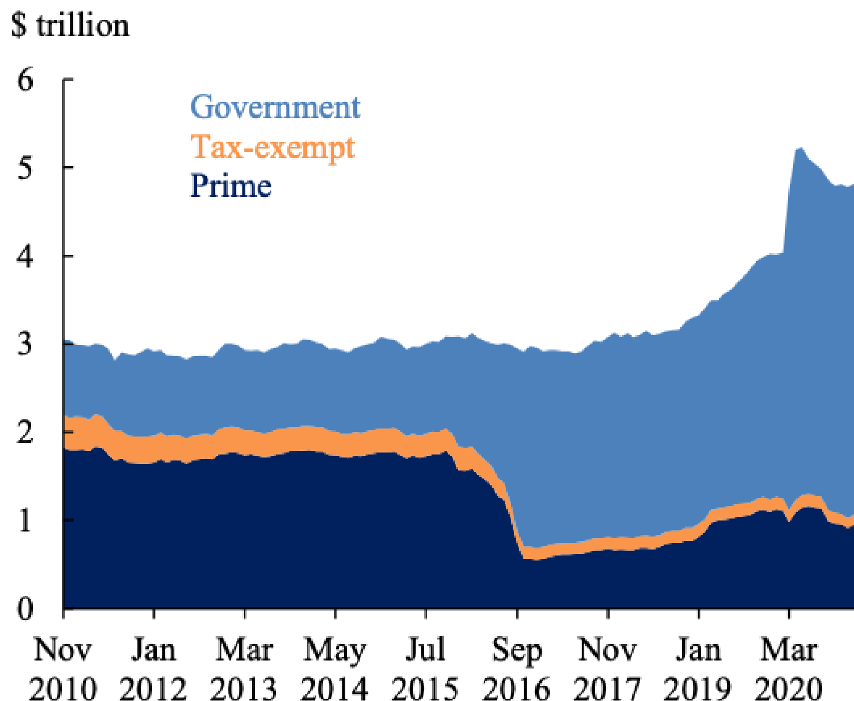
As shown in Figure 1 below, hundreds of billions of dollars flowed out of prime funds and into government funds. For example, there was about $1.8 trillion in prime funds in 2009, which fell to $1.27 trillion by the end of 2015 (after the adoption of the 2014 Reforms).[25] But as the 2014 Reforms came into effect in 2016, assets in prime funds cratered to just 0.37 trillion by the end of 2016. Meanwhile, assets in government funds were $1.1 trillion in 2009, and stayed relatively stable at $1.2 trillion in 2015. By the end of 2016, however, government funds totaled $2.2 trillion.

[23] At the time, SEC Chair Mary Jo White justified the distinction between "retail" and "institutional" money funds by explaining that "While the costs of a floating NAV can be justified against the demonstrable run risk in institutional prime funds, a different balance must be struck for retail and government funds." Statement of Hon. Mary Jo. White, SEC, July 23, 2014, *available at* https://www.sec.gov/news/public-statement/2014-07-23-open-meeting-statment-mjw.

[24] Statement of Hon. Kara M. Stein, July 23, 2014, *available at* https://www.sec.gov/news/public-statement/2014-07-23-open-meeting-statement-kms ("Ultimately, despite the rule's efforts to mitigate the risks posed by gates, I believe the incentives to avoid them will remain powerful. I fear these incentives may result in a greater chance of fire sales during times of stress, and a spread of the panic to other parts of our financial system, while also denying both investors and issuers access to capital.").

[25] Data excludes funds used as cash management tools for other mutual funds.

Figure 1: Prime MMF net assets dropped in March 2020, while government MMF assets grew substantiall



Source: Form N-MFP [26]

While the markets for prime funds and government funds used to be similarly sized, by 2019, there was approximately $2 trillion more in government funds than prime funds. As one looks above, it is clear that the overall level of money market fund assets stayed relatively stable at about $3 trillion dollars from 2010 through all of 2018, despite this massive shift in the composition of that total.

Put simply, a huge pool of assets that formerly had been purchasing high-quality, short-term corporate debt, switched over to buying government securities. Over a few months of 2016 -- and as a direct result of the 2014 Reforms -- nearly $900 billion came out of prime money market funds. We do not recall the banking regulators expressing concerns about the potential impacts of these sudden, massive outflows at the time.

In addition to impacting the funds, the changes impacted banks and investors. Many retail broker-dealers switched from using money market funds as their cash sweep vehicles for their customers and instead became affiliated with banks or developed their

[26] Viktoria Baklanova, Isaac Kuznits, and Trevor Tatum, *Prime MMFs at the Onset of the Pandemic: Asset Flows, Liquidity Buffers, and NAVs*, Sec. and Exch. Comm'n, at 1, Apr. 15, 2021, *available at* https://www.sec.gov/files/prime-mmfs-at-onset-of-pandemic.pdf ("SEC Staff Report").

own.[27] The returns on these accounts are generally much lower for investors than money market fund accounts had previously provided, with much of the difference being additional profits to the retail broker-dealer. In fact, for many retail brokers, this is now a significant source of revenues. For example, net interest margin became the largest revenue source in 2017 for Charles Schwab Corp, which was made possible

> through a combination of:
>
> - Gathering additional assets from new and current clients;
> - Transferring uninvested cash balances in certain client brokerage accounts to the bank sweep feature; and
> - Establishing the bank sweep feature as the default investment option for uninvested cash balances within all new Investors and Advisor Services brokerage accounts during 2016.[28]

There is no free lunch, and these new broker revenues are simply lost returns for investors.

Pandemic Shutdown of 2020

As the pandemic began to spread rapidly in the U.S., leading to a steep decline in business activity, demand for cash and safe assets led institutional investors of prime money market funds to redeem their holdings. Their preference and need for cash and flight-to-safety (e.g., investors' switching to treasuries), saw significant outflows from a wide swath of assets, including non-government money market funds.

Over a period of just a few days, many retail investors liquidated equities holdings, with the proceeds often being swept into government money market funds or bank accounts. Similarly, many corporate treasurers scrambled for cash, including liquidating market exposures and borrowing on lines of credit, again, with the funds often going into government money market funds and bank accounts. And, of course, some institutional investors (particularly corporate treasurers), pulled assets out of funds that were perceived as potentially imposing fees and gates (which had been required as part of the 2014 Reforms).

Prime money market funds recorded outflows of $125 billion in March 2020, representing about 11% of their assets, while government money market funds and

[27] Deposits at banks affiliated with broker-dealers grew from $679 billion in 2015 to $973 in 2019, while brokered deposits grew from $936 billion to $1.104 trillion.

[28] Charles Schwab Corp., 2017 Form 10-K, at 29 (noting that "In 2017 and 2016, average interest earning assets have grown by 14% and 21%, respectively, from the prior years.").

bank accounts experienced much, much greater net inflows.[29] For example, over just the two weeks surrounding the pandemic shutdown (March 11th to March 25th), government fund assets increased by nearly $600 billion.[30]

Notably, not all prime money market funds (or investors) reacted the same way. There were material variances in outflows from prime funds, based upon the fund sponsor type and size. As the Commission staff recently explained:

> the funds with advisers owned by the largest U.S. banks designated as global systemically important banks ("G-SIBs") accounted for 56% of the outflows in the third week of March even though these funds managed only around 28% of net assets in publicly offered prime institutional MMFs.[31]

We have not yet seen any federal financial regulators offer any hypotheses or detailed analysis of this disparity in outflows. Why were prime money market fund assets with sponsors that were systemically significant banks much more likely to withdraw? Similarly, we have seen little analysis into why smaller sponsors generally had more redemptions. If regulators are to make informed decisions, they should not ignore or readily dismiss these very obvious facts. At a minimum, the Commission should understand not just what happened, but why.

We understand that regulators and some have suggested that money market funds caused or materially contributed to the brief, but significant breakdown of the commercial paper market. In response, we offer four observations.

First, while the commercial paper market briefly froze, so did the vast majority of commerce and the overall economy.

Second, and most notably, when the regulatorily instigated massive outflows from prime money market funds occurred in 2016 (as a result of the 2014 Reforms), the commercial paper markets didn't freeze. Rather, as expected, those outflows arguably moderately increased some non-governmental borrowing costs.[32] As shown in Figure 1,

---

[29] Viktoria Baklanova, Isaac Kuznits, and Trevor Tatum, *Prime MMFs at the Onset of the Pandemic: Asset Flows, Liquidity Buffers, and NAVs*, Sec. and Exch. Comm'n, at 3, Apr. 15, 2021, *available at* https://www.sec.gov/files/prime-mmfs-at-onset-of-pandemic.pdf ("SEC Staff Report").

[30] Investment Co. Institute, *Money Market Mutual Fund Assets*, *available at* https://ici.org/research/stats/mmf (viewed Apr. 12, 2021).

[31] Viktoria Baklanova, Isaac Kuznits, and Trevor Tatum, *Prime MMFs at the Onset of the Pandemic: Asset Flows, Liquidity Buffers, and NAVs*, Sec. and Exch. Comm'n, at 3, Apr. 15, 2021, *available at* https://www.sec.gov/files/prime-mmfs-at-onset-of-pandemic.pdf ("SEC Staff Report").

[32] *See The Financial Stability Board's Implications for U.S. Growth and Competitiveness: Hearing Before the Subcomm. on Nat'l Sec., Int'l Dev. And Monetary Policy of the HFSC*, 114th Cong. (2016) (Statement of Paul Schott Stevens, Investment. Co. Institute), *available at* https://financialservices.house.gov/calendar/eventsingle.aspx?EventID=400076 ("We estimate that $910 billion dollars, so far, has left prime and tax-exempt MMFs. The cost to municipal finance, for short-term

those outflows continued for months and were several times greater than the outflows in March 2020.

Third, prime money market funds contributed less than one-fifth of the outflows from the commercial paper market. What about the other four-fifths? Don't we think that financial regulators should be focused on the market participants who comprised more than four-fifths of the outflows from the commercial paper markets?

Fourth, if we look at the financing rates of one-month commercial paper for the past few decades, the funding rates in March 2020 were, at the peak, far below averages during much of the late 1990s and early 2000s.

Interestingly, as the PWG Report acknowledges, "at the end of February, prime [money market funds] offered to the public owned about 19 percent of outstanding [commercial paper]," which was over a $1.1 trillion market.[33] Yet, over the two weeks of March in question, these funds cut their holdings of commercial paper by just $35 billion (about 3 percent of the then-outstanding commercial paper market).[34]

Are we to believe that a 3 percent outflow from the market caused the entire financing system to freeze and necessitate government intervention? This assumption is made even more dubious by the fact that much, much greater outflows from prime money market funds had occurred in 2016, but with muted effects on the commercial paper markets.

Nevertheless, in March 2020, the Board of Governors of the Federal Reserve System announced the creation of the Commercial Paper Funding Facility ("CPFF") and the Money Market Mutual Fund Liquidity Facility ("MMLF"). Both these facilities were supported by the Treasury Department's Exchange Stabilization Fund. By establishing the MMFL facility, the Federal Reserve Bank of Boston promised to "make loans available to eligible financial institutions secured by high-quality assets purchased by the financial institution from money market mutual funds."[35]

These actions were ostensibly aimed to "assist money market funds in meeting demands for redemptions by households and other investors, enhancing overall market functioning and credit provision to the broader economy."[36] Put simply, the Federal Reserve Bank of Boston promised to aid banks buying money market fund assets --

---

purposes, has risen 77 basis points. So, the predictions that we made about the impacts on markets, I think, have come true and much of that increase is as a result of changes in MMF rules. The costs in the short-term borrowing space have certainly risen, as we feared.").

[33] PWG Report, at 11, n.15.

[34] PWG Report, at 11.

[35] Press Release, *Federal Reserve Board broadens program of support for the flow of credit to households and businesses by establishing a Money Market Mutual Fund Liquidity Facility (MMLF)*, Board of Governors of the Federal Reserve System, Mar. 18, 2020, *available at* https://www.federalreserve.gov/newsevents/pressreleases/monetary20200318a.htm.

[36] *Id.*

even though money market funds weren't dipping below the 30 percent weekly liquidity levels, much less the 10 percent daily thresholds.[37] Notably, for the entire period of the stress and up through February 2021, the median weekly liquid asset percentages have been well in excess of 30 percent. It is currently over 50 percent. To the extent these facilities were used, regulators should examine what they were used for and why. For example, were they used to offload less-liquid assets, so that funds could maintain their weekly liquid asset thresholds, instead of tapping into them (as had been originally intended by regulators)? Were the rates more favorable than then-prevailing market rates?

Of course, at the same time the government was intervening in the money market funds business, the Federal Reserve and Treasury Department also intervened in nearly every aspect of the financing markets, including slashing interest rates and explicitly declaring an intention to buy even long-term debt securities and ETFs.

These and other actions dramatically impacted all aspects of the financial markets.

Since March 2020, these prolonged government interventions in the financial markets and the threat of yet more government regulatory intervention have had profound effects on the financial viability of operating a short-term funding vehicle -- and have further pressured money market fund advisers to exit the business.

Put another way, when interest rates are near zero, and you can only invest in very high-quality, short-term products, it is extremely difficult to cover expenses--much less provide returns to investors. This pressure is exacerbated by the significant regulatory pressure to have ultra-high weekly liquid asset ratios, as has been the case since last March.[38] Thus, it isn't surprising that the number of prime money market funds fell from 82 to 71 from February 2020 to February 2021.[39] The longer interest rates are artificially compressed, the lower that number will likely go.

[37] Once the facilities were created, money market funds advisers would be remiss to ignore them as potential avenues to quickly add liquidity to their holdings -- even if not necessary. In this regard, these programs were similar to other federal programs designed to mitigate the economic shock from the onset of the pandemic.

[38] As of February 2021, the median weekly liquid assets for prime money market funds was still over 50 percent. Viktoria Baklanova, Isaac Kuznits, and Trevor Tatum, *Prime MMFs at the Onset of the Pandemic: Asset Flows, Liquidity Buffers, and NAVs*, Sec. and Exch. Comm'n, at 4, Apr. 15, 2021, *available at* https://www.sec.gov/files/prime-mmfs-at-onset-of-pandemic.pdf ("SEC Staff Report").

[39] SEC Staff Report.

Concerns and Opportunities Going Forward

We join the Investment Company Institute,[40] Fidelity,[41] Blackrock,[42] and others in urging the Commission to reverse the tie between weekly liquid asset levels and fees and gates, which was imposed by the 2014 Reforms. Decoupling the liquidity percentages from the imposition of gates should be the Commission's top priority in modernizing money market fund rules.

The linkage between liquidity percentages and gates creates a strong incentive for investors to run, if they see the fund nearing the gate threshold. By openly sharing a point at which investors are likely to be entirely blocked from accessing their cash, and requiring the disclosure of the liquidity percentages, the Commission has provided the kindling for a potential panic.

It is clear that, in March 2020, some investors moved assets to bank accounts and government funds as prime funds' disclosures suggested that they were approaching the 30% liquidity threshold where a redemption fee may be imposed.[43]

Commissioner Stein's primary fear of the 2014 Reforms proved well-founded: the policy that was supposed to prevent runs appears to have precipitated a run. This isn't a hunch. It's what the corporate treasurers who pulled assets from prime funds have said. For example, one survey found that 87 percent of the corporate treasurers who reduced their prime money market fund holdings in March 2020 (which was about half of the treasurers surveyed) cited potential redemption hurdles as one of the drivers of their reduction.[44]

Neither inciting the panic nor blocking investors from their capital protects investors or promotes fair and efficient capital markets overall.

Rather than blocking investors from accessing their funds, we believe that the Commission should consider further delineating requirements on money fund boards to

---

[40] Letter from Eric Pan, Inv. Co. Inst., to Vanessa Countryman, SEC, Apr. 12, 2021, *available at* https://www.sec.gov/comments/s7-01-21/s70121-8662926-235321.pdf.
[41] Letter from Cynthia Lo Bessette, Fidelity, to Vanessa Countryman, SEC, Apr. 12, 2021, *available at* https://www.sec.gov/comments/s7-01-21/s70121-8662947-235324.pdf.
[42] Letter from Thomas Callahan and Kate Fulton, Blackrock, to Vanessa Countryman, SEC, Apr. 12, 2021, *available at* https://www.sec.gov/comments/s7-01-21/s70121-8662484-235306.pdf.
[43] We also note that sudden reductions of corporate and other organizational revenues arising from the coronavirus shutdowns, coupled with the need to make regular outflows for things like payroll and rent, led to a rapid retreat of institutional cash inflows. This is not at all surprising, and would be expected from similar customers regardless of whatever cash-like products they were using. Put simply, much of the net outflows was simply the result of lower inflows.
[44] The Carfang Group, Corporate Treasurer Response to March Market Collapse, *available at* https://61fccc29-49c7-4ff3-abc8-c5ae702f30ad.usrfiles.com/ugd/61fccc_5a7dab46e991401fa2ab907d2fee2d7a.pdf.

have policies and procedures to consider and adopt fees in moments of potential extreme fund or market turmoil.

We also urge the Commission to consider further tweaks to the 2010 Reforms, including the weekly liquid assets threshold. In March 2020, as some prime money market funds approached the 30 percent weekly liquid assets threshold, the funds responded by selling their *other assets*, essentially not using their buffer. While this had the effect of keeping the funds above the threshold, it had the perverse effect of causing those funds to sell their least liquid assets during a time of stress. This is the opposite of what we should hope. At root, the point of having liquid assets is to be able to sell them to meet redemptions in times of stress, and avoid potential fire sales of less liquid assets.

The Commission should focus on money market funds as they exist today in the short term funding markets. The assets in, and compositions of, money market funds are very different than they were in 2008, much less 2014. At the time the Commission adopted the 2014 Reforms, the agency noted that there were 559 money market funds registered with the agency, and their holdings were approximately $3.0 trillion.[45] The slight majority of these assets were in prime funds. That is no longer the market. As described above, as of 2019, approximately 80 percent of the assets are in government funds, with prime funds comprising approximately 15 percent of the total assets.

We are disappointed that the reforms fail to accurately reflect these changes.

We are specifically concerned with many of the so-called reform ideas, including tweaking the use of gates or minimum balance at risk revisions. These provisions would simply block investors' access to their funds. This dramatically undermines the utility of the product, in part because it directly harms -- rather than protects -- investors. Similarly, swing pricing would be extremely difficult -- if not impossible -- to effectively administer.

Other reform ideas focus more directly on the concept of insurance. These include "self-insurance" approaches like capital buffers within the funds or sponsor support by the advisers. But these also include proposals to create external insurance (such as the Federal Deposit Insurance Corporation), for money market funds. While we understand the initial appeal of these approaches -- particularly for those who most frequently focus on banking regulation -- we again remind the Commission that the liquidity and transparency requirements adopted in 2010 are far more rigorous than those currently generally imposed on banks by banking regulators. It should be easy to see how third-party insurance is essential in the banking context, but not in the context of money market funds.

[45] 2014 Reforms, at 47737.

Conclusion

Regulators should examine the short term funding markets and consider reforms to securities lending practices, broker-dealer capital requirements, and other reforms -- including reforms that promote the stability and liquidity of money market funds.

If the Commission and other regulators wish to eradicate money market funds, they are fully capable of doing so. But we urge you to do so knowingly, not under the guise of some “capital buffer” or other structural reforms, and acknowledge that it will come at a cost to investors, businesses, and state and local governments who may otherwise benefit from their short term funding.

Thank you for your consideration. Should you have any questions or would like to discuss these matters further, please contact me at (202) 909-6138.

Sincerely,

Tyler Gellasch
Executive Director