sifma

asset management group

August 16, 2021

Via email to fsb@fsb.org

Financial Stability Board

Re: **Money Market Fund ("MMF") Policy Proposals**

The Asset Management Group of the Securities Industry and Financial Markets Association ("**SIFMA AMG**")[1] respectfully submits this comment letter to the Financial Stability Board (the "**FSB**") with respect to the FSB's request for comment on policy proposals to enhance MMF resilience, as highlighted in the FSB's consultative report dated June 30, 2021 (the "**FSB Report**").[2] We appreciate the opportunity to provide our views to the FSB on these matters that have the potential to impact not only the direct regulation of MMFs, but also the overall functioning of the short-term funding markets.

SIFMA AMG thanks the FSB for the opportunity to comment on potential reform measures for MMFs. SIFMA AMG recognizes the critical importance of ensuring the resiliency of MMFs and the important role that MMFs play in the short-term funding markets. We applaud the FSB for taking steps to evaluate how the resiliency of MMFs may be further improved, after taking into account the impact of previously enacted reforms, the role of MMFs in the overall short-term funding markets, jurisdiction-specific factors, and engaging with the industry and conducting appropriate studies in doing so.

I. Executive Summary

The comments contained herein are focused on the experiences of U.S. MMFs regulated under Rule 2a-7 of the Investment Company Act of 1940, as amended ("**1940 Act**"), and the applicability of policy proposals to such MMFs. SIFMA AMG encourages any final report issued by

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[1] SIFMA AMG brings the asset management community together to provide views on policy matters and to create industry best practices. SIFMA AMG's members represent U.S. and multinational asset management firms whose combined global assets under management exceed $39 trillion. The clients of SIFMA AMG member firms include, among others, tens of millions of individual investors, registered investment companies, endowments, public and private pension funds, UCITS and private funds such as hedge funds and private equity funds.

[2] FINANCIAL STABILITY BOARD, POLICY PROPOSALS TO ENHANCE MONEY MARKET FUND RESILIENCE, CONSULTATION REPORT (June 30, 2021), *available at* https://www.fsb.org/wp-content/uploads/P300621.pdf [hereinafter FSB Report].

the FSB to recognize the flexibility for national regulators to implement policy recommendations appropriately in individual jurisdictions, taking into account jurisdiction-specific factors that may impact the effectiveness of any policy options. As more fully discussed herein, SIFMA AMG strongly views delinking liquidity thresholds and liquidity fees and redemption gates as the most effective means to enhance MMF resilience and an integral part of any final report issued by the FSB and any rulemaking package. SIFMA AMG strongly supports the exclusion of "government MMFs" under Rule 2a-7 from the scope of the policy proposals and future rulemaking. Government MMFs are an increasingly valuable and popular liquidity vehicle for investors, which has been highlighted by their resiliency and significant inflows during the market stresses in March 2020. As a general matter, SIFMA AMG strongly opposes bank-like policy measures, as measures that seek to add capital to MMFs will not address the liquidity issues faced by the markets, including MMFs, in March 2020 and are therefore not responsive to, nor an effective means to address, the events of March 2020. The impact of such bank-like measures has the potential to limit the availability of highly regulated and transparent vehicles that offer important cash management solutions to individual investors and institutions; as well as limit the availability, and increase the costs of, efficient financing for businesses, corporations, financial institutions, hospitals, universities, and state and local governments.

SIFMA AMG is supportive of the complementary measures on risk monitoring and short-term funding markets included in the FSB Report. SIFMA AMG applauds the FSB's recognition that MMF reforms by themselves will not likely solve the structural fragilities in the short-term funding markets and supports a holistic approach to reform that includes consideration of measures to improve the functioning of commercial paper and certificate of deposit markets.

SIFMA AMG's comments on the specific policy options included in the FSB report focus on the following:

- Removal of ties between regulatory thresholds and imposition of liquidity fees and redemption gates. SIFMA AMG strongly supports the delinking of MMF liquidity and fee and gate thresholds. Our members view this policy measure as most directly and meaningfully addressing, in a practical manner, the issues that contributed to stresses on MMFs and the short-term funding markets in March 2020. SIFMA AMG believes delinking liquidity and thresholds for liquidity fees and redemption gates is an essential element of any final report issued by the FSB. SIFMA AMG agrees with delinking as the "representative option" vis a vis the extensions and variants included in this category (authorities approving activation of fees and gates, MMF investor concentration limits, and countercyclical liquidity buffers).

- Limits on eligible assets. While in principle SIFMA AMG does not generally oppose certain limits on eligible assets, many of our members believe these changes will be less effective than the delinking of liquidity and fees and gates in addressing the specific issues presented in March 2020 and enhancing MMF resiliency. Should limitations on eligible assets be considered as part of a policy package, SIFMA AMG believes any such changes should be focused on the types of MMFs that experienced higher redemptions in March 2020 (i.e., institutional prime MMFs) and be part of a reform package that includes the delinking of liquidity with liquidity fees and redemption gates. SIFMA AMG generally opposes the related variants and extensions (limiting MMFs to government MMFs, redemption in-kind, non-daily dealing, and liquidity-based redemption deferrals) because such variants and extensions significantly curtail investors' access to liquidity and the use of MMFs as a valuable cash management vehicle for many different types of investors. These extensions and variants, in turn, will likely result in a decrease in the size of the MMF sector, thereby impairing the functioning of the overall short-term funding markets.

- Additional liquidity requirements and escalation procedures. While in principle SIFMA AMG does not generally oppose additional liquidity requirements and escalation procedures, many of our members believe these changes will be less effective than the delinking of liquidity and fees and gates in addressing the specific issues presented in March 2020 and enhancing MMF resiliency. Should additional liquidity requirements and escalation procedures be considered as part of a policy package, SIFMA AMG believes any such changes should be focused on the types of MMFs that experienced higher redemptions in March 2020 (i.e., institutional prime MMFs) and be part of a reform package that includes the delinking of liquidity with liquidity fees and redemption gates.

- Swing pricing. SIFMA AMG does not support swing pricing requirements for MMFs and believes that implementing swing pricing requirements for MMFs would be ineffective in achieving the goals for reform included in the FSB Report. Swing pricing is less effective in achieving its intended goals in the MMF context as compared to other open-end mutual funds due to fundamental differences between redemption activity and related transaction costs of MMFs as compared to other types of open-end mutual funds, including that MMFs routinely handle large redemptions without similar transaction costs that may be borne by other types of open-end mutual funds. Swing pricing presents significant operational impediments in implementation due to the settlement process for MMFs and also presents significant costs and burdens associated with implementation. Swing pricing would likely also result in the elimination of intraday settlement and impede a MMF's ability to ensure same-day settlement, a key feature and benefit for various types of investors. SIFMA AMG believes the variant or extension presented in the FSB Report — authorities mandating macroprudential swing pricing — presents even further challenges than the swing pricing representative option and SIFMA AMG therefore also does not support such variant.

- Bank-like requirements. SIFMA AMG strongly opposes bank-like requirements for MMFs, such as minimum balance at risk ("**MBR**") requirements, capital buffers, requiring liquidity exchange bank ("**LEB**") membership, or requiring sponsor support. Using loss absorption as the mechanism to enhance MMF resilience, as contemplated by the bank-like requirements, is not responsive to (and therefore not effective in addressing) the liquidity stresses that arose in March 2020, particularly given that all U.S. MMFs met 100% of redemptions and no U.S. MMFs "broke the buck," despite increased redemption activity in March 2020. Such bank-like requirements would have the effect of eliminating or significantly decreasing the size of the MMF sector, thereby impairing the resilience and orderly functioning of the short-term funding markets. SIFMA AMG urges the advancement of market-driven regulatory solutions rather than bank-driven measures.

- Removal of stable net asset value. SIFMA AMG generally opposes the removal of stable net asset values for applicable MMFs because such policy measure does not address the types of MMFs that experienced the largest outflows in March 2020 and the implementation of a floating net asset value for institutional prime MMFs did not prove effective in slowing redemptions in March 2020. Many of our members generally do not view this policy measure as increasing the resilience of MMFs in a meaningful way that outweighs the drawbacks of such policy measure, and find such policy measure not responsive to (and therefore not effective in addressing) the market-wide liquidity stresses that arose in March 2020.

Enclosed is a copy of the comment letter submitted by SIFMA AMG to the U.S. Securities and Exchange Commission (the "**Commission**") with respect to the Commission's request for comment on potential reform measures for MMFs, as highlighted in the Report of the President's Working Group on Financial Markets dated December 2020 (the "**PWG Report**").[3] Specifically with respect to SIFMA AMG's comments on the PWG Report, we would like to highlight the following main points:

1. The important role of MMFs and the effectiveness of previously enacted reforms to Rule 2a-7. MMFs play an important role in the orderly functioning of the short-term funding markets and serve valuable financial and economic functions for a variety of investors (including both retail and institutional investors) and the capital markets more broadly. Policy measures that have the effect of eliminating or significantly decreasing the size of the any portion of the MMFs sector will significantly impair the resilience and orderly functioning of the short-term funding markets.

   As a result of reforms adopted in the United States after the global financial crisis, MMFs proved to be more liquid, resilient, and able to handle the stresses of March 2020. These prior reforms helped ensure all types of institutional and retail MMFs, including government, prime, and tax-exempt MMFs, were able to successfully manage the unprecedented liquidity challenges in March 2020 and provide investors with daily liquidity and meet 100% of redemptions. Certain aspects of the reforms adopted in 2014, mainly the linking of levels of liquidity with the ability to impose liquidity fees and redemption gates, proved to have negative unintended consequences that amplified the redemption behavior exhibited by certain types of prime MMF investors (most notably, institutional prime MMF investors) in response to the market-wide lack of liquidity that arose in March 2020. Accordingly, the delinking of liquidity thresholds from the imposition of liquidity fees and redemption gates should be the focus of any potential future rulemaking.

   For a further discussion of the important role of MMFs in the short-term funding markets, please see Section II of SIFMA AMG's comments on the PWG Report. For a further discussion of the effectiveness of previously enacted reforms to Rule 2a-7, please see Section III of SIFMA AMG's comments on the PWG Report.

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[3] Request for Comment on Potential Money Market Fund Reform Measures in President's Working Group Report, Investment Company Act Release 34188 (Feb. 4, 2021), *available at* https://www.sec.gov/rules/other/2021/ic-34188.pdf.

2. The liquidity crisis in March 2020 and a narrowly tailored MMF policy response. An unprecedented and rapidly developing market-wide liquidity crisis occurred in March 2020 fueled by the COVID-19 pandemic. MMFs were not the root cause of the stresses in the short-term funding markets in March 2020, but, rather, like other participants in the short-term funding markets, were reacting to and managing through a market-wide liquidity crisis. Policy responses to the liquidity crisis in March 2020 should focus on and prioritize addressing root causes in the segments of the short-term funding markets that caused market stresses in March 2020. Any policy measures should be narrowly tailored, data driven, simple to understand and implement, and calibrated to address the liquidity pressures that manifested in a relatively small segment of the MMF industry in a manner that preserves the viability of such products for investors.[4] A broadly tailored, "one-size-fits-all" approach is not appropriate based on the data derived from the market stress events of March 2020 and would invite the potential for far-reaching, unintended consequences and potential harm to the functioning of the short-term funding markets.

   For a further discussion of the liquidity crisis in March 2020, please see Section IV of SIFMA AMG's comments on the PWG Report.

II. Types of "Vulnerabilities" in MMFs

The FSB Report identifies two main types of vulnerabilities in MMFs: (1) susceptibility to sudden and disruptive redemptions that arises from the interaction of several characteristics of MMFs (particularly non-government MMFs), and (2) challenges in selling assets to meet significant redemptions.[5]

With respect to the first perceived vulnerability, susceptibility to redemptions, the FSB Report notes that this arises due to liquidity transformation; the use of MMFs for cash management and investor expectations that cash-like features of MMFs will be maintained at all times; exposure to credit risk; regulatory thresholds that may cause investors to preemptively redeem; and the potential for certain types of investors, namely institutional investors, to amplify redemption risks. The FSB Report states that together, these features can contribute to a first-mover advantage for redeeming investors in a stress event and make MMFs susceptible to runs.[6] With respect to the

[4] As further discussed herein, although SIFMA AMG believes policy measures should be narrowly tailored to address the liquidity pressures experienced by a relatively small segment of the MMF industry, SIFMA AMG supports applying the delinking policy measure discussed below to all types of MMFs that are currently subject to liquidity fees and redemption gates as the dynamics that motivate redemptions in the face of a bright line liquidity threshold that is tied to a liquidity fee or redemption gate apply regardless of the type of MMF.

[5] *See* FSB Report, *supra* note 2 at 22-24.

[6] *See id.* The FSB Report defines first-mover advantage as follows:

> First-mover advantage occurs as when, under certain circumstances, investors who redeem their shares first do so on more favorable terms than investors in the same fund who redeem late. It can occur if, for example, the transaction costs for assets sold to meet redemptions are not properly allocated to redeeming investors. Another example of the first-mover advantage occurs if in a scenario of declining values of a fund's assets, investors can redeem before the fund's net asset value adjusts to fully reflect those declines in value. An investor who redeems solely in anticipation of further market deterioration is not considered as benefiting from a first-mover advantage. First mover advantage may lead to pre-emptive runs.

second perceived vulnerability, challenges in selling assets to meet significant redemptions, the FSB Report notes that this arises because MMFs hold financial instruments that may have limited liquidity, particularly in stressed conditions.[7]

SIFMA AMG agrees with the FSB's characterization that the perceived vulnerabilities listed in the FSB Report are less applicable, or inapplicable, to government MMFs and therefore SIFMA AMG strongly supports the exclusion of government MMFs from future rulemaking. For example, government MMFs' holdings tend to be more liquid and exhibit less credit risk than other types of MMFs' holdings, thereby reducing liquidity transformation and exposure to credit risk. Government MMFs provide investors with a stable, attractive investment option and are widely viewed as among the safest and most liquid investment options for various types of investors.

Data from March 2020 also supports the exclusion of government MMFs from future rulemaking. In March 2020, U.S. government MMFs saw large inflows of over $830 billion as government MMFs became a vehicle of choice to help preserve liquidity during the liquidity crisis.[8] This reinforces the high regard that all types of investors have for government MMFs and such MMFs' attraction as a valuable safe haven in times of uncertainty.

These different risk characteristics and experiences of government MMFs have been previously recognized by the Commission and appropriately taken into account in structuring MMF reforms.[9] SIFMA AMG strongly urges regulators to consider the different risk profiles and experiences of government MMFs in times of stress and exclude government MMFs from future MMF rulemaking.

SIFMA AMG members question the underlying premise of first mover advantage as a causal factor in connection with shareholder redemptions, particularly in the context of the liquidity crisis of March 2020. Our members do not necessarily view first mover advantage as a motivating factor

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See id. at 61.

[7] *See id.* at 22-24.

[8] *See* INVESTMENT COMPANY INSTITUTE REPORT OF THE COVID-19 MARKET IMPACT WORKING GROUP, EXPERIENCES OF US MONEY MARKET FUNDS DURING THE COVID-19 CRISIS 12 (2020), *available at* https://www.sec.gov/comments/credit-market-interconnectedness/cll10-8026117-225527.pdf [hereinafter ICI COVID-19 REPORT].

[9] For example, the Commission has stated:

> … [G]overnment money market funds face different redemption pressures and have different risk characteristics than other money market funds because of their unique portfolio composition. The securities primarily held by government money market funds typically have a lower credit default risk than commercial paper and other securities held by prime money market funds and are highly liquid in even the most stressful market conditions. As noted in our proposal, government funds' primary risk is interest rate risk; that is, the risk that changes in the interest rates result in a change in the market value of portfolio securities. Even the interest rate risk of government money market funds, however, is generally mitigated because these funds typically hold assets that have short maturities and hold those assets to maturity.
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> As discussed in the DERA Study and below, government money market funds historically have experienced inflows, rather than outflows, in times of stress. In addition, the assets of government money market funds tend to appreciate in value in times of stress rather than depreciate.

Money Market Fund Reform; Amendments to Form PF, Investment Company Act Release No. 31166 (July 23, 2014) at 204, available at www.sec.gov/rules/final/2014/33-9616.pdf [hereinafter 2014 Adopting Release].

for redemptions in connection with the MMF redemptions experienced in March 2020 (i.e., redemption behavior was not driven by a fear that another shareholder would redeem and impose costs on the MMF and remaining shareholders) and, thus, encourage regulators to focus on regulatory reforms that more directly address the stresses experienced by MMFs and the larger short-term funding markets in March 2020.

a. Susceptibility to Redemptions

As an initial matter, with respect to the susceptibility to sudden and disruptive redemptions for non-government MMFs, SIFMA AMG notes that inflows into U.S. government MMFs in March 2020 represented flows from investors of all types, including sources other than investors moving from prime MMFs into government MMFs. In fact, other funds that are active in the short-term funding markets, such as ultra-short bond funds, experienced unprecedented redemptions in March 2020.[10] As recognized by the FSB, this highlights that the market flows represent not only strategic outflows from prime MMFs, specifically, into government MMFs, but also a larger market-wide liquidity crisis and overall flight to safety.[11] In considering MMFs' susceptibility to redemptions, it is important to take into consideration the fact that the redemption and liquidity pressures experienced by MMFs in March 2020 were not specific to, or caused by, MMFs, but, rather, were part of a market-wide liquidity issue experienced by the larger short-term funding market.

SIFMA AMG agrees that MMFs perform liquidity transformation (meaning that redemption terms for MMF shares are not necessarily aligned with the liquidity of the assets they hold) and are used for valuable cash management purposes, but highlights that certain features that enable liquidity transformation and MMFs' use for cash management purposes (such as same day settlement) are key characteristics of MMFs that provide significant operational efficiencies and benefits for investors that should be maintained. Further, MMFs currently have restrictions and tools in place designed to help manage redemptions in a manner that still preserves these key features of MMFs.[12] Eliminating certain features of MMFs that enable MMFs to be used for valuable cash management purposes, such as same day settlement (either directly or indirectly through the adoption of policy measures incompatible with such features), would have detrimental consequences for investors, including, for example, retail investors needing immediate access to cash

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[10] *See, e.g.,* Randal K. Quarles, Vice Chair for Supervision and Chair of the Financial Stability Board, Speech at the Peterson Institute for International Economics, The FSB in 2021: Addressing Financial Stability Challenges in an Age of Interconnectedness, Innovation, and Change (Mar. 30, 2021), *available at* https://www.federalreserve.gov/newsevents/speech/quarles20210330a.htm. Further, weekly outflows from bond funds reached record levels of $109 billion. FINANCIAL STABILITY BOARD, HOLISTIC REVIEW OF THE MARKET TURMOIL 21 (Nov. 17, 2020), *available at* https://www.fsb.org/wp-content/uploads/P171120-2.pdf.

[11] *See* FINANCIAL STABILITY BOARD, HOLISTIC REVIEW OF THE MARKET TURMOIL 21 (Nov. 17, 2020), *available at* https://www.fsb.org/wp-content/uploads/P171120-2.pdf. ("These inflows were partly attributable to a reallocation from prime MMFs and other short-term funding market investors, but also driven by disinvestments from other less-liquid asset classes in order to meet demand for cash. Corporates and households also increased their deposits at banks (deposits at US banks increased by around US$476 billion over the course of March)."). When viewed in the context of not only the large inflows into government MMFs, but also the large inflows into bank and broker deposits, outflows from prime and tax-exempt MMFs comprised an even smaller small percentage of the overall flight to quality. This further reinforces how the market stresses in March 2020 were not specific to, nor caused by, prime and tax-exempt MMFs.

[12] For example, MMFs have strict portfolio limitations with respect to minimum levels of liquidity and certain types of MMFs may impose a liquidity fee upon certain occurrences.

such as in a medical emergency or when purchasing a home, and state and local governments that need to make payroll or service bond payments when due. SIFMA AMG members do not view these "vulnerabilities" (liquidity transformation or use as cash management vehicles) as items that regulators should seek to eliminate, but, rather, views these as key characteristics of the MMF wrapper that regulators should seek to preserve, while ensuring MMFs have tools in place to help manage redemptions.

In previously adopting amendments to Rule 2a-7, the Commission recognized the importance of these key features and structured reforms to provide MMFs with tools to manage redemptions while also purposefully preserving "the ability of [MMFs] to function as an effective and efficient cash management tool for investors."[13] SIFMA AMG encourages any final report issued by the FSB to take a similar approach to any future MMF reforms and to structure reforms to preserve the ability of MMFs to function as an effective and efficient cash management tool for investors.

The FSB Report notes investor expectations that cash-like features of MMFs will be maintained at all times; SIFMA AMG, however, highlights investor awareness of MMFs as an investment vehicle for which certain cash-like features may not be maintained at all times. The fact that MMFs are subject to potential loss, in return for a market return on their short-term investments, is clearly disclosed in U.S. MMFs' offering documents and advertisements, as required by current U.S. regulations.[14] In addition, a U.S. MMF's prospectus is required to disclose specific information regarding a MMF's redemption procedures, including related to circumstances under which a MMF may delay honoring a redemption request; the number of days following receipt of shareholder redemptions in which a MMF typically expects to pay out redemption proceeds to redeeming shareholders; and methods a MMF typically expects to use to meet redemption requests, including in stressed market conditions.[15] As such, while MMFs are used as a cash management solution, there are current U.S. regulatory requirements in place that appropriately and adequately disclose to investors the limitations on a MMF's cash-like features.

With respect to MMFs as a cash management solution, SIFMA AMG also notes that MMFs provide investors with an important highly regulated alternative to bank accounts and to less regulated and less transparent liquidity vehicles. This is increasingly important to the extent banks may be unable or unwilling to accept additional deposits due to capital requirements, as MMFs can be used to fill an important gap in the market and provide a safe, highly regulated alternative.[16]

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[13] 2014 Adopting Release, *supra* note 9 at 12-13 ("The 2013 proposal sought to address certain features in money market funds that can make them susceptible to heavy redemptions, by providing money market funds with better tools to manage and mitigate potential contagion from high levels of redemptions, increasing the transparency of their risks, and improving risk sharing among investors, and also to preserve the ability of money market funds to function as an effective and efficient cash management tool for investors").

[14] Item 4(b) of Form N-1A requires:

> You could lose money by investing in the Fund…An investment in the Fund is not insured or guaranteed by the Federal Deposit Insurance Corporation or any other government agency. The Fund's sponsor has no legal obligation to provide financial support to the Fund, and you should not expect that the sponsor will provide financial support to the Fund at any time.

See also 17 C.F.R. § 230.482(a)(4) (2021).

[15] *See* Item 11(c) of Form N-1A.

[16] This is especially relevant given the Federal Reserve's announcement that the Federal Reserve will not extend a

Should certain types of MMFs no longer exist or should policy measures eliminate certain cash management features of MMFs, and banks are unable to accept additional deposits (or penalize some investors for increasing deposits), investor choice for cash management vehicles would be severely curtailed. Further, this may drive money into other types of cash pools that are less regulated, to markets that are outside a specific jurisdiction's regulatory oversight, or to products that otherwise introduce increased investment risk, and would increase risks to shareholders and to the financial markets.[17] The transparency offered by MMFs as a result of the extensive disclosure requirements to which MMFs are subject allows regulators to effectively monitor developments in MMFs generally, as well as with respect to specific individual MMFs.[18] To the extent reforms eliminate key characteristics of MMFs that make MMFs attractive to investors as cash management solutions and cause money to flow from MMFs into less transparent vehicles, regulators would potentially have less transparency into the front-end of the yield curve which could prove increasingly challenging to regulators and impede regulators' efforts, particularly during a time of market stress.

Further, while MMFs' use as a cash management solution may vary based on investor type and SIFMA AMG encourages a tailored approach to rulemaking, the combination of principal stability or low principal volatility, liquidity, and payment of short-term yields, has nonetheless made MMFs a valuable cash management tool for both retail and institutional investors.[19] In this regard, SIFMA AMG highlights the value in providing a highly regulated cash management solution to all types of investors. As previously recognized by the Commission, MMFs suitability for cash management operations has made MMFs popular among corporate treasurers, municipalities, and other institutional investors, some of which rely on MMFs for their cash management operations because MMFs provide diversified cash management more efficiently due both to the scale of their operations and the expertise of MMFs managers, particularly where certain investors may not have readily available resources to analyze the credit quality of every security themselves.[20] Our members believe it is important to retain MMFs' features that enable MMFs to serve as a valuable cash management solution for all types of investors.

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temporary exemption that impacts the amount of capital banks must keep in reserve. *See* Board of Governors of the Federal Reserve System, "Federal Reserve Board Announces that the Temporary Change to its Supplementary Leverage Ratio (SLR) for Bank Holding Companies Will Expire as Scheduled on March 31" (March 19, 2021), *available at* https://www.federalreserve.gov/newsevents/pressreleases/bcreg20210319a.htm. If a bank is in danger of breaching capital requirements, banks may stop taking deposits, which count on their balance sheets as assets.

[17] This concern has been previously recognized by the Commission. *See* 2014 Adopting Release, *supra* note 9 at 74. We note that given the less regulated, and therefore less transparent, nature of other types of cash pools, it is difficult to analyze the amount of money that flowed out of MMFs regulated under Rule 2a-7 and into such products in connection with the implementation of the 2014 amendments to Rule 2a-7. We further note that while government MMFs saw significant inflows in conjunction with outflows from prime MMFs upon implementation of the 2014 amendments to Rule 2a-7, it is difficult to determine whether those flows remained in government MMFs or ultimately went to less regulated products.

[18] For example, MMFs are required to publicly file detailed monthly portfolio holdings reports with the Commission; publicly file on Form N-CR with the Commission within one business day of the occurrence of certain material events; and post prominently on its website monthly portfolio holdings and other fund information and daily information on levels of daily liquid assets, weekly liquid assets, inflows and outflows, and the MMF's shadow price.

[19] *See* 2014 Adopting Release, *supra* note 9 at 7.

[20] *See id.* at 27.

With respect to exposure to credit risk, SIFMA AMG highlights the Commission's adoption of amendments to Rule 2a-7 in 2010 and 2015 to strengthen MMFs' resiliency to credit risks.[21] Under current U.S. regulations, MMFs must limit their investments to (i) securities that at the time of acquisition are determined to present "minimal credit risks," which determination must include an analysis of the capacity of the security's issuer or guarantor to meet its financial obligations and such analysis must include certain prescribed factors, to the extent appropriate; (ii) securities that are issued by another registered MMF; or (iii) government securities.[22] In 2015, the Commission also provided additional guidance on specific credit or asset quality factors to be taken into consideration in making a determination about the eligibility of securities for purchase by MMFs.[23] Moreover, Rule 2a-7 requires advisers to provide an ongoing review of whether each security (other than a government security) continues to present minimal credit risks, which review must include certain assessments prescribed by Rule 2a-7.[24] These reforms were adopted in response to the credit crisis in 2008 when a MMF "broke the buck" following the announcement of Lehman Brothers Holdings Inc.'s bankruptcy. These reforms were intended to increase the overall resiliency of MMFs in light of such credit event, and these reforms have been successful in appropriately and adequately limiting a MMF's exposure to credit risk. SIFMA AMG highlights that the events of March 2020 were related to liquidity stresses, and not credit issues, and any policy response should be appropriately tailored to the liquidity stresses experienced in March 2020.

SIFMA AMG agrees that regulatory thresholds, namely the linking of liquidity fees and redemption gates to specified levels of liquidity, cause investors to redeem to avoid the consequences of a MMF crossing such threshold.[25] SIFMA AMG believes this is a primary reason that certain MMFs exhibited susceptibility to redemptions in March 2020. In March 2020, outflows from institutional prime MMFs increased as the level of weekly liquid assets dropped closer to 30% as institutional investors sought to avoid the potential of being invested in a MMF that may impose a liquidity fee or redemption gate.[26] This dynamic, in turn, prevented MMFs from using their weekly

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[21] *See* Removal of Certain References to Credit Ratings and Amendment to the Issuer Diversification Requirement in the Money Market Fund Rule, Investment Company Act Release No. 31828 (Sept. 16, 2015), *available at* https://www.sec.gov/rules/final/2015/ic-31828.pdf; Money Market Fund Reform, Investment Company Act Release No. 29132 (Feb. 23, 2010), available at https://www.sec.gov/rules/final/2010/ic-29132.pdf.

[22] *See* 17 C.F.R. § 270.2a-7(a)(11) and (d)(2).

[23] *See* Removal of Certain References to Credit Ratings and Amendment to the Issuer Diversification Requirement in the Money Market Fund Rule, Investment Company Act Release No. 31828 (Sept. 16, 2015), *available at* https://www.sec.gov/rules/final/2015/ic-31828.pdf.

[24] *See* 17 C.F.R. § 270.2a-7(g)(3).

[25] Under Rule 2a-7 of the 1940 Act if, at any time, a MMF has invested less than 30% of its total assets in weekly liquid assets, the MMF may institute a liquidity fee or suspend the right of redemption temporarily if the MMF's board of trustees/directors determines that the fee or suspension of redemptions is in the best interests of the MMF. If, at the end of a business day, a MMF has invested less than 10% of its total assets in weekly liquid assets, the MMF must institute a liquidity fee, effective as of the beginning of the next business day, unless the MMF's board of directors/trustees determines that imposing the fee is not in the best interests of the MMF. Requirements related to liquidity fees and redemption gates do not apply to government MMFs. A government MMF, however, may choose to rely on the ability to impose liquidity fees and suspend redemptions consistent with the provisions of Rule 2a-7. 17 C.F.R. § 270.2a-7(c)(2) (2021). Under Rule 2a-7, a MMF's level of weekly liquid assets is required to be posted on its website on a daily basis. 17 C.F.R. § 270.2a-7(h)(10)(ii) (2021).

[26] From March 17 to March 24, average outflows were much stronger from institutional prime MMFs with weekly liquid assets at or below 35% as compared to MMFs with weekly liquid assets above 35%, despite the fact that these MMFs

liquid asset liquidity buffers to meet redemptions, as MMFs feared a decrease in weekly liquid assets would further exacerbate redemptions. This is evidenced by the fact that the institutional MMFs that engaged in Rule 17a-9 transactions in March 2020 did so while such MMFs had weekly liquid assets above 30%. Rather, such MMFs engaged in such transactions to promote and provide liquidity and avoid additional redemption pressure caused by the regulatory structure enacted in the 2014 reforms. Liquidity fees and redemption gates were tools that were provided as part of the 2014 reforms to help address a run on a MMF, however, in their current form, such tools contributed to and exacerbated redemptions at a time of a market-wide liquidity crisis and created liquidity pressures for certain prime MMFs. Therefore, to most appropriately and effectively reduce the likelihood of destabilizing redemptions and mitigate the impact of large redemptions, future reforms should remove the link between a MMF's liquidity and the imposition of liquidity fees and redemption gates. In crafting potential policy responses, regulators should take a narrowly tailored approach to be careful to avoid creating additional, new regulatory thresholds that may serve to incentivize or increase redemption activity or create unintended consequences that negatively impact MMFs and the larger short-term funding markets.

SIFMA AMG agrees with the assertion in the FSB Report that certain types of investors exhibit different redemption behavior. For example, retail investors may use MMFs for saving over a longer term, as an alternative to bank deposit accounts, or to take temporary defensive positions in declining equity markets; whereas institutional investors typically use MMFs as transactional accounts for cash management purposes. These different objectives impact investors' redemption behaviors and should be taken into consideration in narrowly tailoring rulemaking to apply only to those MMFs that experienced significant increased redemptions in March 2020 (e.g., institutional prime MMFs).[27]

b. Challenges in Selling Assets to Meet Significant Redemptions

The FSB report highlights that certain instruments held by MMFs, such as commercial paper and negotiable certificates of deposit, typically have little secondary trading market under even normal market conditions and dealers typically do not intermediate in secondary markets for these instruments.[28] To best address this, SIFMA AMG encourages a holistic approach to reforms that include improvements and enhancements to the underlying commercial paper and certificate of deposit markets, as highlighted in the complementary measures included in the FSB Report. SIFMA AMG highlights that policy measures that further limit a MMF's ability to hold such instruments, without reforms to the commercial paper and certificate of deposit markets, will not address underlying issues in such markets and their impact on the short-term funding markets, and therefore

held liquid assets above the regulatory minimum of 30% of weekly liquid assets. *See* ICI COVID-19 REPORT, *supra* note 8 at 33. The acceleration of outflows as prime MMFs' weekly liquid assets fell closer to 30% has also been acknowledged by the staff of the Division of Economic and Risk Analysis of the Commission. *See* DIVISION OF ECONOMIC AND RISK ANALYSIS, US CREDIT MARKETS: INTERCONNECTEDNESS AND THE EFFECTS OF THE COVID-19 ECONOMIC SHOCK 25 (2020), *available at* https://www.sec.gov/files/US-Credit-Markets_COVID-19_Report.pdf.

[27] Differences in redemption behavior between retail and institutional investors have been recognized previously by the Commission. *See* 2014 Adopting Release, *supra* note 9 at 241 ("retail investors historically have behaved differently from institutional investors in a crisis, being less likely to make large redemptions quickly in response to the first sign of market stress"). These differences in redemption behavior were also evident in March 2020.

[28] *See* FSB Report, *supra* note 2 at 24.

are not the most effective means to address underlying issues experienced in the short-term funding markets in March 2020.

III. Comments on the Policy Measures in the FSB Report

a. Guiding Principles to Reform: A Narrowly Tailored, Data Driven Approach

As an introductory matter to comments on the specific policy measures in the FSB Report, SIFMA AMG encourages any policy measures to be tailored as narrowly as possible to directly address the limited issues faced by non-government MMFs in March 2020. Because changes to MMFs may have far-reaching, unintended consequences that are detrimental to shareholders and the broader short-term funding markets, we urge that any recommendations in the FSB's final report be narrowly tailored to avoid unnecessary disruption. Tailoring reforms narrowly will benefit markets by easing the process of adjusting to changes, and providing a basis to evaluate the need for further actions based on the results achieved. Reforms should also be tailored in a manner to preserve the simplicity of the MMF product and be easy to understand for investors. Overly complicated policy measures risk investor confusion and reduce the utility of the MMF wrapper.

For these reasons, the combination of policy options in the FSB Report may not be needed or appropriate in order to deliver effective and sufficient enhancements to MMF resilience. Rather, a single policy measure may present the most effective means to enhance MMF resilience while avoiding imposing unintended consequences on shareholders or the short-term funding markets. Even considering as a starting point policy tools that authorities or MMFs have at their disposal but have not been used in practice, as the FSB report suggests, may impose significant costs and operational hurdles for MMFs in order to implement such measures that have previously not been used. For example, as further discussed below, while swing pricing is available for other types of open-end mutual funds, the implementation of this policy measure for MMFs presents significant operational impediments and costs. Further, mandating the use of certain tools, rather than permitting the use of such tools on a discretionary basis, can significantly alter the utility of MMFs and decrease demand for MMFs.

SIFMA AMG further urges that the pursuit of policy measures, and the mechanisms used by such policy measures, be limited to those measures and mechanisms that directly bear on the liquidity concerns experienced in March 2020 and the specific types of MMFs that experienced the largest outflows, while preserving the viability of such products for investors. Retail MMFs and non-public institutional prime MMFs did not experience the same level of outflows as publicly offered institutional prime MMFs. Policy measures should be tailored to reflect the difference in investor redemption behavior of the different types of MMFs.[29]

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[29] Public institutional prime MMFs experienced net redemptions of 30% (approximately $100 billion) during the two-week period March 11 to March 24. This is approximately $250 billion less than outflows experienced during the two-weak peak in September 2008, thereby presenting less of an overall impact to the overall short-term funding markets, although outflows were slightly larger compared to 2008 when viewed on a percentage basis. Non-public institutional prime MMFs experienced outflows representing approximately 6% of assets (approximately $17 billion) during the period March 9 to March 2021. *See* PWG REPORT 14 (2020), *available at* https://home.treasury.gov/system/files/136/PWG-MMF-report-final-Dec-2020.pdf. *See also* discussion in SIFMA AMG comments on PWG Report, Section IV "The Liquidity Crisis in March 2020" (highlighting different outflows among different types of MMFs and agreeing with the finding in the PWG Report that outflows experienced by non-public institutional prime MMFs show that such MMFs "do not demonstrate the same vulnerabilities as funds that are offered publicly to a broad range of unaffiliated institutional investors").

Moreover, SIFMA AMG encourages any final report issued by the FSB to recognize the flexibility for national regulators to implement policy recommendations appropriately in individual jurisdictions, taking into account jurisdiction-specific factors that may impact the effectiveness of any policy options. SIFMA AMG agrees with the FSB Report that, in this respect, it is important to consider an individual jurisdiction's existing regulations, size and structure of the MMF sector, use of MMFs by different investors and borrowers, and the functioning of the short-term funding markets, as these factors will impact the need for, the ability to implement, and the effectiveness of certain policy options in any individual jurisdiction. Our members note that as a result of the MMF reforms adopted by the Commission in 2014, certain market participants chose to exit the MMF business or significantly consolidate their MMF product line up. SIFMA AMG encourages regulators to consider how any changes will impact the willingness of market participants to offer MMFs, and how that may negatively impact the level of competition in, and the functioning of, the short-term funding markets.

As noted earlier, SIFMA AMG urges reform measures to exclude government MMFs. Government MMFs did not exhibit increased redemption pressures in March 2020 and such MMFs provide investors with a stable, attractive investment option and are widely viewed as among the safest and most liquid investment options for various types of investors. Government MMFs are currently subject to different regulations under Rule 2a-7 as compared to other types of MMFs, and the current level of regulation has proven effective in ensuring government MMFs are resilient and able to manage redemptions. As such, SIFMA AMG opposes additional regulatory requirements for government MMFs.[30]

The market events that occurred in March 2020 were caused by a liquidity crisis and policy measures should be tailored accordingly.[31] As such, in this section we first address liquidity-related policy measures (items b.-e. below), and then proceed to the other policy measures included in the FSB Report (items f. and g. below).

b. Removal of Ties Between Regulatory Thresholds and Imposition of Fees and Gates

SIFMA AMG strongly supports the delinking of liquidity and thresholds for imposing liquidity fees and redemption gates. SIFMA AMG views this policy measure as the most effective means to address the specific issues that contributed to stresses on certain types of MMFs and the short-term funding markets in March 2020 through reducing the likelihood of preemptive redemptions, and increasing the usability of liquidity buffers and reducing the need to sell less liquid assets. SIFMA AMG views this as the most effective means to enhance the resiliency of MMFs and therefore views this policy measure as an essential element of any MMF reform.

As noted earlier in Section II.a., linking the ability to impose liquidity fees and redemption gates to a specified level of weekly liquid assets that is publicly available created an unintended consequence of incentivizing institutional investors to redeem as a MMF's liquidity approached the threshold at which a liquidity fee or redemption gate could be imposed which would restrict their ability to access cash. The 30% weekly liquid asset threshold, in turn, resulted in MMFs selling fewer liquid assets to meet redemptions in March 2020, as MMFs feared a decrease in weekly liquid assets

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[30] *See supra* Section II for a further discussion on the differing risk profiles and experiences of government MMFs.

[31] *See* discussion in SIFMA AMG comments on PWG Report, Section IV "The Liquidity Crisis in March 2020."

would accelerate redemption behavior. This exacerbated liquidity pressures. Requirements to maintain a minimum level of weekly liquid assets do not serve their intended purpose if MMFs are not willing or able to use liquidity buffers in times of stress. Accordingly, delinking liquidity and thresholds for imposing a liquidity fee or redemption gate is a vital part of effectively addressing an unintended consequence that resulted from the implementation of the 2014 reforms to Rule 2a-7 that contributed to stress in the short-term funding markets in March 2020. Improving the usability of liquidity buffers, as this policy measure will do, will better equip MMFs to manage through times of stress and will therefore help improve the resilience and functioning of the short-term funding markets. Moreover, by removing one element that increased redemption behavior in March 2020, this policy measure helps reduce the likelihood that official sector interventions would be needed to halt redemptions. Further, this policy measure is unlikely to cause investors to shift to less regulated investment products and therefore avoids such a consequence that would be likely to negatively impact the broader short-term funding markets.

This policy measure as presented in the FSB Report still would maintain liquidity fees and redemption gates as a tool for MMFs to use to help slow redemptions, without the potential use of such tools being tied to a specified level of liquidity. As such, the utility and protections provided by liquidity fees and redemption gates would remain available to MMFs; however, the aspects of such liquidity fees and redemption gates that contributed to liquidity pressures on some MMFs would be removed.

While institutional prime MMFs came under the most pressure during the market stresses in March 2020 as compared to other types of MMFs, SIFMA AMG supports applying the delinking policy measure to all types of MMFs that are currently subject to liquidity fees and redemption gates. The dynamics that motivate redemptions in the face of a bright line liquidity threshold that is tied to a liquidity fee or redemption gate apply regardless of the type of MMF. Further, creating a consistent framework for all types of MMFs subject to liquidity fees and redemption gates as to when such liquidity fees and redemption gates may be imposed may also alleviate the potential for investor confusion.

The FSB Report notes that the policy measure to delink liquidity with thresholds for liquidity fees and redemption gates does not address other sources of MMF vulnerabilities and would leave MMFs susceptible to large redemptions in times of stress. SIFMA AMG disagrees with this assertion, as MMFs have successfully managed redemptions through other times of stress prior to the imposition of fees and gates, such as during the European sovereign debt crisis. During times of stress, advisers and boards intensify their oversight of MMFs and adjust portfolios as needed. Current U.S. regulatory requirements limit a MMF's exposure to credit risk by requiring MMFs to hold securities that meet "minimal credit risk" requirements, impose diversification requirements that limit risk exposure to any one issuer, impose liquidity requirements to enable MMFs to withstand increased redemption requests, require "know your customer" policies and procedures pursuant to which MMFs consider investor characteristics and their likely redemption behavior, and mandate stress testing to help address the potential risks to a MMF from possible market events. In addition, increased shareholder transparency through daily website reporting, as currently required under Rule 2a-7, incentivizes conservative liquidity management of MMFs.[32] This highlights that

[32] SIFMA AMG notes that given the requirement to post levels of weekly liquid assets on a MMF's website on a daily basis, coupled with the fact that liquidity is of primary importance to MMF investors (particularly institutional investors), it is generally not expected that in normal market conditions MMFs would be managed significantly closer to 30%

MMFs have the tools and capabilities under current regulations to safeguard against redemption pressures and successfully manage through stressed conditions, without the need for additional large structural reforms to MMFs to do so.

Further, we would like to highlight the earlier discussion in Section II noting the inflows to government MMFs were largely from products other than prime MMFs in the face of an unprecedented liquidity crisis. This shows that susceptibility to large redemptions was faced by other products in the short-term funding markets as part of a market-wide liquidity crisis and not specific to MMFs. Regulatory thresholds associated with fees and gates, however, are specific to MMFs and data proves that such regulatory thresholds significantly contributed to redemption pressures faced by MMFs.[33] Removing such regulatory thresholds provides regulators with a clear and effective route to address a specific and primary cause of redemption pressure on MMFs in March 2020.

The FSB Report notes that European variable net asset value ("VNAV") MMFs not subject to fees and gates experienced high outflows in March 2020. In this regard, while recognizing the importance of drawing on lessons learned in other jurisdictions, SIFMA AMG urges recognition of differences in the U.S. MMF market as compared to the European MMF market in considering the adequacy of policy responses specific to U.S. MMFs. In particular, European VNAV MMFs have weekly liquidity ratio requirements of 15% and daily liquidity ratio requirements of 7.5%, as compared to U.S. institutional prime MMFs that have minimum weekly liquid asset requirements of 30% and daily liquid asset requirements of 10%.[34] Simply analogizing redemption behavior of European VNAV MMFs to U.S. MMFs during March 2020, without additional consideration to such MMFs' differing jurisdiction-specific liquidity requirements and profiles, is an inappropriate means on which to base future regulatory reforms for a particular jurisdiction.

The FSB Report notes that this policy measure could increase uncertainty for investors regarding the use of fees and gates. Under the current U.S. regulatory regime, however, there remains uncertainty regarding whether a MMF would impose a fee or gate if its weekly liquid assets fall below 30%, as the ability to impose a fee or gate is left to the discretion of the board of trustees/directors. Removing this regulatory threshold would not necessarily increase investor uncertainty, as there was never certainty as to when a fee or gate would be imposed, but would rather simply remove an aspect of fees and gates that resulted in increased redemption behavior. SIFMA AMG highlights that investors will continue to have access to daily reporting of a MMF's weekly liquid asset levels on the MMF's website, which enables investors to make informed investment decisions based on a MMF's liquidity levels and the investor's own risk tolerances and investment needs, versus based on fear of a MMF crossing a regulatory threshold that may or may not result in the imposition of a liquidity fee or redemption gate.

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weekly liquid assets in the absence of a tie between 30% weekly liquid assets and liquidity fees and redemption gates. In fact, from 2010 to 2013 (prior to the adoption of liquidity fees and redemption gates), weekly liquid assets for institutional prime MMFs averaged approximately 42% of such MMFs' assets, which is significantly higher than the 30% minimum weekly liquid assets threshold (as a percentage of their portfolios). This shows that even without the possibility of implementing a liquidity fee or redemption gate, MMFs are operated conservatively in order to be equipped to manage redemptions through times of stress. *See* ICI COVID-19 REPORT*, supra* note 8 at note 59.

[33] *See supra* note 26 and related text.

[34] *See* 17 C.F.R. § 270.2a-7(d)(4); Regulation (EU) 2017/1131 of the European Parliament and of the Council at Chapter III, Articles 24-25 (14 June 2017), *available at* https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32017R1131&from=en.

For the reasons discussed above, SIFMA AMG views the delinking of liquidity and thresholds for liquidity fees and redemption gates as the policy measure presented in the FSB Report that has the strongest direct correlation to the cause of stresses experienced by certain types of MMFs in March 2020 and therefore the policy measure that most meaningfully addresses, in a practical manner, the issues that contributed to stresses on certain types of MMFs and the short-term funding markets. SIFMA AMG believes delinking liquidity and thresholds for imposing liquidity fees and redemption gates is the most effective way to enhance the resiliency of MMFs and therefore an essential element of any MMF reform, and that additional reforms (if any) should be paired with this policy measure for the most effective outcome.

i. <u>Variants and Extensions</u>

The FSB Report includes three variants or extensions to this policy option: (1) authorities approving activation of fees and gates, (2) MMF investor concentration limits, and (3) countercyclical liquidity buffers. SIFMA AMG believes the removal of the tie between regulatory thresholds and the imposition of fees and gates is appropriately characterized as the "representative option" and is the most effective means to reduce the likelihood of stabilizing redemptions and mitigate the impact of large redemptions. To the extent regulators consider any such variants or extensions, SIFMA AMG urges such variants or extensions to be part of a larger rulemaking package that includes the delinking of liquidity fees and redemption gates.

1. Authorities Approving Activation of Fees and Gates

Requiring authorities to approve the activation of fees and gates without delinking liquidity fees and gates is unlikely to address the liquidity issues that occurred in March 2020. Steps that impose additional time between the determination of imposing a liquidity fee or redemption gate and the actual implementation of such fee or gate reduce the utility of the liquidity fee or redemption gate, especially in a time of market stress, and are therefore unlikely to increase the resiliency of MMFs and the short-term funding markets. Investors' adversity to liquidity fees and redemption gates that drove increased redemption behavior as MMFs approached 30% of weekly liquid assets is generally rooted in a concern of liquidity and an inability to readily access funds. Requiring authorities to approve the activation of fees or gates does not remedy investors' concerns and is therefore unlikely to address the contributors to stresses in the market such as those experienced in March 2020.

Interposing an additional entity in the decision-making process could also increase investor uncertainty with respect to the activation of fees and gates. SIFMA AMG members feel that MMFs, their sponsors, and the boards of trustees/directors, are best positioned to make decisions regarding a particular MMF's implementation of a liquidity fee or redemption gate.

To the extent liquidity levels remain a concern of regulators in considering the representative option (and to the extent such variant is considered as part of a reform package that also includes delinking liquidity fees and redemption gates), SIFMA AMG is supportive of exploration of the FSB's proposal to require a transition period during which a MMF that breached a certain liquidity level would be required to increase its liquid assets to reach a temporarily higher requirement.

2. MMF Investor Concentration Limits

While SIFMA AMG does not oppose MMF investor concentration limits in principle, imposing investor concentration limits would not address the increased redemptions faced by certain MMFs due to current regulatory requirements that tie fees and fates to specified levels of liquidity. To the extent concentration limits are included in any final report, such limits should be part of a larger reform package that includes delinking liquidity fees and redemption gates.

SIFMA AMG notes that U.S. MMFs are required to adopt "know your customer" policies and procedures to comply with the requirement that MMFs hold securities that are sufficiently liquid to meet reasonably foreseeable shareholder redemptions in light of the MMF's obligations under Section 22(e) of the 1940 Act and any commitments the MMF has made to shareholders. Under "know your customer" policies and procedures, MMFs consider factors that may impact a MMF's liquidity needs, such as characteristics of investors and their likely redemptions. In this regard, MMFs already have a process in place to assess risk characteristics of shareholders, such as investor concentration. In adopting this requirement, the Commission did not identify specific characteristics to be addressed in such policies and procedures as the Commission believed MMFs are in the best position to do so. The Commission also did not set limits as to the scope of such policies and procedures because different MMFs may have different needs in this regard.[35] SIFMA AMG believes the same holds true related to investor concentrator limits and that MMFs are best positioned to analyze the need for any investor concentration limits, which may vary by MMF depending on the composition of the MMF's shareholder base. SIFMA AMG cautions against a "one size fits all" approach regarding any investor concentration limits, as the needs of a MMF may vary based on the individual's MMF's shareholder base and holdings.

Further, with respect to investor concentration limits, SIFMA AMG notes potential challenges in calibrating concentration limits and in implementation due to shares being held in omnibus accounts. Specifically, share ownership is less transparent when shares are held in omnibus accounts and many MMF shares are held in omnibus accounts.

3. Countercyclical Liquidity Buffers

While SIFMA AMG does not oppose countercyclical weekly liquid asset requirements in principle, many of our members view this policy measure overall as a less effective means to enhance MMF resiliency as compared to delinking liquidity and liquidity fees and redemption gates and our members express concerns about significant implementation challenges with respect to countercyclical liquidity buffers. SIFMA AMG therefore supports the delinking of liquidity and liquidity fees and redemption gates over countercyclical weekly liquid asset requirements. Should regulators delink liquidity and the imposition of liquidity fees and redemption gates, many of the benefits of countercyclical liquidity asset requirements will be realized in a more effective manner than through a countercyclical policy measure. Both policy measures would reduce the salience of the liquidity threshold to diminish the incentive for increased outflows and improve the usability of weekly liquid asset buffers, however, countercyclical weekly liquidity asset requirements could be less effective in doing so by still maintaining the potential for a bright line threshold that could incentivize redemptions and by introducing additional unnecessary complexities as compared to the delinking of liquidity and liquidity fees and redemption gates. Any externalized trigger for liquidity fees and redemption gates, even with countercyclical adjustments, has the potential to incentivize redemption behavior.

The delinking of liquidity with thresholds for liquidity fees and redemption gates removes threshold effects that motivate investors to redeem. Maintaining a threshold at which liquidity fees

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[35] Money Market Fund Reform, Investment Company Act Release No. 29132 at 53 (Feb. 23, 2010), available at https://www.sec.gov/rules/final/2010/ic-29132.pdf.

or redemption gates could be imposed, but shifting that threshold through countercyclical weekly liquid asset requirements, has the potential to exchange one red flag for another and mitigate the usefulness of countercyclical weekly liquid asset requirements. The events of March 2020 show that investors, particularly institutional investors, are incredibly information sensitive and news driven. As weekly liquid asset levels dropped closer to 30% (the threshold at which a board could impose a liquidity fee or redemption gate), institutional investors quickly reacted to this information and increased their redemption activity. Many of our members have expressed concern that it is likely that institutional investors will react to other types of information that may trigger countercyclical requirements and such triggers may therefore increase redemption behavior in a similar manner as was seen in March 2020 when weekly liquid asset levels reached the threshold at which a board could impose a liquidity fee or redemption gate.

The FSB Report highlights that this variant could apply to all types of MMFs, including those not currently subject to liquidity fees and redemption gates. For the reasons discussed above in Section II, SIFMA AMG opposes such a requirement for government MMFs. In addition to such a requirement being unnecessary for government MMFs, imposing such a requirement for government MMFs has the potential to overly complicate the regulatory framework applicable to such MMFs without additional benefit.

To the extent regulators consider countercyclical weekly liquid asset requirements, SIFMA AMG urges regulators to further consider how to construct a countercyclical requirement that would apply on an automatic basis, versus requiring action by applicable authorities. Requiring action by authorities would slow the implementation of any countercyclical weekly liquid asset requirement, presumably in a time of stress, thereby reducing the utility of the countercyclical weekly asset requirement. Further, many of our members have expressed concern that action by authorities could send a heightened negative signal to investors and cause increased redemptions.

SIFMA AMG also urges regulators to consider constructing this policy measure to apply on a market-wide basis, versus per MMF. If applied on a market-wide basis, the countercyclical weekly liquid asset requirement could be employed on a less disruptive basis than singling out one MMF in particular, which could contribute to stress on that particular fund. We note, however, the difficulty of obtaining information that may be necessary to implement or oversee the trigger of a countercyclical weekly liquid asset requirement and again highlight the additional benefits of delinking liquidity with liquidity fees and gates insofar as delinking does not present the additional complexities associated with implementing or calibrating countercyclical weekly liquid requirements and would therefore more effectively enhance the resiliency of MMFs. Should regulators consider countercyclical weekly liquid asset requirements, SIFMA AMG urges regulators to consider such policy measure only as part of a larger reform package that also includes delinking liquidity and liquidity fees and redemption gates.

c. Limits on Eligible Assets

While in principle SIFMA AMG does not generally oppose certain limits on eligible assets, our members generally believe such changes will be less effective than the delinking of liquidity and fees and gates in addressing the specific issues presented in March 2020 and enhancing MMF resilience. To the extent regulators consider limits on eligible assets, SIFMA AMG believes any such changes should be focused on the types of MMFs that experienced higher redemptions in March 2020 as part of a reform package that includes the delinking of liquidity with liquidity fees and redemption gates.

As noted above, increased redemption behavior in March 2020 was primarily driven by fear that a liquidity fee or redemption gate would be imposed as a MMF's weekly liquid assets dropped to 30% and investors would be unable to access liquidity. Redemption behavior was not driven by fears that 30% of a MMF's portfolio in weekly liquid assets was too low a level of liquidity for a MMF. Imposing higher minimum liquidity requirements is addressing an issue that did not necessarily cause or contribute to stresses experienced in March 2020 and many of our members generally view any increase as unlikely to materially impact such stresses.

Imposing higher liquidity minimums could have negative unintended consequences for MMFs subject to the higher minimum. For example, imposing a higher minimum level of weekly liquid assets could decrease MMF yields and reduce the spread between prime and government MMFs. These consequences could then, in turn, shrink the size of the MMFs subject to such higher weekly liquid asset minimum by decreasing investor demand for such products. This could then increase the cost of funding to issuers.[36] SIFMA AMG urges regulators to consider these consequences in considering whether to additional limits on eligible assets for MMFs.

SIFMA AMG further highlights that MMFs currently operate conservatively and manage their portfolios significantly above the 30% weekly liquid asset minimum in normal market conditions. In fact, since 2010, prime MMFs' weekly liquid assets (as a percentage of their portfolios) have exceeded the 30% weekly liquid asset minimum on average by 12 to 15 percentage points.[37] This is true even before requirements related to liquidity fees and redemption gates were imposed and, therefore, even if liquidity levels are delinked from requirements related to liquidity fees and redemption gates, it is generally not expected that MMFs would manage significantly closer to the minimum level of weekly liquid assets. For example, from 2010 to 2013 (prior to the adoption of liquidity fees and redemption gates), weekly liquid assets for institutional prime MMFs and retail prime MMFs averaged approximately 42% and 39% of such funds' assets, respectively, which is significantly higher than the 30% minimum weekly liquid assets threshold (as a percentage of their portfolios).[38] To the extent regulators consider imposing a higher liquidity minimum, SIFMA AMG encourages regulators to consider that MMFs typically manage their MMFs' liquidity at a higher level than any required minimum and therefore imposing a higher minimum as a practical matter would result in a de facto even higher minimum than actually required as a regulatory matter. Accordingly, should regulators propose higher liquidity minimums, our members generally urge regulators to take an incremental approach in determining any higher liquidity minimum given managers are likely to manage their MMFs' liquidity higher than any required minimum and any significant increase could impact the nature and usefulness of the product and reduce investor interest in such MMFs.

To the extent regulators explore requiring MMFs to invest a higher portion of their assets in shorter dated and/or more liquid instruments, SIFMA AMG believes it is appropriate to narrowly tailor such requirements to those types of MMFs that experienced the heaviest outflows in March 2020 and to exclude other types of MMFs from such requirements. As discussed above, public institutional prime MMFs experienced the largest redemptions as compared to other MMFs. This

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[36] *See* discussion in SIFMA AMG comments on PWG Report, Section II "The Important Role of Money Market Funds in the Short-Term Funding Markets" for a more comprehensive discussion of the potential consequences of reducing the size of the prime MMF industry.

[37] *See* ICI COVID-19 REPORT, *supra* note 8 at 23.

[38] *See id.* at n. 59.

pattern of investor redemption behavior is consistent with patterns during prior periods of market stress. SIFMA AMG believes narrowly tailoring reform measures to address only those types of MMFs that experienced heavier outflows in March 2020 is the most appropriate and effective manner to approach MMF reform.

i. Variants and Extensions

The FSB Report includes four variants or extensions to this policy option: (1) limit MMFs to government MMFs; (2) redemption in-kind; (3) non-daily dealing; and (4) liquidity-based redemption deferrals. SIFMA AMG believes the limitation on eligible assets is appropriately characterized as the "representative option" and is a more effective and appropriate means to mitigate the impact of large redemptions than the various extensions and variants, while also maintaining investor choice and important features of MMFs. As noted above SIFMA AMG believes any limitation on eligible assets will be most effective as part of a rulemaking package that includes delinking liquidity fees and redemption gates. SIFMA AMG generally opposes the related variants and extensions because the related variants and extensions significantly curtail investors' access to liquidity and the use of such products as a cash management vehicle, thereby causing investors to view MMFs as less liquid and resulting in a decrease in the size of the MMF sector.

1. Limit MMFs to Government MMFs

Limiting MMFs to government MMFs would have a significant negative impact on investors and the short-term funding markets in numerous ways. First, reforms that eliminate prime and tax-exempt MMFs will limit the amount and types of products available to meet investors' investment and liquidity needs. This will curtail investor choice and will eliminate a highly regulated, transparent vehicle currently available to investors to manage their cash management needs and used as an alternative to less regulated and less transparent liquidity vehicles.

Second, investors may seek to deposit a significant portion of redemptions from prime and tax-exempt MMFs at banks. There would be capital implications for these additional deposits, which could increase systemic risk. It is also uncertain whether all banks could provide the requisite financing to issuers on the scale currently available through MMFs, and the cost of financing to issuers has the potential to increase. MMFs' use as a highly regulated alternative to bank accounts is increasingly important to the extent banks may be unable or unwilling to accept additional deposits due to capital requirements, as MMFs can be used to fill an important gap in the market and provide a safe, highly regulated alternative.[39] SIFMA AMG encourages regulators to explore whether banks in a given jurisdiction could handle inflows of money that would otherwise have been invested in prime and tax-exempt MMFs.

Third, elimination of prime or tax-exempt MMFs may drive money into other types of cash pools that are less regulated, to markets that are outside the specific jurisdiction's regulatory oversight, or to products that otherwise introduce increased investment risk. This would increase risks not only to shareholders, but also to the financial markets.

Fourth, elimination of prime or tax-exempt MMFs has the potential to significantly impair available financing to businesses, corporations, financial institutions, hospitals, universities, and state and local governments. MMFs help support the economy through their significant investments in various high quality, short-term debt securities, including commercial paper, certificates of deposit,

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[39] *See supra* note 16.

repurchase agreements, variable rate demand notes, state and municipal securities, and Eurodollar deposits. Prime MMFs in particular provide significant financing to businesses and financial institutions through the purchase of commercial paper, certificate of deposits, and Eurodollar deposits. The commercial paper market is used for the financing of payrolls and accounts payable and inventories, and represents funding that is essential to maintain employment. If the commercial paper market constricts greatly because of the elimination of prime MMFs, the cost of financing for businesses and financial institutions has the potential to increase and the access to the short-term markets will likely be compromised. Further, MMFs (tax-exempt MMFs in particular) provide significant financing to state and local governments to help meet short-term financing needs through investments in variable rate demand notes issued by state and local governments. MMFs are also a source of financing for non-profit organizations, such as universities and hospitals.

Without prime and tax-exempt MMFs, the cost of financing for all of these institutions and their related projects would likely increase and be less efficient, thereby disrupting the flow of short-term capital to businesses and negatively impacting governments, bank and non-bank issuers, and municipalities. Ultimately, increased borrowing costs are likely to be passed through to taxpayers and consumers, with potential negative consequences on local and broader global economies. Accordingly, eliminating the prime and tax-exempt MMF sectors is likely to negatively impact operations of businesses and financial institutions in a meaningful way and will not improve the resilience and functioning of short-term funding markets.[40] In fact, such policy measures will significantly harm the resilience and functioning of short-term funding markets and undermine the overarching goals of increased resilience of MMFs and the short-term funding markets.

Fifth, if prime and tax-exempt MMFs are eliminated, then other potentially less regulated and less transparent vehicles may represent a larger portion of the front-end of the yield curve. MMFs are subject to extensive disclosure requirements, and the transparency offered by MMFs allows regulators to effectively monitor developments in MMFs generally, as well as with respect to specific individual MMFs.[41] In handling any future unforeseen market-wide liquidity or other crisis, regulators would potentially have less transparency into the front-end of the yield curve to the extent there is a smaller prime and tax-exempt MMF sector (highly regulated vehicles) in the front-end of the yield curve. This could prove increasingly challenging to regulators and impede regulators' efforts, particularly during a time of market stress.

As discussed above, SIFMA AMG supports a narrowly tailored, data driven approach to policy reform. This policy measure oversteps insofar as it fails to consider a reform that would directly address the increased redemptions faced by certain non-government MMFs in March 2020

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[40] For examples of letters regarding the importance of MMFs to issuers and the potential risks if MMFs shrink, *see Oversight of the Mutual Fund Industry: Ensuring Market Stability and Investor Confidence: Hearing Before the Subcomm. on Capital Mkts. and Gov't Sponsored Enter. of the Comm. on Financial Serv.*, 112th Cong. 226 (2011) (Letter from James A. Kaitz, President and CEO, Association for Financial Professionals), *available at* http://financialservices.house.gov/UploadedFiles/112-42.pdf. *See also*, Joint Letter of the American Public Power Association, Council of Development Finance Agencies, Council of Infrastructure Financing Authorities, Government Finance Officers Association, International City/County Management Association, International Municipal Lawyers Association, National Association of Counties, National Association of Local Housing Financing Agencies, National Association of State Auditors, Comptrollers and Treasurers, National Association of State Treasurers, National League of Cities, U.S. Conference of Mayors, *available at* www.sec.gov/comments/4-619/4619-130.pdf.

[41] *See supra* note 18.

(delinking liquidity fees and redemption gates), and instead would entirely eliminate an entire sector of the MMF and short-term funding markets.

2. Redemptions In-Kind

U.S. MMFs already have at their disposal the ability to reserve the right to redeem shares in-kind (i.e., meet redemptions by transferring assets held by a MMF to redeeming investors).[42] The use of in-kind redemptions in the United States historically has been infrequent due to various operational and other considerations further discussed below, and many funds that reserve the right to redeem in-kind do so as a tool to manage liquidity risk under emergency circumstances or to manage the redemption activity of a fund's large institutional investors. Rather than mandating redemptions in-kind in certain stress periods, SIFMA AMG believes the current U.S. regulatory framework that provides MMFs with the ability to reserve the right to redeem shares in-kind is the more appropriate manner to address redemptions in-kind as MMFs are best positioned to determine when a redemption in-kind may be necessary and appropriate. Allowing discretion on the part of the adviser to consider all facts and circumstances and available tools in managing a MMF through a stressed period serves to best protect the interests of shareholders.

Further, the circumstances facing any particular MMF may differ from other MMFs, and mandating the use of redemptions in-kind on a market-wide basis may prove difficult, ineffective, and inappropriate. To the extent regulators sought to define a "stress period," this could have the unintended consequence of creating another regulatory threshold that increases redemption activity. SIFMA AMG also notes the existence of other liquidity management tools already at MMFs' disposal to mitigate the impact of large redemptions, such as liquidity fees and redemption gates, that can be used in certain conditions.

The FSB Report highlights that this variant would transfer liquidity risk to redeeming institutional investors and reduce liquidity transformation and make MMFs more resilient. Simply transferring the risk from the MMF to the investor does not eliminate the risk, but, rather, transfers it to another portion of the market that may be less equipped to manage such risk. This, in turn, could create negative effects outside of the MMF sector when investors seek to dispose of assets they receive in-kind from a MMF, which could contribute to overall market stress and dislocations.[43]

In addition, SIFMA AMG notes that redeeming shares in-kind can present significant operational challenges and costs that should be studied before consideration of mandating MMFs to redeem in-kind. As previously recognized by the President's Working Group, portfolio holdings of MMFs sometimes are not freely transferable or are only transferable in large blocks of shares, so delivery of an exact pro rata portion of each portfolio holding to a redeeming shareholder presents

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[42] Funds have the ability to redeem in kind, subject to the limitations under Rule 18f-1 under the 1940 Act for funds that have made an election under Rule 18f-1. An 18f-1 election commits a fund to pay in cash all requests for redemption by any shareholder of record, limited in amount with respect to each shareholder during any 90-day period to the lesser of $250,000 or 1% of the fund's net asset value at the beginning of the period. 17 CFR § 270.18f-1 (2021).

[43] The President's Working Group has also previously recognized that "[s]hareholders with immediate liquidity needs who receive securities from MMFs would have to sell those assets, and the consequences for short-term markets of such sales would be similar to the effects if the money market fund itself had sold the securities." SIFMA AMG agrees with this statement and believes it continues to apply today. Report of the President's Working Group on Financial Markets: Money Market Fund Reform Options at 26 (Oct. 2010), *available at* https://www.treasury.gov/press-center/press-releases/Documents/10.21%20PWG%20Report%20Final.pdf.

complex challenges and may be impracticable.[44] Moreover, this policy measure presents additional challenges based on type of shareholder as certain MMF holdings may be unable to be transferred to retail investors and retail investors may not be operationally equipped to receive in-kind redemptions. As management and personnel capacity of MMFs during "stress periods" are focused on managing redemption or liquidity pressures, mandating MMFs to redeem in-kind may impose additional undue burden on fund management during a time of stress when other effective and less burdensome liquidity management tools are available to MMFs. For these reasons, SIFMA AMG believes the current U.S. regulatory framework that provides MMFs with the ability to reserve the right to redeem shares in-kind, as opposed to mandating redemptions in-kind in certain stress periods, is the more appropriate manner to address redemptions in-kind as MMFs are best positioned to determine when a redemption in-kind may be necessary and appropriate.

3. Non-Daily Dealing and Liquidity-Based Redemption Deferrals

Under the FSB's non-daily dealing variant, MMFs would no longer offer daily redemptions and, instead, the frequency of redemptions would be aligned with the liquidity of the assets (such as weekly or biweekly redemptions). The liquidity-based redemption deferral variant would allow only a fraction of each redemption request to be met on the same day depending on the share of very liquid assets held by the MMF, effectively dividing investors' claims into two tiers – a portion redeemable daily and a less liquid portion only available with a delay.

While MMFs often seek to satisfy redemption requests and pay redemption proceeds on a same or next day basis in order to facilitate MMFs' use as a valuable cash management solution for investors, MMFs are not *required* to satisfy redemption requests on a same or next day basis under current U.S. laws and regulations. Rather, under the current U.S. regulatory framework, MMFs are required to satisfy redemption requests within seven days, with certain exceptions.[45] Accordingly, should market or other conditions warrant, U.S. MMFs currently have at their disposal the ability to delay payment of redemption proceeds for up to seven days. SIFMA AMG believes the current U.S. regulatory framework that provides MMFs with the flexibility to delay redemptions for up to seven days based on their individual needs and circumstances provides MMFs with a more appropriate liquidity management tool while maintaining key features of the MMF wrapper rather than mandating non-daily dealing or liquidity-based redemption deferrals.

As noted above, in previously adopting amendments to Rule 2a-7, the Commission recognized the importance of key features of MMFs such as same day settlement and structured

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[44] *See id.*

[45] No registered investment company shall suspend the right of redemption, or postpone the date of payment or satisfaction upon redemption of any redeemable security in accordance with its terms for more than seven days after the tender of such security to the company or its agent designated for that purpose for redemption, except—

> (1) for any period (A) during which the New York Stock Exchange is closed other than customary week-end and holiday closings or (B) during which trading on the New York Stock Exchange is restricted;
>
> (2) for any period during which an emergency exists as a result of which (A) disposal by the company of securities owned by it is not reasonably practicable or (B) it is not reasonably practicable for such company fairly to determine the value of its net assets; or
>
> (3) for such other periods as the Commission may by order permit for the protection of security holders of the company.

Section 22(e) of the 1940 Act.

reforms to provide MMFs with tools to manage redemptions while also purposefully preserving "the ability of [MMFs] to function as an effective and efficient cash management tool for investors."[46] MMFs currently have the ability to delay redemption proceeds up to seven days to help manage redemptions, and regulations that mandate non-daily dealing or liquidity-based redemption deferrals will simply serve to eliminate the ability of MMFs to function as an effective and efficient cash management tool for investors, a key feature of MMFs that the Commission previously sought to maintain, without addressing a primary cause of redemptions from certain MMFs in March 2020 (the linking of liquidity levels with liquidity fees and redemption gates). Moreover, a key principle embodied in the 1940 Act is that of full, unfettered redeemability of fund shares. Policy proposals that seek to inhibit an investor's ability to fully or partially redeem their shares, or postpone payment upon redemption, is at odds with basic principles of the 1940 Act, particularly when such ability may be inhibited under normal market conditions.[47]

The FSB Report highlights that these variants impose liquidity restrictions on investors even in normal market conditions. As MMFs have generally not exhibited liquidity issues during normal market conditions, these variants unnecessarily and unfairly curtail investors' liquidity. These variants would significantly alter the profile and functionality of MMFs, and impede their utility to investors. Many MMF investors (primarily, but not exclusively, institutional investors) move money in and out of their accounts for a variety of time-sensitive business and personal transactions. Same day settlement is considered a critical feature of certain MMFs for such investors. Eliminating this feature will significantly impair the use of MMFs as important cash management vehicles for a variety of investors and our members expect that shareholders will object to the delay or deferment of all or a portion of their accounts. Further, these proposals introduce additional complexity to the MMF regulatory framework in a manner that is likely to increase investor confusion as investors may be unsure how long of a settlement period may be imposed, or what portion of their investment may be subject to deferral, which would impede the use of MMFs to fund day-to-day operations. For these reasons, these variants may cause investors to turn to other less regulated and less transparent liquidity vehicles to manage their cash management needs, or cause investors to seek to deposit a significant portion of redemptions from MMFs at banks. Please see the discussion in Section III.c.i.1. for a discussion of the implications and risks associated with such flows.

Further, the liquidity-based redemption deferral variant in particular would impose significant costs to implement that may make MMFs unviable for sponsors to operate. As discussed above, a decrease in the size of the MMF sector could have significant negative implications for the broader short-term funding markets. SIFMA AMG also notes the existence of other liquidity management tools already at MMFs disposal to mitigate the impact of large redemptions, such as liquidity fees and redemption gates, that can be used in certain conditions.

d. Additional Liquidity Requirements and Escalation Procedures

This option would mandate that MMFs hold minimum amounts of assets that can be readily converted to cash over a two-week period or less. As part of a larger reform package that includes delinking liquidity fees and redemption gates, SIFMA AMG is supportive of further exploration of whether a market exists for an additional biweekly liquid asset category (e.g., whether banks will underwrite assets with such maturities). SIFMA AMG highlights, however, the potential for such

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[46] *See supra* note 13.

[47] *See* Section 22(e) of the 1940 Act.

additional category to overly complicate the framework of Rule 2a-7 without additional benefit, and notes the earlier discussion encouraging policy measures that are simple to understand and implement.

This option would also impose escalation procedures in the event of a regulatory threshold breach that would require MMFs to use price-based tools, such as liquidity fees or swing pricing first; then quantity-based tools, such as notice or settlement periods; before then being able to impose a redemption gate. As discussed above, SIFMA AMG believes removal of regulatory thresholds is the most effective means to enhance the resiliency of MMFs. Continuing to tie various tools to regulatory thresholds (even with escalation procedures) creates the potential to increase redemption activity, particularly in times of stress. Further, certain types of tools may work differently, or more effectively, for individual MMFs based on their shareholder base, holdings, and other fund-specific considerations, or during different types of market conditions. Accordingly, structuring escalation procedures to apply on a market-wide basis regardless of fund-specific characteristics or the type of market condition or stress may prove difficult, ineffective, and inappropriate. Rather, SIFMA AMG encourages exploration of whether providing guidance on escalation procedures, such as factors to consider on a facts and circumstance basis with respect to the implementation of certain tools, as opposed to mandating certain escalation procedures, may be a more effective approach should regulators consider the use of escalation procedures.

e. Swing Pricing[48]

SIFMA AMG does not support swing pricing for MMFs as we do not believe it will enhance MMF resilience. Swing pricing is not necessary for MMFs and would not result in the same benefits, or address the same issues, that swing pricing addresses in other open-end funds due to differences in how MMFs handle redemptions as compared to other open-end funds.

Swing pricing adjusts a fund's net asset value downward when net redemptions exceed a threshold to pass to redeeming shareholders certain transaction costs associated with their trading activity. Many of the reasons that swing pricing may benefit other mutual funds in managing liquidity risks are less applicable to MMFs. While a bond fund may be likely to have to sell bonds to meet redemption requests, MMFs frequently handle large redemptions and typically know when to expect to such redemptions.[49] As such, MMFs typically let securities mature to meet redemptions and therefore do not incur transaction costs as bond funds do in meeting redemptions (or incur transaction costs at a much lower rate). The level of transaction costs associated with MMF trading is much lower than transaction costs of other mutual fund trading due to the types of securities in which MMFs invest such that any swing factor is likely to be too small to achieve the stated goals of this policy measure and impact any "first mover advantage."[50] Based on this, the reasons and benefits for implementing swing pricing simply do not apply to MMFs and swing pricing is therefore unlikely to address any liquidity issue that arose in March 2020. To our knowledge, swing pricing has

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[48] Comments and positions herein regarding swing pricing are focused on MMFs and are not being made in the context of other open-end mutual funds.

[49] As discussed above, MMFs maintain "know your customer" procedures under Rule 38a-1 of the 1940 Act to consider investor characteristics and their likely redemption behavior. *See* Money Market Fund Reform, Investment Company Act Release 29132 (Feb. 23, 2010) at 53, *available at* https://www.sec.gov/rules/final/2010/ic-29132.pdf.

[50] *See* discussion in Section II questioning first mover advantage as an underlying causal factor in connection with shareholder redemption activity in March 2020.

not been tested to show that it would be helpful for MMFs given the small pricing differentials in the securities held by MMFs. Rather, initial internal analysis conducted by members has shown that the implementation of swing pricing during March 2020 may not have had a meaningful impact on MMFs or "first mover advantage."

The FSB Report highlights that the mechanism used by swing pricing to enhance MMF resiliency is the imposition on redeeming investors the cost of their redemptions. In this regard, we highlight that a MMF is permitted to impose a liquidity fee on redemptions in certain circumstances, and these fees serve a similar purpose as the net asset value adjustments contemplated by swing pricing by allocating at least some of the costs of providing liquidity to redeeming rather than non-transacting shareholders. These liquidity fees would also generate additional liquidity to meet redemption requests. The purpose served by liquidity fees would not be diminished even if liquidity fees are delinked from requirements related to weekly liquid asset levels. Accordingly, MMFs have tools at their disposal to accomplish similar goals as swing pricing, but such tools are fashioned in a manner that reflects the unique manner in which MMFs operate in order to still permit MMFs to provide same day liquidity.

As mentioned above, many MMF investors (primarily, but not exclusively, institutional investors including governments, corporations, and not-for-profits) use intraday and same-day settlement to effectively manage day-to-day cash needs and move money in and out of their accounts intraday for a variety of time-sensitive business and personal transactions. This is considered a critical feature of MMFs for such investors. Swing pricing would likely effectively eliminate intraday settlement due to operational and timing issues where implementing swing pricing would require net shareholder flow information at the end of the day (which would not be available for intraday movements). Same-day settlement transactions are also subject to operational timing issues and imposing a swing pricing requirement could significantly impair a MMF's ability to provide same day liquidity. To effectuate same day settlement, MMFs must compute their net asset value, receive and process redemptions, and complete Fedwire instructions after the MMF's closing time (typically 4:00 pm ET) but before the Federal Reserve's Fedwire cutoff time (6:45 pm ET). For MMFs with multiple net asset value strike times, the process of computing net asset values and processing redemptions is completed multiple times a day. Receipt of net shareholder flow information is necessary to determine whether such flows exceeded the applicable threshold to implement swing pricing and also to swing the net asset value on any given day, and it is unlikely a MMF could obtain this information from the appropriate sources before the net asset value calculation process with sufficient time to calculate and implement swing pricing multiple times a day and/or meet the Federal Reserve's current cutoff time to provide Fedwire instructions for the transmittal of redemption proceeds to investors in order to accommodate same day settlement.

As noted above, in previously adopting amendments to Rule 2a-7, the Commission recognized the importance of key features of MMFs such as same day settlement and structured reforms to provide MMFs with tools to manage redemptions while also purposefully preserving "the ability of [MMFs] to function as an effective and efficient cash management tool for investors."[51] MMFs currently have tools such as liquidity fees to help manage redemptions that serve a similar purpose as the net asset value adjustments contemplated by swing pricing. Requiring swing pricing would overly complicate the MMF regulatory framework at a significant cost to MMFs,

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[51] *See supra* note 13.

shareholders, sponsors, and intermediaries, without additional benefit to justify such costs given MMFs already have a tool available to them — liquidity fees — that serves a similar purpose as the net asset value adjustments contemplated by swing pricing. Imposing swing pricing requirements on MMFs will likely serve to eliminate the ability of MMFs to function as an effective and efficient cash management tool for investors, a key feature of MMFs that the Commission previously sought to maintain. Eliminating these important features would significantly change the utility of MMFs to investors. In turn, this could cause investors to move their money to less regulated, less transparent investment vehicles. For a discussion of the negative implications of such movement, see Section III.c.i.1.

In addition, swing pricing reduces transparency and increases investor uncertainty regarding the liquidity and prices of their shares. Other operational and implementation challenges generally applicable to other open-end mutual funds related to swing pricing are also applicable to MMFs. We note that eligible U.S. mutual funds have yet to implement swing pricing largely because implementation would require substantial reconfiguration of current distribution and order-processing practices. MMFs provide no exception to these challenges. Concerns related to swing pricing may be more complex for MMFs used as sweep accounts.

i. Variants and Extensions

The FSB Report includes one variant or extension to swing pricing: authorities mandating macroprudential swing pricing. SIFMA AMG does not support this variant for the same reasons as discussed above related to the representative swing pricing option above and SIFMA AMG believes that this variant presents even further challenges than the swing pricing representative option.

Regardless of whether MMFs or authorities determine whether to implement swing pricing, the same issues will remain regarding calibrating a swing factor that produces effective results given the level of transaction costs associated with MMF trading is much lower than transaction costs of other mutual fund trading. In addition, we note that authorities do not have access to the same real-time data available to MMFs. Accordingly, MMFs and their sponsors are best positioned to consider whether to implement swing pricing and any swing factor. Further, having authorities mandate swing pricing in certain conditions could have an unintended consequence of increasing redemption behavior to the extent investors view this as a negative signal indicating trouble in the market or a particular MMF.

f. Bank-Like Policy Measures: MBR, Capital Buffer Requirements, LEB Membership, Sponsor Support

SIFMA AMG strongly opposes bank-like policy measures such as MBR requirements, capital buffer requirements, LEB membership, and mandating sponsor support. SIFMA AMG urges regulators to advance market-driven regulatory solutions rather than bank-driven measures.

Inappropriate mechanism to address liquidity concerns and respond to the events of March 2020. The FSB Report notes that the mechanism to enhance MMF resilience related to bank-like policy measures is loss absorption. In discussing this mechanism, the FSB Report notes that MMFs' susceptibility to redemptions arises in part because MMFs are exposed to credit and liquidity risk, which can cause investors to lose confidence in maintaining principal stability. The events of March 2020 are more appropriately characterized as investor concern of being unable to access money in a time of market-wide liquidity stress rather than a loss of confidence in the overall MMF wrapper as an investment product. This was primarily driven by overall market-wide liquidity concerns coupled with regulatory thresholds that may impede an investor's ability to redeem from a MMF versus any specific credit or liquidity issues in a particular MMF. During the market stresses of March 2020, all U.S. MMFs met 100% of redemptions and no U.S. MMFs "broke the buck," despite increased redemption activity. It is ineffective and inappropriate to implement policy measures that are based on a mechanism (loss absorption) to address an issue that did not occur in March 2020. As discussed above, the Commission has previously taken effective steps to reduce MMFs' exposure to credit risks in response to the 2008 credit crisis.[52] The market events of March 2020 were in response to a liquidity crisis, rather than a credit crisis, and any policy response, and mechanism to implement that response, should be tailored to address liquidity concerns. For example, capital at banks does not prevent or stop bank runs. Rather, what prevents runs or mass shareholder redemptions is a high level of liquidity, and holding liquid assets in portfolio in order to meet redemptions increases liquidity (as MMFs currently do).[53] Bank-like policy measures that impose capital requirements, however, do not increase liquidity and will not enhance MMF resiliency to the stresses faced in March 2020. For a discussion of policy measures in the FSB Report that seek to address liquidity concerns, see Section III.b.-e.

Further, each bank-like policy measure in the FSB Report seeks to address the same primary or secondary objective as other measures in the FSB Report. As discussed above, those other measures are more appropriately structured to best achieve the stated objectives in an effective manner while still maintaining the utility of the MMF product. Additional reforms that seek to achieve the same objectives are unnecessary, particularly when such reforms use a mechanism to achieve such objectives that is unrelated to the issue at hand and would entail significant negative consequences on MMFs, their sponsors, shareholders, and the short-term funding markets.

MMFs as investment vehicles and not bank accounts. Simply put, bank-like capital requirements are inappropriate for MMFs. Unlike banks, MMFs do not use leverage or hold non-transparent assets, and they do not have operating assets, use off-balance sheet financing or have deposit insurance. It is for these reasons that banks have capital buffers that are structured to shield the Federal Deposit Insurance Corporation, depositors and other creditors. Investors in MMFs are shareholders, not creditors. They are subject to potential loss, in return for a market return on their short-term investments, and this fact is clearly disclosed in MMFs' offering documents and advertisements.[54] Pursuant to Rule 2a-7, MMFs must limit their investments to short-term assets and maintain specified liquidity levels, which allow MMFs to avoid certain issues experienced by banks and to meet redemptions in most situations, thereby addressing the issue of potential runs more effectively

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[52] *See* discussion *supra* Section II.a.

[53] As explained in Section III.b., delinking liquidity with thresholds for imposing a liquidity fee or redemption gate would further improve the usability of liquid assets to meet redemptions. This would more effectively address the liquidity pressures experienced by certain types of MMFs in March 2020 as compared to imposing bank-like requirements.

[54] Item 4(b) of Form N-1A requires disclosure that states:

> You could lose money by investing in the Fund…An investment in the Fund is not insured or guaranteed by the Federal Deposit Insurance Corporation or any other government agency. The Fund's sponsor has no legal obligation to provide financial support to the Fund, and you should not expect that the sponsor will provide financial support to the Fund at any time.

See also 17 C.F.R. § 230.482(a)(4) (2021).

than capital requirements could.

Additionally, bank-like requirements encourage a false notion that MMFs are more like bank deposits than investments, thereby increasing moral hazard from the investor perspective. For example, if investors view invested principal as either insured or protected, investors may seek funds with the highest yields without consideration of the funds' risk profile.

Decrease in the size of the MMF sector and significant negative impact on short-term funding markets. Moreover, each of these policy measures would have the effect of altering the liquidity profile of MMFs in such a way that these products will no longer exist in a manner that is attractive to investors or would impose significant costs on sponsors — each of these outcomes would cause the size of the MMF industry to decrease significantly or cease to exist.[55] In this regard, we highlight the discussion under "The Important Role of Money Market Funds" in the enclosed letter submitted to the Commission and remind the FSB of the important role that MMFs play in the short-term funding markets.[56] Our members believe that asset management firms would be unable to provide the capital needed to support MMFs on a comparable scale to bank regulatory capital. The cost of the firm's holding capital on a bank-like scale would either be borne by fund shareholders (who would bear higher fees and/or lower returns, making investments in these funds less attractive), or by management firms who would likely elect to exit the MMF business. If the level of required capital cannot be sustained by the marketplace, the result of a capital requirement would be to severely curtail the availability of MMFs, eliminating an attractive cash management option for investors and eliminating a source of financing for issuers.

As discussed above, if investors reject reformed MMFs, a significant portion of redemptions from MMFs may be deposited at banks. For a discussion of the risks and considerations related to this, please see Section III.c.i.1. Further, any significant reduction in the source of financing or increase in its cost could significantly affect governments, bank and non-bank issuers and municipalities. In particular, as discussed above, MMFs are a significant source of short-term financing for the U.S. Treasury and Government Sponsored Enterprises (GSEs) as well as state and local governments and non-profit organizations, such as universities and hospitals.[57] Ultimately, increased borrowing costs are likely to be passed through to taxpayers and consumers, with potential negative consequences on local and broader global economies. Accordingly, policy measures that serve to significantly decrease or eliminate any portion of the MMF industry will not improve the resilience and functioning of short-term funding markets. In fact, such policy measures will significantly harm the resilience and functioning of short-term funding markets and undermine the overarching goals of increased resilience of MMFs and the short-term funding markets.

In short, bank-like policy measures are impractical, and we expect that they would be unattractive to investors, fund sponsors and intermediaries. In addition to the significant issues

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[55] *See, e.g.,* Craig M. Lewis, "The Economic Implications of Money Market Fund Capital Buffers," (Nov. 2013), *available at* https://www.sec.gov/files/rsfi-wp2014-01.pdf ("The analysis shows that, after compensating capital buffer investors for absorbing credit risk, the returns available to money market fund shareholders are comparable to default free securities, which would significantly reduce the utility of the product to investors").

[56] *See, e.g., supra* note 40.

[57] *See* discussion *supra* Section III.c.i.1.

noted above, each bank-like proposal presents its own individual additional challenges which are discussed below. Further, in adopting the 2014 amendments to Rule 2a-7, the Commission already considered capital buffers, MBR requirements, and LEB membership and determined such measures were not the best approach in achieving regulatory goals. The reasons the Commission did not adopt capital buffer, MBR, and LEB requirements in 2014 apply equally today, if not to a greater extent given that the use of such measures is not responsive to the specific liquidity issues that occurred in March 2020 and therefore would not effectively address any such issues.

i. MBR

Implementing MBR requirements present significant challenges with respect to transparency and complexity. The disclosure necessary to inform shareholders about the structure and ever-changing size of the MBR would be cumbersome and complex. It is unlikely that investors will be able to understand how an MBR functions. This type of policy measure introduces undue complexity to an otherwise simple product.

The complex hierarchy of share subordination under the MBR arrangement gives rise to a fundamental flaw: the arrangement punishes shareholders for exercising their right to redeem their shares. It is fundamentally unfair, and at odds with the investor protection afforded under the 1940 Act to penalize shareholders for exercising their right to access their funds.

Importantly, our members expect that shareholders will object to the delayed availability of a portion of their accounts. The MBR creates uncertainty as to available account balances, which would impede the use of MMFs to fund day-to-day operations. As noted above, same-day liquidity is of primary importance to many investors. Brokers expect that many clients will urge brokers to make available the delayed portion from other sources. Brokers may be in a position to accommodate this request from certain clients, but not others, depending on the client's other available balances and other factors. This possible differing treatment among clients is another drawback of the MBR arrangement.

Further, the technological impediments to the MBR are significant. Given the tremendous negative investor impacts of the MBR, our members expect a vast reduction in total MMF assets if the MBR is adopted, at the same time that intermediaries and MMFs would need to make extensive and burdensome changes to myriad systems to implement the MBR. Accordingly, we expect that intermediaries will be unwilling to bear the costs of implementation. We expect that the cost ultimately will be passed along to shareholders. Moreover, the MBR framework also presents implementation challenges not only for fund sponsors, but also for intermediaries that establish omnibus accounts for underlying investors in MMFs. Because shares may be held in omnibus accounts, the allocation of shares and trades across underlying investors is not always available to the MMF. Accordingly, the responsibility of implementing the MBR requirement would fall on the intermediary rather than the MMF.

SIFMA AMG further agrees with the extensive challenges listed in the FSB Report, including implementation and administration challenges for MMFs, intermediaries, and service providers; and investor confusion or unease. However, SIFMA AMG disagrees with the assertion that the reduced demand for MMFs subject to MBR requirements will only last for a period of time. Imposing this requirement on MMFs will cause many sponsors to exit the business, resulting in a potentially permanent decrease in demand. In addition to the challenges listed in the report, SIFMA AMG also highlights various U.S. state law limitations; unequal effects on investors in stable versus floating net asset value MMFs; and issues in calibrating the appropriate size of the MBR.

The FSB Report highlights that in rare, predefined events, such as material loss to the MMF over a short period of time, the loss would be absorbed by the MBR shares. such as when the fund suffers a large drop in net asset value or is closed. In this regard, we note the existence of Rule 22e-3 under the 1940 that provides an exemption from Section 22(e) of the 1940 Act (suspension of the right of redemption or postponement of date of payment) for MMF liquidations in certain circumstances when the fund's board has irrevocably approved its liquidation.[58] Rule 22e-3 is intended to reduce the vulnerability of investors to the harmful effects of a run on the MMF, and minimize the potential for disruption to the securities markets.[59] Rule 22e-3 provides MMFs options to address a run on a MMF in certain rare circumstances in a manner that is better suited to address the overarching goal of MMF resilience than the MBR policy measure presented in the FSB Report. Further, seeking to define what would qualify as a rare, predefined event to trigger loss absorption by MBR shares risks creating an unintended consequence of increased redemption activity as a MMF approaches the regulatory threshold.

In previously considering MBR requirements, the Commission expressed concern that the contingent nature of the way losses are distributed among shareholders would force early redeeming shareholders to bear the losses they are trying to avoid. The Commission also noted that an MBR requirement may cause investors who value liquidity in MMFs to shift their investments to other short-term investments with fewer restrictions on redemptions and higher yields and that "a reduction in the demand of money market instruments may have an impact on the ability of financial institutions to issue commercial paper." Further, the Commission highlighted the complexities that an MBR would introduce for what has otherwise been a relatively simple product, and that implementing an MBR could involve significant operational costs (including changes to systems and amendments to governing documents (which could require shareholder approval)). The Commission concluded that:

> [W]e continue to believe that overall, the complexity of an MBR may be more costly for unsophisticated investors because they may not fully appreciate the implications. In addition, money market funds and their intermediaries (and money market fund shareholders that have in place cash management systems) could incur potentially significant operational costs to modify their systems to reflect a MBR requirement. We believe that an MBR coupled with a [net asset value] buffer would turn money market funds into a more complex instrument whose valuation may become more difficult for investors to understand.[60]

As noted above, these conclusions and concerns apply equally today, if not to a greater degree.

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[58] 17 C.F.R. § 270.22e-3 (2021).

[59] *See* 2014 Adopting Release, *supra* note 9 at 113.

[60] *See id.* at 687.

ii. Capital Buffers

Capital buffers present significant issues with respect to shareholder transparency. Were the capital buffer drawn on, disclosing that the capital buffer has been drawn upon would risk a run by causing investor alarm, similar to how redemption behavior increased when a MMF's level of weekly liquid assets decreased closer to 30%. Rather than acting as a safety net and preventing a run, capital buffer deployment will produce the unintended consequence of triggering investor fear and therefore a run. Not disclosing that the capital buffer had been drawn on, however, would seemingly go against the transparency generally provided under Rule 2a-7.

In connection with capital buffer requirements, SIFMA AMG highlights administrative difficulties, costs related to financing, issues in building adequate capital buffers, and challenges in determining the appropriate size of the capital buffer.

In adopting the 2014 amendments to Rule 2a-7, the Commission recognized significant drawbacks with respect to requiring MMFs to maintain capital buffers. Specifically, the Commission recognized the significant costs to implement capital buffers (including opportunity costs that the Commission was unable to estimate), that buffers do not protect shareholders completely from the possibility of heightened rapid redemption activity during periods of market stress, and that shareholders have an incentive to redeem shares quickly as the buffer becomes impaired and rapid redemptions could impair a fund's business model and viability. The Commission also noted that buffers may cause funds to avoid holding risker short-term debt securities and instead hold low yielding investments that may not be consistent with investor preference and would reduce the utility of the product to investors and negatively impact capital formation. The Commission highlighted that capital buffers may negatively impact capital formation through investors moving their funds to alternative investment vehicles and managers' reducing holdings in commercial paper and municipal securities, which, the Commission specifically reported, could cause an "effect on the short-term financing markets if the decrease in demand for short-term securities from money market funds results in an increase in the cost of capital for issuers of commercial paper and other securities." Accordingly, the Commission did not adopt capital buffer requirements because the buffer "would reduce yields on money market funds and would therefore render such funds to be unattractive to many investors to a greater extent than the reforms [the Commission was] adopting."[61] The Commission's conclusions and concerns with respect to capital buffers in 2014 apply equally today, if not to a greater degree.

iii. LEB Requirements

Similar to capital buffers, LEBs present significant issues with respect to shareholder transparency were the LEB running out of capacity. Disclosing that the LEB is running out of capacity would risk a run by causing investor alarm, similar to how redemption behavior increased when a fund's level of weekly liquid assets decreased closer to 30%. Rather than acting as a safety net and preventing a run, this could produce the unintended consequence of triggering investor fear and therefore a run. Not disclosing that the LEB is running out of capacity, however, would seemingly go against the transparency generally provided under Rule 2a-7. Also, policy measures that

[61] *See id.* at 682.

involve pooling liquidity resources to be shared by all members present an unfair result to MMFs that invest in safer assets or manage their portfolios more conservatively and are therefore less likely to have a need to access the LEB.

SIFMA AMG further agrees with the extensive challenges listed in the FSB Report, including moral hazards effects and significant operational, governance, and legal hurdles. SIFMA AMG also highlights challenges related to access to the discount window by the LEB, and issues with building adequate capacity.

In previously analyzing LEB membership, the Commission expressed concern that a private liquidity facility would not have sufficient purchasing capacity in the event of a widespread run without access to the Federal Reserve's discount window and highlighted that the Commission does not have legal authority to grant discount window access to an LEB. As was raised at the Commission's roundtable on MMFs in 2011, access to the discount window would raise complicated policy considerations and likely would require legislation. Moreover, the Commission highlighted concerns about conflicts of interest inherent in an LEB managed by participants that do not all have the same interests, including related to allocating limited liquidity resources during a crisis and choosing which funds gain access. The Commission ultimately concluded that:

> These potential issues collectively created a concern that such a facility may not prove effective in a crisis and thus we would not be able to achieve our regulatory goals of reducing money market funds' susceptibility to liquidity runs and the corresponding impacts on investor protection and capital formation. Combined with [the Commission's] lack of authority to create an [LEB] with access to the Federal Reserve's discount window, these concerns ultimately have led us to not pursue this alternative.[62]

The Commission's conclusions and concerns in 2014 apply equally to the consideration of this policy measure, if not to an even greater extent.

iv. <u>Sponsor Support</u>

The FSB report provides a policy option whereby a MMF sponsor would be able to provide capital support to MMFs under predefined conditions. In the United States, MMF sponsors are already permitted to provide sponsor support, subject to certain requirements such as public disclosure through a filing with the Commission. SIFMA AMG believes the currently regulatory framework regarding sponsor support in the United States is appropriate and adequate, without the need for future reforms. SIFMA AMG cautions against permitting sponsor support in only certain predefined conditions, as the reasons a sponsor may provide support to a MMF may vary based on the facts and circumstances applicable to that particular MMF and believes proving sponsors the ability to provide support under conditions as they see fit is the most effective means to mitigate the impact of large redemptions or other adverse market conditions.

SIFMA AMG supports maintaining the ability to provide sponsor support on a discretionary basis as opposed to requiring mandatory activation of sponsor support in certain predefined

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[62] *See id.* at 693.

conditions. SIFMA AMG notes several options available in the United States to facilitate (rather than mandate) sponsor support of MMFs, which we believe is the most appropriate manner in which to govern and regulate sponsor support. For example, Rule 17a-9 under the 1940 Act permits purchases of certain securities from a MMF by an affiliate, subject to certain conditions. In fact, without an explicit requirement regarding sponsor support, MMF sponsors made purchases under Rule 17a-9 in March 2020 to support certain MMFs.

Many of the ways in which sponsor support may be structured require a detailed analysis of the affiliated transaction prohibitions in Section 17 of the 1940 Act and, at times, may require no-action or exemptive relief from the staff of the Commission.[63] Section 17 of the 1940 Act is intended to protect investors from abuses of self-dealing, a fundamental underlying policy of the 1940 Act. The Commission has issued exemptions from the prohibitions of Section 17 in order to permit funds and affiliates to enter into certain transactions, subject to various terms and conditions. However, we are not aware of situations where the Commission has mandated funds and affiliates to enter into such transactions. Doing so would be contradictory to the overarching policy of Section 17 of the 1940 Act that prohibits such affiliated transactions.

Further, certain types of sponsor support are not responsive to a liquidity crisis and would therefore not address the liquidity issues faced by MMFs in March 2020. For example, capital contributions may not provide much assistance to MMFs in a liquidity crisis. Certain types of sponsor support may also require significant tax planning to ensure the support achieves its intended effect. For example, in considering a capital contribution it is imperative to address tax provisions which may negate the restorative effect of the contribution on share value (which could require that the MMF make a distribution to shareholders in the amount of the contribution).[64] These issues would need to be considered in evaluating structures governing sponsor support. Considerations related to the size of the support and most appropriate type of sponsor support should not be subject to a "one-size-fits-all" approach and may overly complicate any regulatory framework governing sponsor support.

Accordingly, SIFMA AMG does not support making sponsor support for MMFs mandatory and instead believes the current regime of providing options to facilitate sponsor support is the most appropriate manner to regulate sponsor support. To further the ability of sponsors to support U.S. MMFs, SIFMA AMG supports the Commission codifying the temporary relief issued to the Investment Company Institute to permit the purchase of MMF securities by an affiliate where reliance on Rule 17a-9 could conflict with Section 23A and 23B of the Federal Reserve Act.[65] This could obviate the need for future Commission staff no-action letters relating to the interaction of Rule 17a-9 and certain banking law provisions, which is one way to provide more certainty with respect to sponsor support.

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[63] Section 17(a) prohibits sales of securities by an affiliate to a fund and may be implicated if an affiliate enters into an agreement to provide support to the MMF as the support agreement could be viewed as the issuance of a security to the MMF. Further, Section 17(d) prohibits joint transactions between a fund and an affiliate.

[64] *See* JOAN OHLBAUM SWIRSKY, THE GUIDE TO RULE 2A-7 (3rd ed. 2017).

[65] *See* Letter to Susan Olson, Investment Company Institute (March 19, 2020), *available at* https://www.sec.gov/investment/investment-company-institute-031920-17a.

In conclusion, the bank-like policy measures in the FSB Report are inappropriate policy measures to implement for investment vehicles like MMFs and present overly burdensome operational and administrative complexities and costs on all MMF stakeholders. These policy measures are not responsive to the issues that occurred in March 2020 and will therefore be ineffective in addressing such matters. These policy measures will eliminate or significantly decrease the MMF sector and therefore negatively impact the resiliency and functioning of the short-term funding markets.

g. Removal of Stable Net Asset Value

SIFMA AMG generally opposes the removal of a stable net asset value for applicable MMFs because such policy measure does not address the contributors to stresses in the short-term funding markets in March 2020, does not improve the resiliency or functioning of the short-term funding markets, and would not decrease the likelihood that official sector intervention is needed to address a run on a fund. During the market stress in March 2020, the U.S. MMFs that saw the heaviest outflows were institutional prime MMFs. In the United States, institutional prime MMFs were required to float their net asset values beginning in 2016. Despite the requirement for institutional prime MMFs to float their net asset values, there is no evidence that floating their net asset value impacted investor redemption behavior in March 2020.[66] Rather, investor redemption behavior was driven by liquidity concerns as opposed to concerns over a MMF's net asset value. Many of our members view imposing a floating net asset value requirement on MMFs that are not currently subject to such a requirement as (1) not addressing the types of MMFs that saw the heaviest outflows in March 2020, and (2) imposing a requirement that has proven unsuccessful in slowing redemptions on other MMFs.

The Commission has stated that a primary goal of their rulemaking is "to preserve to the extent feasible, while protecting investors and the markets, the benefits of [MMFs] for investors and the short-term funding markets by retaining a stable [net asset value] alternative."[67] The reasons that the Commission did not apply the floating net asset value requirement to certain types of MMFs still exist today. Namely, retail investors historically have behaved differently from institutional investors in a crisis, being less likely to make large redemptions quickly in response to the first sign of market stress. For example, during the March 2020 liquidity crisis, institutional prime MMFs had substantially larger redemptions than retail prime MMFs. Despite the availability of additional tools, such as liquidity fees and redemption gates and enhanced website disclosures, retail investor behavior during the COVID-19 liquidity crisis did not differ significantly from retail investor behavior during the global financial crisis. In adopting the 2014 reforms, the Commission noted that "the significant benefits of providing an alternative stable [net asset value] fund option justify the risks associated with the potential for a shift in retail investors' behavior in the future, particularly given that retail MMFs will be able to use fees and gates as tools to stem heavy redemptions should they occur."[68] Given that there was no shift in retail investors' behavior in March 2020, and retail

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[66] *See, e.g.,* Lei Li et al, *Runs and Interventions in the Time of Covid-19: Evidence from Money Funds,* CENTRE FOR ECONOMIC POLICY RESEARCH COVID ECONOMICS, Issue 29 at 53, note 3, *available at* https://cepr.org/sites/default/files/CovidEconomics29.pdf (finding further no evidence that lower floating net asset values drove additional outflows during the COVID-19 crisis).

[67] *See* 2014 Adopting Release, *supra* note 9 at 170.

[68] *See id.* at 220.

MMFs continue to have liquidity fees and redemption gates as tools to stem heavy redemptions should they occur, many of our members see no policy reason to implement a floating net asset value for MMFs that are permitted to maintain a stable net asset value at this time.

With respect to government MMFs, the Commission excluded such MMFs from the requirement to float their net asset value due to government MMFs facing different redemption pressures and having different risk characteristics than other MMFs because of their portfolio composition. This rationale is even stronger today than in 2014 because following the 2014 amendments to Rule 2a-7, government MMFs are required to hold at least 99.5% of their assets in government securities, cash, or repurchase agreements that are "collateralized fully."[69] The Commission also highlighted that government MMFs also historically experienced inflows, rather than outflows, in times of stress.[70] As discussed earlier, this remained the case during the liquidity crisis in March 2020.[71]

Importantly, the Commission also stated that it determined not to impose fees and gates and floating net asset value reforms on government MMFs in an effort to facilitate investor choice by providing a MMF investment option that maintains a stable net asset value and that does not require investors to consider the imposition of fees and gates.[72] Government MMFs in their current structure remain an important investment option for a variety of investors to meet their differing investment and liquidity needs that may not be satisfied by products subject to a floating net asset value requirement.

As previously recognized by the Commission, "[MMFs'] stable share price facilitates their role as a cash management vehicle, provides tax and administrative convenience to both [MMFs] and their shareholders, and enhances [MMFs'] attractiveness as an investment option."[73] Our members believe it remains important to continue to have the ability to offer to investors MMFs with a stable share price in order to provide the benefits noted above. Furthermore, implementing a floating net asset value would impose additional costs on applicable MMFs and their intermediaries to implement, as retail distribution channels and operations are different than institutional channels and operations that have already implemented a floating net asset value. This policy measure would likely also cause a further decrease in the size of the MMF sector, which, as discussed more fully above, would negatively impact the resilience and functioning of the short-term funding markets.

IV. Comments on Complementary Measures in the FSB Report

SIFMA AMG encourages further exploration of whether additional risk management and monitoring measures, such as further enhanced stress testing, would prove effective in enhancing MMF resiliency. In this regard, however, SIFMA AMG cautions against imposing requirements that would add undue burden to a MMF and its adviser during a time of stress.

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[69] Prior to the 2014 amendments to Rule 2a-7, Rule 2a-7 did not impose requirements as to the amount of government securities that a government MMF held. Rather, certain government MMFs were subject to Rule 35d-1 under the 1940 Act, which requires a fund to adopt a policy to invest, under normal circumstances, at least 80% of its assets in the particular type of investments suggested by the fund's name (such as, for example, government securities).

[70] *See* 2014 Adopting Release, *supra* note 9 at 204.

[71] *See supra* note 8 and related text.

[72] *See* 2014 Adopting Release, *supra* note 9 at 205.

[73] *See id.* at 15.

SIFMA AMG supports measures that aim at improving the functioning of the underlying markets. SIFMA AMG agrees with the FSB Report that the structure of the commercial paper and certificate of deposit markets make them susceptible to illiquidity in times of stress. SIFMA AMG also agrees with the FSB Report that MMF reforms by themselves will not likely solve the structural fragilities in short-term funding markets. SIFMA AMG therefore supports a holistic approach to reforms and consideration of measures to improve the functioning, efficiency, and transparency of the commercial paper and certificate of deposit markets.

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SIFMA AMG sincerely appreciates the opportunity to comment and your consideration of these views. We stand ready to provide any additional information or assistance that the FSB might find useful. In particular, we and our members would welcome the opportunity to work with the FSB and other industry representatives to address future policy measures for MMFs. Please do not hesitate to contact either Timothy Cameron at (202) 962-7447 or tcameron@sifma.org or Lindsey Keljo at (202) 962-7312 or lkeljo@sifma.org with any questions.

Respectfully submitted,

Timothy W. Cameron, Esq.
Asset Management Group – Managing Director and Head
Securities Industry and Financial Markets Association

Lindsey Weber Keljo, Esq.
Asset Management Group – Managing Director and Associate General Counsel
Securities Industry and Financial Markets Association

Enclosures: SIFMA AMG comment letter on PWG Report, dated April 12, 2021

sifma
asset management group

April 12, 2021

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

Re: **Potential Reform Measures for Money Market Funds (File No. S7-01-21)**

Dear Ms. Countryman:

The Asset Management Group of the Securities Industry and Financial Markets Association ("**SIFMA AMG**")[1] respectfully submits this comment letter to the U.S. Securities and Exchange Commission (the "**Commission**") with respect to the Commission's request for comment on potential reform measures for money market funds, as highlighted in the Report of the President's Working Group on Financial Markets dated December 2020 (the "**Report**").[2] We appreciate the opportunity to provide our views to the Commission on these matters that have the potential to impact not only the direct regulation of money market funds, but also the overall functioning of the short-term funding markets.

Our comments focus on the following main points:

1. The important role of money market funds and the effectiveness of previously enacted reforms to money market funds. Money market funds play an important role in the orderly functioning of the short-term funding markets and serve valuable financial and economic functions for a variety of investors (including both retail and institutional investors) and the capital markets more broadly. Policy measures that have the effect of eliminating or significantly decreasing the size of the prime, retail, and tax-exempt money market fund sectors will significantly impair the resilience and orderly functioning of the short-term funding markets.

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[1] SIFMA AMG brings the asset management community together to provide views on policy matters and to create industry best practices. SIFMA AMG's members represent U.S. and multinational asset management firms whose combined global assets under management exceed $39 trillion. The clients of SIFMA AMG member firms include, among others, tens of millions of individual investors, registered investment companies, endowments, public and private pension funds, UCITS and private funds such as hedge funds and private equity funds.

[2] Request for Comment on Potential Money Market Fund Reform Measures in President's Working Group Report, Investment Company Act Release 34188 (Feb. 4, 2021), *available at* https://www.sec.gov/rules/other/2021/ic-34188.pdf.

As a result of reforms adopted after the global financial crisis, money market funds proved more liquid, resilient, and able to handle the stresses of March 2020. These prior reforms helped ensure all types of institutional and retail money market funds, including government, prime, and tax-exempt money market funds, were able to successfully manage the unprecedented liquidity challenges in March 2020 and provide investors with daily liquidity and meet 100% of redemptions. Certain aspects of the reforms adopted in 2014, mainly the linking of levels of liquidity with the ability to impose liquidity fees and redemption gates, proved to have negative unintended consequences that amplified the redemption behavior exhibited by certain types of prime money market fund investors (most notably, institutional prime money market fund investors) in response to the market-wide lack of liquidity that arose in March 2020. Accordingly, the delinking of liquidity thresholds from the imposition of liquidity fees and redemption gates should be the focus of any potential future rulemaking.

2. The liquidity crisis in March 2020 and a narrowly tailored money market fund policy response. An unprecedented and rapidly developing market-wide liquidity crisis occurred in March 2020 fueled by the COVID-19 pandemic. Money market funds were not the root cause of the stresses in the short-term funding markets in March 2020, but, rather, like other participants in the short-term funding markets, were reacting to and managing through a market-wide liquidity crisis. Policy responses to the liquidity crisis in March 2020 should focus on and prioritize addressing root causes in the segments of the short-term funding markets that caused market stresses in March 2020. Any policy measures should be narrowly tailored, data driven, simple to understand and implement, and calibrated to address the liquidity pressures that manifested in a relatively small segment of the money market fund industry in a manner that preserves the viability of such products for investors.[3] A broadly tailored, "one-size-fits-all" approach is not appropriate based on the data derived from the market stress events of March 2020 and would invite the potential for far-reaching, unintended consequences and potential harm to the functioning of the short-term funding markets.

3. Effectiveness of policy measures in the Report. As more fully discussed herein, SIFMA AMG views delinking liquidity thresholds and liquidity fees and redemption gates as the most effective way to achieve the stated goals of money market fund reform. SIFMA AMG supports exploration of other alternatives when a money market fund's weekly liquid assets drop below a specified threshold in a manner that does not motivate increased redemption behavior or impede the usability of weekly liquid asset buffers, such as additional board reporting, requiring a fund to overcorrect (e.g., increase its level of weekly liquid assets to a specified percentage above 30%, such as 35%), or prohibiting additional purchases of any non-overnight instruments until the minimum level of weekly liquid assets is reestablished.
    a. Exclusion of government money market funds. SIFMA AMG strongly agrees with the Report's exclusion of money market funds that operate as

[3] As further discussed herein, although SIFMA AMG believes policy measures should be narrowly tailored to address the liquidity pressures experienced by a relatively small segment of the money market fund industry, SIFMA AMG supports applying the delinking policy measure discussed below to all types of money market funds that are currently subject to liquidity fees and redemption gates as the dynamics that motivate redemptions in the face of a bright line liquidity threshold that is tied to a liquidity fee or redemption gate apply regardless of the type of money market fund. *See infra* note 20 for information on the size of various segments of the money market fund sector.

"government money market funds" from future rulemaking. Government money market funds are an increasingly valuable and popular liquidity vehicle for investors, which has been highlighted by their significant inflows during the market stresses in March 2020.

b. Delinking liquidity and liquidity fee and redemption gate thresholds. SIFMA AMG strongly supports the delinking of money market fund liquidity and fee and gate thresholds. Our members view this policy measure as most directly and meaningfully addressing, in a practical manner, the issues that contributed to stresses on money market funds and the short-term funding markets in March 2020. SIFMA AMG believes delinking liquidity and thresholds for liquidity fees and redemption gates is an essential element of any reform for money market funds.

c. Countercyclical weekly liquid asset requirements. SIFMA AMG views countercyclical weekly liquid asset requirements as a less effective policy measure than the delinking of liquidity and liquidity fees and gates in resolving the liquidity pressures experienced by certain types of money market funds in March 2020 and achieving the overall goals of money market fund reform. Although countercyclical requirements may be useful in principle, SIFMA AMG views countercyclical requirements as having the potential to create a bright line test that can increase redemption behavior and believes difficulty in administering countercyclical requirements can impede any countercyclical requirement's effectiveness. SIFMA AMG therefore supports the delinking of liquidity and liquidity fees and redemption gates over imposing countercyclical weekly liquid asset requirements because should the Commission delink liquidity and liquidity fees and redemption gates, many of the benefits of the countercyclical weekly liquid asset policy measure will have been achieved (lessening redemption pressures as a money market fund approaches a specified level of minimum weekly liquid assets and improving the usability of liquidity buffers) but in a more effective manner with potential for fewer unintended consequences than through countercyclical weekly liquid asset requirements.

d. Liquidity management changes.[4] While in principle SIFMA AMG does not generally oppose certain liquidity management changes, many of our members believe these changes will be less effective than the delinking of liquidity and fees and gates in addressing the specific issues presented in March 2020 and achieving the overall goals of money market fund reform. Should the Commission consider liquidity management changes, SIFMA AMG believes any such changes should be focused on the types of money market funds that experienced higher redemptions in March 2020 as part of a reform package that includes the delinking of liquidity with liquidity fees and redemption gates. SIFMA AMG strongly opposes automatic financial or punitive measures in connection with liquidity management changes.

e. Reforms of imposing redemption gates. While SIFMA AMG does not generally oppose certain reforms of conditions for imposing redemption gates, SIFMA AMG believes these measures will be less effective than the delinking of

[4] Some of our members have differing views regarding imposing a higher weekly liquid asset minimum and the types of money market funds to which such changes should apply, and many of them will submit these views to you in their separate comment letters.

liquidity and fees and gates in addressing the specific issues presented in March 2020 and achieving the overall goals of money market fund reform.

f. Swing pricing. SIFMA AMG does not support swing pricing requirements for money market funds and believes that implementing swing pricing requirements for money market funds would be ineffective in achieving the goals for reform included in the Report. Swing pricing presents significant operational impediments in implementation due to the settlement process for money market funds, fundamental differences between redemption activity and related transaction costs of money market funds as compared to other types of open-end mutual funds, and significant costs and burdens associated with implementation. Swing pricing would also result in the elimination of intraday settlement and impede a money market fund's ability to ensure same-day settlement, a key feature and benefit for various types of investors. Further, many of the reasons that swing pricing may benefit other types of mutual funds in managing liquidity risks are less applicable to money market funds, including that money market funds routinely handle large redemptions without similar transaction costs that may be borne by other types of open-end mutual funds.

g. Bank-like requirements. SIFMA AMG strongly opposes bank-like requirements for money market funds, such as minimum balance at risk ("**MBR**") requirements, capital buffers, requiring liquidity exchange bank ("**LEB**") membership, or requiring sponsor support. Such policy measures do not advance the stated goals of money market fund reform and are not responsive to (and therefore not effective in addressing) the liquidity stresses that arose in March 2020. Such requirements would have the effect of eliminating or significantly decreasing the size of the prime and tax-exempt money market fund sectors, thereby impairing the resilience and orderly functioning of the short-term funding markets. SIFMA highlights the role of the Commission as the primary regulator of money market funds and urges the Commission to advance market-driven regulatory solutions rather than bank-driven measures.

h. Floating net asset value for all prime and tax-exempt money market funds. SIFMA AMG generally opposes a requirement for all prime and tax-exempt money market funds to float their net asset value because such policy measure does not address the types of money market funds that experienced the largest outflows in March 2020 and the implementation of a floating net asset value for prime institutional money market funds did not prove effective in slowing redemptions in March 2020. Many of our members generally do not view this policy measure as advancing the stated goals of money market fund reform, and find such policy measure not responsive to (and therefore not effective in addressing) the market-wide liquidity stresses that arose in March 2020.

I. Summary of Report and Request for Comment

The Report is intended to begin the important process of review and assessment in response to stresses in the short-term funding markets in March 2020. After providing background on money market funds, prior reform measures applicable to money market funds, and the events in certain short-term funding markets in March 2020, the Report sets forth 10 potential policy measures to address the risks prime and tax-exempt money market funds may pose to short-term funding markets. These potential policy measures for prime and tax-exempt money market funds include:

- Removal of the tie between money market fund liquidity and fee and gate thresholds
- Reform of conditions for imposing redemption gates
- MBR
- Liquidity management changes
- Countercyclical weekly liquid asset requirements
- Floating net asset values for all prime and tax-exempt money market funds
- Swing pricing requirement
- Capital buffer requirements
- Require LEB membership
- New requirements governing sponsor support

The Report sets forth three overarching goals of reform:

- Would the reforms effectively address the money market fund structural vulnerabilities that contributed to stress in short-term funding markets?
- Would the reforms improve the resilience and functioning of short-term funding markets?
- Would the reforms reduce the likelihood that official sector interventions and taxpayer support will be needed to halt future money market fund runs or address stresses in short-term funding markets generally?

The Commission has requested comment on the potential policy measures described in the Report both individually and in combination. The Commission has also requested comment on the effectiveness of previously enacted money market fund reforms, and the effectiveness of implementing policy measures described in the Report in addition to, or in place of, previously enacted reforms, as well as other topics relevant to further money market fund reform, including other approaches for improving the resilience of money market funds and short-term funding markets generally. The Commission has asked commenters to address the effectiveness of the measures in achieving the overarching goals of reform listed in the Report. Commenters also may address the potential impact of the measures on money market fund investors, fund managers, issuers of short-term debt, and other stakeholders.

We thank the Commission for the opportunity to comment on potential reform measures for money market funds. SIFMA AMG recognizes the critical importance of ensuring the resiliency of money market funds and the important role that money market funds, particularly prime and tax-exempt money market funds, play in the short-term funding markets. We applaud the Commission for taking steps to evaluate how the resiliency of money market funds may be further improved, after taking into account the impact of previously enacted reforms and the role of money market funds in the overall short-term funding markets, and engaging with the industry in doing so.

II. The Important Role of Money Market Funds in the Short-Term Funding Markets

Money market funds play an important role in the orderly functioning of the short-term funding markets. This role has been recognized by various regulatory authorities, including recently by the staff of the Division of Economic and Risk Analysis of the Commission where the staff recognized that "[t]hrough their participation in the [short-term funding markets], [money market funds] serve an important financial and economic function for both retail and institutional investors and for the capital markets" and are an "important participant" in the short-term funding markets.[5]

Money market funds are an attractive investment product for various types of investors and provide integral cash management solutions. Money market funds provide investors with a highly regulated product that provides the benefits of high levels of liquidity, minimal credit risks, diversity of holdings, strict maturity requirements, low principal volatility, and a high level of transparency. Money market funds also offer investors same day liquidity, a valuable feature and benefit to many types of investors. The ability to use the amortized cost method of valuation to maintain a stable net asset value contributes to the popularity of retail and government money market funds as a popular cash management vehicle, providing tax and administrative efficiencies to such funds and their shareholders.

Money market fund investors include individual investors, retirement accounts, college savings plans, health savings plans, endowments, small businesses, large corporations, pension plans, state and local governments, variable annuities, insurance companies, and nonprofit organizations. Different types of investors tend to use money market funds to meet different objectives. For example, retail investors may use money market funds for saving over a longer term, as an alternative to bank deposit accounts, or to take temporary defensive positions in declining equity markets; whereas institutional investors typically use money market funds as transactional accounts for cash management purposes. These different objectives impact investors' redemption behaviors.[6] During times of volatility (such as in March 2020) when investors are uncertain where to invest their money, money market funds provide a valuable safe haven to investors given their highly regulated structure. Money market funds provide investors with an important highly-regulated alternative to bank accounts and to less regulated and less transparent liquidity vehicles. This is increasingly important to the extent banks may be unable or unwilling to accept additional deposits due to capital requirements, as money market funds can be used to fill an important gap in the market and provide a safe, highly-regulated alternative.[7]

Money market funds help support the economy through their significant investments in various high quality, short-term debt securities, including commercial paper, certificates of deposit, repurchase agreements, Treasuries, U.S. government agency debt, variable rate demand notes, state and municipal securities, and Eurodollar deposits. Many businesses and corporations manage their liquidity needs through money market funds, including managing payroll, paying office leases, and moving cash to finance daily operations. Money market funds (primarily prime money market funds) provide significant financing to businesses and financial institutions through the purchase of commercial paper, certificate of deposits, and Eurodollar deposits. Money market funds (primarily tax-exempt money market funds) also provide significant financing to state and local governments to help meet short-term financing needs through investments in variable rate demand notes issued by state and local

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[5] DIVISION OF ECONOMIC AND RISK ANALYSIS OF THE COMMISSION, US CREDIT MARKETS: INTERCONNECTEDNESS AND THE EFFECTS OF THE COVID-19 ECONOMIC SHOCK 24 (2020), *available at* https://www.sec.gov/files/US-Credit-Markets_COVID-19_Report.pdf (highlighting that, for example, money market funds invest about $250 billion in commercial paper, $950 billion in repurchase agreements, and $540 billion in short-term securities issued by Federal Home Loan Banks).

[6] Differences in redemption behavior between retail and institutional investors have been recognized previously by the Commission. *See* Money Market Fund Reform; Amendments to Form PF, Investment Company Act Release No. 31166 (July 23, 2014) at 241, *available at* www.sec.gov/rules/final/2014/33-9616.pdf [hereinafter 2014 Adopting Release] ("retail investors historically have behaved differently from institutional investors in a crisis, being less likely to make large redemptions quickly in response to the first sign of market stress"). As discussed under "The Liquidity Crisis of March 2020," these differences in redemption behavior were also evident in March 2020.

[7] See *infra* note 11 and accompanying text.

governments. Money market funds are also a source of financing for non-profit organizations, such as universities and hospitals. Without prime and tax-exempt money market funds, the cost of financing for all of these institutions and their related projects would likely increase and be less efficient, thereby disrupting the flow of short-term capital to businesses and negatively impacting governments, bank and non-bank issuers, and municipalities.

Reforms that significantly alter the structure, including the liquidity profile, of prime or tax-exempt funds, or make prime or tax-exempt money market funds an unviable option for sponsors, will result in significant harm to the overall functioning of the short-term funding markets. More specifically, reforms that eliminate or further reduce the size of the prime or tax-exempt money market fund sectors will significantly impair available financing to businesses, corporations, financial institutions, hospitals, universities, and state and local governments, and will limit the amount and types of products available to meet investors' investment and liquidity needs. Reforms that further reduce or eliminate the size of the prime or tax-exempt money market fund sectors will also significantly impact the commercial paper market by reducing the number of purchasers of commercial paper.[8] Money market funds represented approximately 21% of the commercial paper market as of June 2020.[9] The commercial paper market is used for the financing of payrolls and accounts payable and inventories, and represents funding that is essential to maintain employment. If the commercial paper market constricts greatly because of the elimination or reduction in size of prime money market funds, the cost of financing for businesses and financial institutions is likely to increase and the access to the short-term markets will likely be compromised. This, in turn, is likely to negatively impact operations of businesses and financial institutions in a meaningful way.[10]

Moreover, if the size of prime and tax-exempt money market funds further decreases (or such products are eliminated), then other potentially less regulated and less transparent vehicles may represent a larger portion of the front-end of the yield curve. In handling any future unforeseen market-wide liquidity or other crisis, regulators would potentially have less transparency into the front-

[8] Total U.S. commercial paper outstanding as of June 30, 2020 was approximately $1,007 billion. This is about one half of the all-time high in commercial paper outstanding in July 2007. Money market funds used to account for nearly 47% of the commercial paper market in September 2001. Money market fund participation in the commercial paper market has declined, particularly as the government money market fund sector increased and the prime money market fund sector decreased following fundamental reforms to Rule 2a-7 adopted in 2014. As assets in prime money market funds declined, there existed lower demand for commercial paper from money market funds. DIVISION OF INVESTMENT MANAGEMENT'S ANALYTICS OFFICE OF THE COMMISSION, PRIMER: MONEY MARKET FUNDS AND THE COMMERCIAL PAPER MARKET 2-3 (2020), *available at* https://www.sec.gov/files/primer-money-market-funds-commercial-paper-market.pdf.

[9] *See* INVESTMENT COMPANY INSTITUTE REPORT OF THE COVID-19 MARKET IMPACT WORKING GROUP, EXPERIENCES OF US MONEY MARKET FUNDS DURING THE COVID-19 CRISIS 6 (2020), *available at* https://www.sec.gov/comments/credit-market-interconnectedness/cll10-8026117-225527.pdf [hereinafter ICI COVID-19 REPORT] and DIVISION OF ECONOMIC AND RISK ANALYSIS OF THE COMMISSION, US CREDIT MARKETS: INTERCONNECTEDNESS AND THE EFFECTS OF THE COVID-19 ECONOMIC SHOCK 25 (2020), *available at* https://www.sec.gov/files/US-Credit-Markets_COVID-19_Report.pdf.

[10] For examples of letters regarding the importance of money market funds to issuers and the potential risks if money market funds shrink, *see Oversight of the Mutual Fund Industry: Ensuring Market Stability and Investor Confidence: Hearing Before the Subcomm. on Capital Mkts. and Gov't Sponsored Enter. of the Comm. on Financial Serv.*, 112th Cong. 226 (2011) (Letter from James A. Kaitz, President and CEO, Association for Financial Professionals), *available at* http://financialservices.house.gov/UploadedFiles/112-42.pdf. *See also*, Joint Letter of the American Public Power Association, Council of Development Finance Agencies, Council of Infrastructure Financing Authorities, Government Finance Officers Association, International City/County Management Association, International Municipal Lawyers Association, National Association of Counties, National Association of Local Housing Financing Agencies, National Association of State Auditors, Comptrollers and Treasurers, National Association of State Treasurers, National League of Cities, U.S. Conference of Mayors, *available at* www.sec.gov/comments/4-619/4619-130.pdf.

end of the yield curve to the extent there is a smaller prime and tax-exempt money market fund sector (highly regulated vehicles) in the front-end of the yield curve. This could prove increasingly challenging to regulators and impede regulators' efforts, particularly during a time of market stress.

Moreover, in considering policy responses that may eliminate or shrink the prime or tax-exempt money market fund market, we encourage the Commission to consider where money from prime and tax-exempt funds will go and the remaining options for businesses, financial institutions, and state and local governments to find financing to help meet short-term financing needs. For example, we encourage the Commission to explore whether banks could handle inflows of money that would otherwise have been invested in prime and tax-exempt money market funds.[11] As mentioned earlier, investors use certain money market funds as an alternative to bank deposits. Should such funds no longer exist, and banks are unable to accept additional deposits (or penalize some investors for increasing deposits), investor choice for cash management vehicles would be severely curtailed. Policy responses that eliminate or shrink the prime or tax-exempt money market fund market may drive money into other types of cash pools that are less regulated, to markets that are outside U.S. regulatory oversight, or to products that otherwise introduce increased investment risk.[12] This would increase risks to shareholders and to the U.S. financial markets.

In light of the Commission's mission to protect investors and also facilitate capital formation, prior to any proposed rulemaking on the regulation of money market funds and with the opportunity for comments prior to any rulemaking proposal, SIFMA urges the Commission and its staff to conduct their own comprehensive studies on the economic impact of potential proposals on not only money market funds but also the commercial paper and short-term funding markets. This would include, for example, how any reforms may impact the demand and viability of different types of money market funds and the implications for investors, financial institutions, corporate borrowers, municipalities, and states that sell their debt to money market funds (such as increases in the cost of financings for such entities). Eliminating or further significantly decreasing the size of the prime and tax-exempt money market fund sectors will have real consequences for not only such money market funds themselves, but also the businesses, corporations, financial institutions, hospitals, universities, and state and local governments that use money market funds for their liquidity and financing needs, and the commercial paper and short-term funding markets in general.

III. The Effectiveness of Previously Enacted Reforms

In 2010, the Commission adopted amendments to Rule 2a-7 under the Investment Company Act of 1940, as amended ("**1940 Act**"), that tightened the risk-limiting conditions of Rule 2a-7 and

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[11] This is especially relevant given the Federal Reserve's announcement that the Federal Reserve will not extend a temporary exemption that impacts the amount of capital banks must keep in reserve. *See* Board of Governors of the Federal Reserve System, "Federal Reserve Board Announces that the Temporary Change to its Supplementary Leverage Ratio (SLR) for Bank Holding Companies Will Expire as Scheduled on March 31" (March 19, 2021), *available at* https://www.federalreserve.gov/newsevents/pressreleases/bcreg20210319a.htm. If a bank is in danger of breaching capital requirements, banks may stop taking deposits, which count on their balance sheets as assets.

[12] This concern has been previously recognized by the Commission. *See* 2014 Adopting Release, *supra* note 6 at 74. We note that given the less regulated, and therefore less transparent, nature of other types of cash pools, it is difficult to analyze the amount of money that flowed out of money market funds regulated under Rule 2a-7 and into such products in connection with the implementation of the 2014 amendments to Rule 2a-7. We further note that while government money market funds saw significant inflows in conjunction with outflows from prime money market funds upon implementation of the 2014 amendments to Rule 2a-7, it is difficult to determine whether those flows remained in government money market funds or ultimately went to less regulated products.

included new liquidity and shorter maturity requirements. In 2014, the Commission adopted fundamental reforms to Rule 2a-7 that: (i) required money market funds that do not qualify as "government money market funds" or "retail money market funds" to float their net asset value (removing such funds' ability to use the amortized cost method of valuation to maintain a stable price per share), and (ii) provided money market funds with the ability to impose a liquidity fee or redemption gate in certain circumstances.[13] The 2014 reforms also included increased diversification requirements, enhanced stress testing, and increased transparency through additional website and other types of reporting and disclosures. In 2015, the Commission then adopted further amendments to Rule 2a-7 to remove references to credit ratings, provide more guidance on specific credit or asset quality factors to be taken into consideration in making a determination as to the eligibility of securities for purchase by money market funds, and further tighten diversification requirements. These previously enacted reforms were intended to make money market funds less susceptible to a run, provide funds with tools to address a run on the fund, and increase the overall resiliency of money market funds. These reforms were in response to the credit crisis in 2008 when a money market fund "broke the buck" following the announcement of Lehman Brothers Holdings Inc.'s bankruptcy.

As a result of these reforms, money market funds proved more liquid, resilient, and able to handle the stresses of March 2020. For example, following the 2010 reforms, institutional prime money market funds held on average 43% of their assets in weekly liquid assets, as compared to 33% of their assets prior to the 2010 reforms. Retail money market funds experienced an even larger increase, with weekly liquid asset levels rising from an average of 27% (from 2007 to 2009) to 41% (from 2010 to June 2020).[14] Further, weighted average maturities of money market funds are shorter than before the global financial crisis, making money market funds less susceptible to risks related to rising interest rates.[15] Reforms that increased shareholder transparency contributed to greater certainty and investor confidence in money market fund products. SIFMA AMG applauds the work of the Commission in adopting prior reforms to Rule 2a-7 designed to make money market funds better equipped to handle market stresses and meet redemptions.

Certain aspects of the 2014 reforms, however, had negative unintended consequences that contributed to, or exacerbated, stresses in March 2020 and that require reevaluation in light of the events of March 2020. Liquidity fees and redemption gates adopted as part of the 2014 reforms were intended to provide money market funds with tools to address a run on a fund. A liquidity fee or redemption gate may be imposed with action by a fund's board of trustees/directors when a fund's level of weekly liquid assets falls below 30%.[16] Under Rule 2a-7, a fund's level of weekly liquid assets is

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[13] Specifically, if, at any time, a money market fund has invested less than 30% of its total assets in weekly liquid assets, the fund may institute a liquidity fee or suspend the right of redemption temporarily if the fund's board of trustees/directors determines that the fee or suspension of redemptions is in the best interests of the fund. If, at the end of a business day, a money market fund has invested less than 10% of its total assets in weekly liquid assets, the fund must institute a liquidity fee, effective as of the beginning of the next business day, unless the fund's board of directors/trustees determines that imposing the fee is not in the best interests of the fund. Requirements related to liquidity fees and redemption gates do not apply to government money market funds. A government money market fund, however, may choose to rely on the ability to impose liquidity fees and suspend redemptions consistent with the provisions of Rule 2a-7. 17 C.F.R. § 270.2a-7(c)(2) (2021).

[14] *See* ICI COVID-19 REPORT, *supra* note 9 at 23.

[15] *See id* at 22-23. Specifically, for the 12-month period from September 2007 through August 2008, the average weighted average maturity for prime money market funds was 46 days. Conversely, for the 12-month period from March 2019 through February 2020, the average weighted average maturity for prime market funds was 35 days. Over the same period, government money market funds' average weighted average maturity decreased by three days (from 35 days to 32 days), and tax-exempt money market funds' average weighted maturity increased by two days (from 28 days to 30 days).

[16] *See supra* note 13.

required to be posted on its website on a daily basis.[17] In March 2020, outflows from institutional prime money market funds increased as the level of weekly liquid assets dropped closer to 30% as institutional investors sought to avoid the potential of being invested in a fund that may impose a liquidity fee or redemption gate.[18] This dynamic, in turn, prevented money market funds from using their weekly liquid asset liquidity buffers to meet redemptions, as money market funds feared a decrease in weekly liquid assets would further exacerbate redemptions. This is evidenced by the fact that the institutional money market funds that engaged in Rule 17a-9 transactions in March 2020 did so while such funds had weekly liquid assets above 30%. Rather, such funds engaged in such transactions to promote and provide liquidity and avoid additional redemption pressure caused by the regulatory structure enacted in the 2014 reforms. Whereas reforms to increase transparency attributed to reduced investor uncertainty in various ways, the uncertainty of whether a liquidity fee or redemption gate would be put in place upon a money market fund crossing a certain liquidity threshold contributed to stresses on money market funds in March 2020. These tools that were provided as part of the 2014 reforms to help address a run on a fund, in their current form, actually contributed to and exacerbated redemptions at a time of a market-wide liquidity crisis, creating liquidity pressures for certain prime money market funds.

The reforms adopted in 2014 also included other structural changes, namely, the requirement to float a money market fund's net asset value for funds that do not qualify as "government money market funds" or "retail money market funds" under Rule 2a-7. This structural change removed the ability of such funds to "break the buck" and was implemented in response to the credit events in 2008 to mitigate "first mover advantage" in funds that maintain a stable net asset value. It is significant that the money market funds with the heaviest outflows in March 2020 were funds with a floating net asset value, namely institutional prime money market funds. This highlights that a floating net asset value does not solve the problem of how to slow redemptions on a money market fund in a liquidity crisis. Policy measures that may be effective in responding to a credit crisis, such as the global financial crisis, are not necessarily effective in responding to a liquidity crisis, such as the impact of COVID-19 in March 2020.

The reforms adopted in 2014 also caused a large decrease in the size of the prime and tax-exempt money market fund sector. Over $1 trillion left the prime and tax-exempt money market fund industry in anticipation of the implementation of the 2014 reforms in 2016. This shift helps explain why outflows from prime money market funds on an aggregate dollar basis were smaller during COVID-19 market stresses than during the global financial crisis because there was less money in the prime and tax-exempt money market fund sector overall. Importantly, however, the 2014 reforms were structured in a manner that allowed these money market funds to continue to exist to preserve the valuable function that these money market funds provide to the short-term funding markets.

Overall, previously enacted reforms were successful in making money market funds better equipped to handle market-wide stresses and SIFMA AMG urges the Commission to focus on policy

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[17] 17 C.F.R. § 270.2a-7(h)(10)(ii) (2021).

[18] From March 17 to March 24, average outflows were much stronger from institutional prime money market funds with weekly liquid assets at or below 35% as compared to money market funds with weekly liquid assets above 35%, despite the fact that these funds held liquid assets above the regulatory minimum of 30% of weekly liquid assets. *See* ICI COVID-19 REPORT, *supra* note 9 at 33. The acceleration of outflows as prime funds' weekly liquid assets fell closer to 30% has also been acknowledged by the staff of the Division of Economic and Risk Analysis of the Commission. *See* DIVISION OF ECONOMIC AND RISK ANALYSIS, US CREDIT MARKETS: INTERCONNECTEDNESS AND THE EFFECTS OF THE COVID-19 ECONOMIC SHOCK 25 (2020), *available at* https://www.sec.gov/files/US-Credit-Markets_COVID-19_Report.pdf.

measures that directly address the liquidity pressures experienced by a small segment of the money market fund sector in March 2020.[19]

IV. The Liquidity Crisis in March 2020

In order to effectively evaluate policy measures aimed at addressing the liquidity pressures that manifested themselves in certain non-government money market funds during the market-wide liquidity events of March 2020, in light of the overarching goals of reform, it is important to fully understand the market events that occurred in March 2020 and the causes of, and contributions to, such events.

Money market funds are an important source of funding for the short-term funding markets and, like other participants in the short-term funding markets, experienced stress resulting from market-wide liquidity events related to the COVID-19 pandemic. Playing a role in the markets and reacting to market stresses, however, should not be confused with causing such market stresses. Money market funds were not the root cause of the stresses in the short-term funding markets in March 2020, but, rather, were like other participants in the short-term funding markets managing through a much larger market-wide liquidity crisis.[20]

An unprecedented liquidity crisis occurred in March 2020 fueled by the COVID-19 pandemic. As fears grew of possible business disruptions in light of government lockdown orders and access to liquidity, investors (particularly institutional investors) became increasingly risk adverse and sought to preserve or increase liquidity. At the same time, the U.S. dollar surged against other currencies and there existed extraordinary demand for U.S. dollar liquidity. Foreign central banks sold over $100 billion in U.S. Treasury debt in March 2020. These events created a liquidity crisis and placed unprecedented pressure on all participants in the short-term funding markets, including some non-government money market funds.

Concurrently with these events (states issuing lockdown orders and investors rapidly seeking to preserve or increase liquidity), financial institutions and corporations were also using money market funds in the ordinary course of routine business for ongoing cash management, such as payroll expenses. In fact, tax return filings for partnerships and S-corporations were due on March 16, 2020[21] and many businesses had biweekly or semimonthly payroll expenses around the same time. Outflows from money market funds in March 2020 also included these types of routine flow activity. Money market funds are used by many financial institutions (including pension funds, insurance companies, corporations, and other funds) to manage their liquidity and cash management needs and as corporate treasurers redeemed from institutional prime money market funds to ensure unrestricted access to their

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19 As of April 7, 2021, prime money market funds had approximately $512.16 billion in assets under management (representing approximately 11.4% of the money market fund sector). Of that, approximately $261.99 billion consisted of institutional prime money market fund assets under management (representing approximately 5.8% of the money market fund sector). As of April 7, 2021, tax-exempt money market funds had approximately $99.44 billion in assets under management (representing approximately 2.2% of the money market fund sector). Investment Company Institute, *Money Market Fund Assets* (Apr. 8, 2021), https://ici.org/research/stats/mmf/mm_04_08_21.

20 This concept is acknowledged in the Report, noting that "there were other stresses in short-term funding markets in March 2020 that may have contributed to the pressure on [money market funds]." *See* PRESIDENT'S WORKING GROUP ON FINANCIAL MARKETS, OVERVIEW OF RECENT EVENTS AND POTENTIAL REFORM OPTIONS FOR MONEY MARKET FUNDS 19 (2020), *available at* https://home.treasury.gov/system/files/136/PWG-MMF-report-final-Dec-2020.pdf.

21 Internal Revenue Service, *Filing and Payment Deadlines Questions and Answers* (last updated Nov. 19, 2020), https://www.irs.gov/newsroom/filing-and-payment-deadlines-questions-and-answers.

cash during the liquidity crisis in March 2020, such funds were forced to sell some of their holdings in a market with few buyers to meet redemptions. This, in turn, placed liquidity pressures on some of these funds.

Different types of money market funds experienced different levels of flows in response to the market-wide liquidity crisis in March 2020.[22] Both retail and government money market funds performed well during the period of market stress in March 2020 and proved very resilient.[23] Retail money market funds experienced modest outflows in March 2020. Retail prime money market funds experienced net redemptions of 9% (approximately $40 billion) during the two-week period March 13 to March 26, and tax-exempt money market funds[24] experienced net redemptions of 8% (approximately $11 billion) during the two-week period March 12 to March 25.[25] As noted in the Report, there does not appear to be a relationship between a decline in a particular retail money market fund's market-based price and the size of its outflows. Overall dollar amounts of tax-exempt money market fund outflows in March 2020 were less than during the global financial crisis in 2008, thereby presenting less of an overall impact to the overall short-term funding markets.[26]

Public institutional prime money market funds experienced net redemptions of 30% (approximately $100 billion) during the two-week period March 11 to March 24. This is approximately $250 billion less than outflows experienced during the two-weak peak in September 2008, thereby presenting less of an overall impact to the overall short-term funding markets, although outflows were slightly larger compared to 2008 when viewed on a percentage basis. Non-public institutional prime money market funds[27] experienced outflows representing approximately 6% of assets (approximately $17 billion) during the period March 9 to March 20.[28] SIFMA AMG agrees with the finding in the Report that the outflows experienced by non-public institutional prime money market funds show that such funds "do not demonstrate the same vulnerabilities as funds that are offered publicly to a broad

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[22] The time periods used in this section provide data for the largest outflows experienced by different types of money market funds during a given two-week period. These two-week periods may be different for different types of money market funds. Outflows for prime and tax-exempt money market funds peaked on March 17, 2020 and March 23, 2020, respectively. *See* PRESIDENT'S WORKING GROUP ON FINANCIAL MARKETS, OVERVIEW OF RECENT EVENTS AND POTENTIAL REFORM OPTIONS FOR MONEY MARKET FUNDS 20 at n. 10 (2020), *available at* https://home.treasury.gov/system/files/136/PWG-MMF-report-final-Dec-2020.pdf. As discussed below, the Federal Reserve announced the Money Market Mutual Fund Liquidity Facility ("**MMLF**") for prime money market funds on March 18, 2020 and announced the extension of the MMLF to tax-exempt money market funds on March 20, 2020. Board of Governors of the Federal Reserve System, *Money Market Mutual Fund Liquidity Facility* (last updated Mar. 11, 2021), https://www.federalreserve.gov/monetarypolicy/mmlf.htm.

[23] *See* discussion *supra* Section III "The Effectiveness of Previously Enacted Reforms" for a discussion of how previously enacted reforms contributed to money market funds being more liquid, more resilient, and better equipped to handle stress.

[24] Most, but not all, tax-exempt money market funds are retail money market funds. *See* Investment Company Institute, *Money Market Fund Assets* (Apr. 8, 2021), https://ici.org/research/stats/mmf/mm_04_08_21.

[25] *See* PRESIDENT'S WORKING GROUP ON FINANCIAL MARKETS, OVERVIEW OF RECENT EVENTS AND POTENTIAL REFORM OPTIONS FOR MONEY MARKET FUNDS 14-15 (2020), *available at* https://home.treasury.gov/system/files/136/PWG-MMF-report-final-Dec-2020.pdf.

[26] *Id.* at 15. Outflows on a percentage basis were largely comparable. The definition of a "retail money market fund" was not adopted until after the global financial crisis, so data comparing retail money market funds in 2008 (before the definition was adopted) and in 2020 (after the definition was adopted) has certain limitations.

[27] Non-public institutional prime money market funds refer to those funds that are not offered to the public such as "central" funds that asset managers use for internal cash management.

[28] *See* PRESIDENT'S WORKING GROUP ON FINANCIAL MARKETS, OVERVIEW OF RECENT EVENTS AND POTENTIAL REFORM OPTIONS FOR MONEY MARKET FUNDS 14 (2020), *available at* https://home.treasury.gov/system/files/136/PWG-MMF-report-final-Dec-2020.pdf.

range of unaffiliated institutional investors."[29] As discussed earlier under "The Important Role of Money Market Funds in the Short-Term Funding Markets," differences in redemption behavior between retail and institutional prime investors have been recognized previously and should be taken into account in crafting a policy response to the events in March 2020.[30] Historically, retail prime money market funds have not suffered the same level of volatility or liquidity pressures as institutional money market funds in times of market stress because retail investors use money market funds as a longer term investment strategy for their cash and not as short-term transactional cash management vehicle.

In March 2020, government money market funds saw large inflows of over $830 billion as government money market funds became a vehicle of choice to help preserve liquidity during the liquidity crisis.[31] It is noteworthy, however, that these inflows represent flows from investors of all types, including sources other than investors moving from prime money market funds into government money market funds. Prime money market funds experienced outflows of approximately $139 billion in March 2020, leaving nearly $700 billion of the inflows into government money market funds in March 2020 attributable to flows from other sources.[32] In fact, other funds that are active in the short-term funding markets, such as ultra-short bond funds, experienced unprecedented redemptions in March 2020.[33] As recognized by the Financial Stability Board, this highlights that the market flows represent not only strategic outflows from prime money market funds, specifically, into government money market funds, but also a larger market-wide liquidity crisis and overall flight to safety.[34] This also reinforces the high regard that all types of investors have for government money market fund products and their attraction as a safe haven in times of uncertainty.

As a result of the rapid demand for liquidity, short-term markets froze and governments around the world, including the United States, implemented measures to meet the unprecedented, simultaneous liquidity demand from all types of market participants. In response to the pressures placed on short-term markets, the Federal Reserve, as a lender of last resort, instituted a number of programs for the benefit of a broad range of market participants with the shared fundamental goal of enhancing overall market functioning and credit provision to the broader economy in a time of a

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29 *Id.*
30 *See supra* note 6.
31 *See* ICI COVID-19 REPORT, supra *note* 9 at 12.
32 *See id* at 13. Mutual funds experienced outflows of approximately $348 billion in March. *Id.*
33 Randal K. Quarles, Vice Chair for Supervision and Chair of the Financial Stability Board, Speech at the Peterson Institute for International Economics, The FSB in 2021: Addressing Financial Stability Challenges in an Age of Interconnectedness, Innovation, and Change (Mar. 30, 2021), *available at* https://www.federalreserve.gov/newsevents/speech/quarles20210330a.htm. Further, weekly outflows from bond funds reached record levels of $109 billion. Financial Stability Board, "Holistic Review of the Market Turmoil" (Nov. 17, 2020), *available at* https://www.fsb.org/wp-content/uploads/P171120-2.pdf.
34 *See* FINANCIAL STABILITY BOARD, HOLISTIC REVIEW OF THE MARKET TURMOIL 21 (2020), *available at* https://www.fsb.org/wp-content/uploads/P171120-2.pdf. ("These inflows were partly attributable to a reallocation from prime [money market funds] and other short-term funding market investors, but also driven by disinvestments from other less-liquid asset classes in order to meet demand for cash. Corporates and households also increased their deposits at banks (deposits at US banks increased by around US$476 billion over the course of March.)"). When viewed in the context of not only the large inflows into government money market funds, but also the large inflows into bank and broker deposits, outflows from prime and tax-exempt money market funds comprised an even smaller small percentage of the overall flight to quality. This further reinforces how the market stresses in March 2020 were not specific to, nor caused by, prime and tax-exempt money market funds.

market-wide liquidity emergency.[35] One of these programs, the MMLF, was focused directly on money market funds.

On March 18, 2020, the Federal Reserve announced the MMLF, pursuant to which the Federal Reserve Bank of Boston made loans available to eligible financial institutions secured by high-quality assets purchased by the financial institution from money market funds and included regulatory relief on bank capital requirements in order to facilitate lending under the MMLF.[36] The MMLF did not open until March 23, 2020 and it took some time for banks to become operational with the MMLF. Outflows for prime money market funds, however, peaked on March 17, 2020 (the day the Federal Reserve announced the Commercial Paper Funding Facility) and outflows for tax-exempt money market funds peaked on March 23, 2020 (one business day after the MMLF was expanded to include tax-exempt securities).[37] The effect of the announcement of the MMLF highlights the nature of the events of March 2020 as a liquidity crisis with redemption behavior driven by concerns of liquidity and ability to access funds, rather than as a credit crisis with redemption behavior being driven by concerns about credit quality.

Although government intervention reassured and calmed the markets during this period of unprecedented stress, it is noteworthy that peak use of the MMLF was nearly three times less than the level of peak use of a similar facility created in 2008 in response to the global crisis.[38] In understanding the market events of March 2020, it is also noteworthy that money market funds are but one participant in the short-term funding markets, and the increase in the Federal Reserve's assets that were attributable to the MMLF were relatively limited when viewed holistically in comparison to the amounts other types of support that added to the Federal Reserve's balance sheet.[39] Furthermore,

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[35] The Federal Reserve, as lender of last resort, was able to successfully intervene to not only stem outflows from certain types of money market funds, but more importantly to stabilize short-term funding markets and restore the functioning of the commercial paper and certificate of deposit market. *See* DIVISION OF ECONOMIC AND RISK ANALYSIS OF THE COMMISSION, US CREDIT MARKETS: INTERCONNECTEDNESS AND THE EFFECTS OF THE COVID-19 ECONOMIC SHOCK 26 (2020), *available at* https://www.sec.gov/files/US-Credit-Markets_COVID-19_Report.pdf (also finding that Federal Reserve announcements other than the MMLF likely contributed to improvements in market conditions more broadly); *see also* Lei Li et al, *Runs and Interventions in the Time of Covid-19: Evidence from Money Funds,* CENTRE FOR ECONOMIC POLICY RESEARCH COVID ECONOMICS, Issue 29 at 50, *available at* https://cepr.org/sites/default/files/CovidEconomics29.pdf (finding that the Federal Reserve emergency interventions were effective in stemming outflows from money market funds and stabilizing the short-term funding markets, quickly restoring the functioning of commercial paper and certificate of deposit markets, consistent with the view that the lender of last resort enables financial institutions to resume the supply credit to the ultimate borrowers).

[36] Board of Governors of the Federal Reserve System, *Money Market Mutual Fund Liquidity Facility* (last updated Mar. 11, 2021), https://www.federalreserve.gov/monetarypolicy/mmlf.htm. The MMLF originally covered prime money market funds. On March 20, 2020, the Federal Reserve announced that it would extend the MMLF to tax-exempt money market funds.

[37] *See* PRESIDENT'S WORKING GROUP ON FINANCIAL MARKETS, OVERVIEW OF RECENT EVENTS AND POTENTIAL REFORM OPTIONS FOR MONEY MARKET FUNDS 12 (2020), *available at* https://home.treasury.gov/system/files/136/PWG-MMF-report-final-Dec-2020.pdf. *See also* DIVISION OF ECONOMIC AND RISK ANALYSIS OF THE COMMISSION, US CREDIT MARKETS: INTERCONNECTEDNESS AND THE EFFECTS OF THE COVID-19 ECONOMIC SHOCK 26 (2020), *available at* https://www.sec.gov/files/US-Credit-Markets_COVID-19_Report.pdf (also finding that other Federal Reserve announcements around this time likely contributed to improvements in market conditions more broadly). The worst week of the crisis for money market funds was the week ended March 18, 2020. *See* ICI COVID-19 REPORT, *supra* note 9.

[38] *See* ICI COVID-19 REPORT, *supra* note 9 at 25. While aggregate dollar use is significantly lower (and therefore the amount of taxpayer support is significantly lower), when use is scaled by outflows from prime money market funds, the use as a percentage relative to outflows from prime funds is similar in both September 2008 and March 2020.

[39] Other actions and facilities that constituted the large majority of the growth of the Federal Reserve's balance sheet included purchases of U.S. Treasuries, purchases of U.S. agency securities, support to foreign central banks through foreign currency swap agreement programs, and other facilities to provide liquidity to market participants and programs established

while the CARES Act included a provision to allow the U.S. Treasury to guarantee money market funds, a tool that had been used in 2008, the U.S. Treasury has not needed or used this authority during the COVID-19 crisis (and has not been used to date). SIFMA AMG applauds the swift and appropriate actions of the Federal Reserve in providing emergency liquidity necessary for the broader economy to continue functioning when faced with an abrupt demand for liquidity resulting from the uncertainty of the COVID-19 pandemic.

Regulators also provided relief from certain restrictions that inhibited the ability of certain sponsors to support their funds. The Federal Reserve, in conjunction with the Federal Deposit Insurance Corporation and Office of the Comptroller of the Currency, provided temporary relief from certain limits on transactions with affiliates under Section 23A of the Federal Reserve Act to allow banks to purchase assets from affiliated money market funds, subject to certain conditions.[40] Commission staff also issued temporary no-action relief to permit the purchase of money market fund securities by an affiliate where reliance on Rule 17a-9 under the 1940 Act could conflict with Section 23A and 23B of the Federal Reserve Act, subject to certain conditions.[41] SIFMA AMG applauds the swift action taken by such regulators during a market-wide liquidity crisis in order to provide valuable relief to permit certain sponsors to support money market funds and increase the functioning of the overall short-term funding markets.

Despite these unprecedented liquidity challenges, money market funds, including prime and tax-exempt money market funds, were able to provide investors with daily liquidity and meet 100% of redemptions, even as investors increased their redemption activity. No money market fund "broke the buck" or instituted a liquidity fee or redemption gate at any time in March 2020.

It is in this light that we urge regulators to examine policy measures in response to the market-wide liquidity crisis in March 2020 and urge the Commission and its staff to conduct their own comprehensive studies on the events in March 2020.[42] As noted above, money market funds are a key participant in the short-term funding markets, however, money market funds were not the root cause of the issues faced in the short-term funding markets in March 2020. Rather, money market funds, like other participants in the short-term funding markets, experienced market-wide liquidity events resulting from the COVID-19 pandemic. SIFMA AMG urges regulators to craft holistic policy measures that recognize the interconnectedness of different segments of the short-term funding market and the role that each has played in the March 2020 market stresses. As further discussed below under "Comments on the Policy Measures in the Report," policy measures directed at the regulation of money markets should be narrowly tailored to directly address the liquidity pressures experienced by

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under the Coronavirus Aid, Relief, and Economic Security ("**CARES**") Act. *See id.* at 38, Figure 3.22 (showing changes in the Federal Reserve's assets for selected periods in 2020 attributable to various actions and facilities).

[40] *See* Money Market Mutual Funds Template Letter (Mar. 17, 2020), *available at* https://www.federalreserve.gov/supervisionreg/legalinterpretations/fedreserseactint20200317.pdf.

[41] *See* Letter to Susan Olson, Investment Company Institute (March 19, 2020), *available at* https://www.sec.gov/investment/investment-company-institute-031920-17a.

[42] For example, we highlight that the Report states that while government money market funds saw significant inflows in March 2020, the prime and tax-exempt money market fund sectors faced significant outflows. The Report, however, does not provide further context into how inflows into government money market funds represent flows from investors of all types, including sources other than investors moving from prime and tax-exempt money market funds into government money market funds. The Report also does not provide context into the relatively small size of the prime and tax-exempt money market fund outflows when viewed in the context of the larger flight to quality into bank and broker deposits (in addition to government money market funds). We urge the Commission and their staff to conduct their own analysis on the events in March 2020, taking into account these larger variables necessary to understand such events and their impact.

certain money market funds in March 2020 while preserving the viability of such products for investors.

V. Comments on the Policy Measures in the Report

As an introductory matter to comments on the specific policy measures in the Report, SIFMA AMG encourages any policy measures to be tailored as narrowly as possible to directly address the limited issues faced by non-government money market funds in March 2020. Because changes to money market funds may have far-reaching, unintended consequences that are detrimental to shareholders and the broader short-term funding markets, we urge that any changes be narrowly tailored to avoid unnecessary disruption. Tailoring reform narrowly will benefit markets by easing the process of adjusting to changes, and providing a basis to evaluate the need for further actions based on the results achieved. Reforms should also be tailored in a manner to preserve the simplicity of the money market fund product and be easy to understand for investors. Overly complicated policy measures risk investor confusion and reduce the utility of the money market fund wrapper.

SIFMA AMG further urges the Commission to only pursue policy measures that directly bear on the liquidity concerns experienced in March 2020 and the specific types of funds that experienced the largest outflows, while preserving the viability of such products for investors. As discussed under "The Liquidity Crisis in March 2020," retail money market funds and non-public institutional prime money market funds did not experience the same level of outflows as publicly offered institutional prime money market funds. Policy measures should be tailored to reflect the difference in investor redemption behavior of the different types of money market funds.[43]

SIFMA AMG agrees that reform measures should exclude government money market funds. Government money market funds provide investors with a stable, attractive investment option and are widely viewed as among the safest and most liquid investment options for various types of investors. Government money market funds are currently subject to different regulations under Rule 2a-7 as compared to other types of money market funds, and the current level of regulation has proven effective in ensuring government money market funds are resilient and able to manage redemptions. As such, SIFMA AMG supports not imposing additional regulatory requirements on government money market funds.

As explained above, the market events that occurred in March 2020 were caused by a liquidity crisis and policy measures should be tailored accordingly. As such, in this section we first address liquidity-related policy measures (items (a)-(e) below), and then proceed to the other policy measures included in the Report (items (f)-(g) below).

a. Removal of the Tie Between Liquidity and Fee and Gate Thresholds

SIFMA AMG strongly supports the delinking of liquidity and thresholds for imposing liquidity fees and redemption gates. SIFMA AMG views this policy measure as the most effective means to address the specific issues that contributed to stresses on certain types of money market funds and the short-term funding markets in March 2020, and the most effective means to achieve the stated goals of

[43] *See* discussion *supra* Section IV "The Liquidity Crisis in March 2020" (highlighting different outflows among different types of money market funds and agreeing with the finding in the Report that outflows experienced by non-public institutional prime money market funds show that such funds "do not demonstrate the same vulnerabilities as funds that are offered publicly to a broad range of unaffiliated institutional investors").

money market fund reform. SIFMA AMG therefore views this policy measure as an essential element of any money market fund reform.

As noted earlier under "The Effectiveness of Previously Enacted Reforms," linking the ability to impose liquidity fees and redemption gates to a specified level of weekly liquid assets that is publicly available created an unintended consequence of incentivizing institutional investors to redeem as a fund's liquidity approached the threshold at which a liquidity fee or redemption gate could be imposed which would restrict their ability to access cash. The 30% weekly liquid asset threshold, in turn, resulted in money market funds selling fewer liquid assets to meet redemptions in March 2020, as money market funds feared a decrease in weekly liquid assets would accelerate redemption behavior. This exacerbated liquidity pressures. Requirements to maintain a minimum level of weekly liquid assets do not serve their intended purpose if money market funds are not willing or able to use liquidity buffers in times of stress. Accordingly, delinking liquidity and thresholds for imposing a liquidity fee or redemption gate is a vital part of effectively addressing an unintended consequence that resulted from the implementation of the 2014 reforms to Rule 2a-7 that may have contributed to stress in the short-term funding markets in March 2020. Improving the usability of liquidity buffers, as this policy measure will do, will better equip money market funds to manage through times of stress and will therefore help improve the resilience and functioning of the short-term funding markets. Moreover, by removing one element that increased redemption behavior in March 2020, this policy measure helps reduce the likelihood that official sector interventions would be needed to halt redemptions.

This policy measure as presented in the Report still would maintain liquidity fees and redemption gates as a tool for money market funds to use to help slow redemptions, but would instead be subject to a determination by the money market fund's board of trustees/directors that the imposition of such a liquidity fee or redemption gate was in the best interests of the fund, without that determination being tied to a specified level of liquidity. As such, the utility and protections provided by liquidity fees and redemption gates would remain available to money market funds; however, the aspects of such liquidity fees and redemption gates that contributed to liquidity pressures on some money market funds would be removed.

While institutional prime money market funds came under the most pressure during the market stresses in March 2020 as compared to other types of money market funds, SIFMA AMG supports applying the delinking policy measure to all types of money market funds that are currently subject to liquidity fees and redemption gates. The dynamics that motivate redemptions in the face of a bright line liquidity threshold that is tied to a liquidity fee or redemption gate apply regardless of the type of money market fund. Further, creating a consistent framework for all types of money market funds subject to liquidity fees and redemption gates as to when such liquidity fees and redemption gates may be imposed may also alleviate the potential for investor confusion.

The Report notes that the policy measure to delink liquidity with thresholds for liquidity fees and redemption gates addresses one focal point that may have triggered redemptions, but does not otherwise mitigate run incentives. In this regard, SIFMA AMG would like to highlight the earlier discussion in "The Liquidity Crisis in March 2020" noting the inflows to government money market funds were largely from products other than prime money market funds in the face of an unprecedented liquidity crisis. This highlights that redemptions faced by institutional prime money market funds were part of a larger liquidity crisis in the overall short-term funding market, and SIFMA AMG encourages any policy response to employ a holistic approach in addressing these matters, including matters that may have contributed overall to a flight to safety in government money market funds.

The Report also notes that if money market funds maintain fewer liquid assets as a result of this policy measure, then money market funds may be less equipped to manage significant redemptions without engaging in fire sales. Given the requirement to post levels of weekly liquid assets on a fund's website on a daily basis, coupled with the fact that liquidity is of primary importance to money market fund investors (particularly institutional investors), it is not expected that in normal market conditions money market funds would be managed significantly closer to 30% weekly liquid assets in the absence of a tie between 30% weekly liquid assets and liquidity fees and redemption gates. In fact, from 2010 to 2013 (prior to the adoption of liquidity fees and redemption gates), weekly liquid assets for institutional prime money market funds averaged approximately 42% of such funds' assets, which is significantly higher than the 30% minimum weekly liquid assets threshold (as a percentage of their portfolios).[44] This shows that even without the possibility of implementing a liquidity fee or redemption gate, money market funds are operated conservatively in order to be equipped to manage redemptions through times of stress. Increased shareholder transparency through daily website reporting, as currently required under Rule 2a-7, further incentivizes conservative liquidity management of money market funds.

To the extent liquidity levels remain a concern of the Commission in considering this policy measure, SIFMA AMG encourages exploration of measures, other than liquidity fees and redemption gates, that could be imposed in a manner that does not motivate increased redemption behavior if a fund's level of weekly liquid assets decreases below 30%. For example, increased board reporting, requiring a fund to overcorrect (e.g., increase its level of weekly liquid assets to a specified percentage above 30%, such as 35%), or prohibiting additional purchases of any non-overnight instruments until the minimum level of weekly liquid assets is reestablished. SIFMA AMG cautions against imposing requirements that would add undue burden to a money market fund and its adviser during a time of stress.

For the reasons discussed above, SIFMA AMG views the delinking of liquidity and thresholds for liquidity fees and redemption gates as the policy measure presented in the Report that has the strongest direct correlation to the cause of stresses experienced by certain types of money market funds in March 2020 and therefore the policy measure that most meaningfully addresses, in a practical manner, the issues that contributed to stresses on certain types of money market funds and the short-term funding markets. SIFMA AMG believes delinking liquidity and thresholds for imposing liquidity fees and redemption gates is the most effective way to achieve the goals of money market fund reform

[44] *See* ICI COVID-19 REPORT, *supra* note 9 at note 59. Since 2010, prime money market funds' weekly liquid assets (as a percentage of their portfolios) have exceeded the 30 percent minimum on average by 12 to 15 percentage points. From 2014 to 2019 (excluding the period June 2016 to May 2017), weekly liquid assets for institutional prime money market funds averaged 44% of their assets. The comparable figures for retail prime money market funds were 39% from 2010 to 2013, and 42% from 2014 to 2019 (excluding the period from June 2016 to May 2017). Results exclude the period from June 2016 through May 2017 as such period reflects prime funds transitioning their portfolios ahead of the Commission's October 2016 deadline for institutional prime money market funds to float their net asset values. *See id.* The change in the regulatory structure to provide money market funds with the ability to impose liquidity fees and redemption gates resulted in only a 2% to 3% increase in weekly liquid assets, on average, depending on type of prime money market fund. This further highlights that motivations to manage money market funds above the minimum 30% weekly liquid asset requirement exist outside of the ability to impose liquidity fees and redemption gates.

and therefore an essential element of any money market fund reform, and that additional reforms (if any) should be paired with this policy measure for the most effective outcome.

b. Countercyclical Weekly Liquid Asset Requirements

While SIFMA AMG does not oppose countercyclical weekly liquid asset requirements in principle, many of our members view this policy measure overall as a less effective means to achieve similar goals as delinking liquidity and liquidity fees and redemption gates that presents significant implementation challenges. SIFMA AMG therefore supports the delinking of liquidity and liquidity fees and redemption gates over countercyclical weekly liquid asset requirements. Should the Commission delink liquidity and the imposition of liquidity fees and redemption gates, many of the benefits of countercyclical liquidity asset requirements will be realized and many of the goals of money market fund reform would have been achieved in a more effective manner than through a countercyclical policy measure. Both policy measures would reduce the salience of the liquidity threshold to diminish the incentive for increased outflows and improve the usability of weekly liquid asset buffers, however, countercyclical weekly liquidity asset requirements could be less effective in doing so by still maintaining the potential for a bright line threshold that could incentivize redemptions and by introducing additional unnecessary complexities as compared to the delinking of liquidity and liquidity fees and redemption gates. Any externalized trigger for liquidity fees and redemption gates, even with countercyclical adjustments, has the potential to incentivize redemption behavior.

The delinking of liquidity with thresholds for liquidity fees and redemption gates mitigates the drawback noted in the Report related to countercyclical weekly liquid asset requirements that threshold effects may still motivate investors to redeem by removing the threshold liquidity requirements to impose a liquidity fee or redemption gate. Maintaining a threshold at which liquidity fees or redemption gates could be imposed, but shifting that threshold through countercyclical weekly liquid asset requirements, has the potential to exchange one red flag for another and mitigate the usefulness of countercyclical weekly liquid asset requirements. The events of March 2020 show that investors, particularly institutional investors, are incredibly information sensitive and news driven. As weekly liquid asset levels dropped closer to 30% (the threshold at which a board could impose a liquidity fee or redemption gate), institutional investors quickly reacted to this information and increased their redemption activity. Many of our members have expressed concern that it is likely that institutional investors will react to other types of information that may trigger countercyclical requirements and such triggers may therefore increase redemption behavior in a similar manner as was seen in March 2020 when weekly liquid asset levels reached the threshold at which a board could impose a liquidity fee or redemption gate.

As noted earlier under "Removal of the Tie Between Liquidity and Fee and Gate Thresholds," SIFMA AMG is supportive of the exploration of other types of measures that could be imposed if a fund's level of weekly liquid assets decreases below a specified level in a manner that does not motivate increased redemption behavior. For example, additional board reporting, requiring overcorrections, or prohibiting additional purchases of any non-overnight instruments until the minimum level of weekly liquid assets is reestablished. SIFMA AMG cautions against imposing requirements that would add undue burden to a money market fund and its adviser during a time of stress.

To the extent the Commission does consider countercyclical weekly liquid asset requirements, SIFMA AMG urges the Commission to further consider how the Commission could construct a countercyclical requirement that would apply on an automatic basis, versus requiring Commission action. Requiring Commission action would slow the implementation of any countercyclical weekly liquid asset requirement, presumably in a time of stress, thereby reducing the utility of the countercyclical weekly asset requirement. Further, many of our members have expressed concern that Commission action could send a heightened negative signal to investors and cause increased redemptions. SIFMA AMG also urges the Commission to consider constructing this policy measure to apply on a market-wide basis, versus per fund. If applied on a market-wide basis, the countercyclical weekly liquid asset requirement could be employed on a less disruptive basis than singling out one fund in particular, which could contribute to stress on that particular fund. We note, however, the difficulty of obtaining information that may be necessary to implement or oversee the trigger of a countercyclical weekly liquid asset requirement and again highlight the additional benefits of delinking liquidity with liquidity fees and gates insofar as delinking does not present the additional complexities associated with implementing or calibrating countercyclical weekly liquid requirements and would therefore more effectively achieve the goals of such policy measures. Should the Commission consider countercyclical weekly liquid asset requirements, SIFMA AMG urges the Commission to consider such policy measure only as part of a larger reform package that also includes delinking liquidity and liquidity fees and redemption gates.

c. Liquidity Management Changes

While in principle SIFMA AMG does not generally oppose certain liquidity management changes, many of our members believe such changes will be less effective than the delinking of liquidity and fees and gates in addressing the specific issues presented in March 2020 and achieving the overall goals of money market fund reform. To the extent the Commission considers liquidity management changes, including changes such as a higher weekly liquid asset minimum, SIFMA AMG believes any such changes should be focused on the types of money market funds that experienced higher redemptions in March 2020 as part of a reform package that includes the delinking of liquidity with liquidity fees and redemption gates.[45] SIFMA AMG strongly opposes automatic financial or punitive measures in connection with the liquidity management changes presented in the Report.

As noted above, increased redemption behavior in March 2020 was driven by fear that a liquidity fee or redemption gate would be imposed as a money market fund's weekly liquid assets dropped to 30% and investors would be unable to access liquidity. Redemption behavior was not driven by fears that 30% of a money market fund's portfolio in weekly liquid assets was too low a level of liquidity for a money market fund. Imposing a higher minimum level of weekly liquid assets is addressing an issue that did not cause or contribute to stresses experienced in March 2020 and many of our members generally view any increase as unlikely to materially impact such stresses.

Imposing a higher weekly liquid asset minimum could have negative unintended consequences for money market funds subject to the higher minimum. For example, imposing a higher minimum level of weekly liquid assets could decrease money market fund yields and reduce the spread between prime and government money market funds. These consequences could then, in turn, shrink the size of the money market funds subject to such higher weekly liquid asset minimum by decreasing investor demand for such products. This could then increase the cost of funding to issuers.[46] We urge the

[45] *See supra* note 4.
[46] *See* discussion *supra* Section II "The Important Role of Money Market Funds in the Short-Term Funding Markets" for a more comprehensive discussion of the potential consequences of reducing the size of the prime money market fund industry.

Commission to consider these consequences in considering whether to propose liquidity management changes for money market funds.

SIFMA AMG further highlights that, as discussed above, money market funds already manage their portfolios significantly above the 30% weekly liquid asset minimum in normal market conditions.[47] This is true even before requirements related to liquidity fees and redemption gates were imposed and, therefore, even if liquidity levels are delinked from requirements related to liquidity fees and redemption gates, it is not expected that money market funds would manage significantly closer to the minimum level of weekly liquid assets.[48] To the extent the Commission does consider imposing a higher minimum for weekly liquid assets, SIFMA AMG encourages the Commission to consider that money market funds typically manage their funds' liquidity at a significantly higher level than any required minimum and therefore imposing a higher minimum as a practical matter would result in a de facto even higher minimum than actually required as a regulatory matter.[49] Accordingly, should the Commission propose higher weekly liquid asset minimums, our members generally urge the Commission to take an incremental approach in determining any higher weekly liquid asset minimum given managers are likely to manage their funds' liquidity significantly higher than any required minimum and any significant increase could impact the nature and usefulness of the product and reduce investor interest in such funds.

To the extent the Commission explores imposing a higher weekly liquid asset minimum, SIFMA AMG believes it is appropriate to narrowly tailor such requirements to those types of money market funds that experienced the heaviest outflows in March 2020 and to exclude other types of money market funds from such requirements. As discussed under "The Liquidity Crisis of March 2020," public institutional prime money market funds experienced the largest redemptions as compared to other money market funds. This pattern of investor redemption behavior is consistent with patterns during prior periods of market stress. SIFMA AMG believes narrowly tailoring reform measures to address only those types of money market funds that experienced heavier outflows in March 2020 is the most appropriate and effective manner to approach money market fund reform.

Among the liquidity management changes presented in the Report, the Report presents a policy measure to impose an additional weekly liquid asset threshold of 40% with penalties if weekly liquid assets fall below 40%. While SIFMA AMG does not oppose additional weekly liquid asset thresholds, SIFMA AMG strongly opposes any policy measure that would impose a financial or punitive penalty on the fund adviser or sponsor should weekly liquid assets fall below a specified level. Such a penalty is inconsistent with the approach taken in other provisions of the 1940 Act, and we are not aware of any other provision in the 1940 Act in which the Commission automatically imposes a direct and immediate fine or other penalty on a mutual fund or its adviser (particularly without providing a fund or its adviser the benefit of any processes and proceedings related to the violation and subsequent penalty). Such penalties are not responsive to, and therefore ineffective in addressing, the issues

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[47] *See supra* note 44 and accompanying text.
[48] *See id.*
[49] For example, since 2010, prime money market funds' weekly liquid assets (as a percentage of their portfolios) have exceeded the 30 percent minimum on average by 12 to 15 percentage points. From 2010 to 2013 (prior to the adoption of liquidity fees and redemption gates), weekly liquid assets for institutional prime money market funds and retail prime money market funds averaged approximately 42% and 39% of such funds' assets, respectively, which is significantly higher than the 30% minimum weekly liquid assets threshold (as a percentage of their portfolios) *See* ICI COVID-19 REPORT, *supra* note 9. Should the Commission impose a requirement to maintain a minimum level of 40% of weekly liquid assets, it can be expected that the funds subject to such minimum would likely manage a similar amount higher than any minimum weekly liquid asset requirement.

experienced by money market funds in managing through the market-wide liquidity crisis in March 2020 and would create fiduciary duty and conflict of interest issues for advisers that are untenable as advisers would be forced to balance the use of weekly liquid assets to manage redemptions against the potential financial penalty for doing so. Essentially, any sale of an asset at less than par would become a conflicted trade and second guessed. Consistent with the overarching principles of the 1940 Act, the Commission should seek to avoid creating conflicts of interest in crafting any policy measure.

As noted above, money market funds already manage their portfolios significantly above the 30% weekly liquid asset minimum in normal market conditions without the imposition of any financial or punitive penalty.[50] The imposition of such penalties would be trying to solve a problem that simply does not exist. Further, Rule 2a-7 already provides for a mechanism to address instances when a fund's weekly liquid assets fall below 30% (prohibiting a fund from acquiring any asset other than a weekly liquid asset until weekly liquid assets increase above 30%). SIFMA AMG believes this correction process is the more appropriate and effective manner in which to address a decline in weekly liquid assets. Other measures that could be imposed should a money market fund's weekly liquid assets drop below a specified minimum include additional board reporting, requiring a fund to overcorrect (e.g., increase its level of weekly liquid assets to a specified percentage above 30%, such as 35%), or prohibiting additional purchases of any non-overnight instruments until the minimum level of weekly liquid assets is reestablished.[51] The Commission should carefully consider (and avoid) the potential for negative unintended consequences in connection with this policy measure. For example, these types of penalties may reduce the usability of liquidity buffers as funds may be less willing to sell weekly liquid assets in times of stress to avoid a financial penalty.

The Report also presents an additional category for assets with slightly longer maturities (e.g., biweekly liquid assets). SIFMA AMG encourages further exploration of whether a market exists for an additional biweekly liquid asset category (e.g., whether banks will underwrite assets with such maturities). SIFMA AMG also highlights the potential for such additional category to overly complicate the framework of Rule 2a-7 without additional benefit, and notes the earlier discussion encouraging policy measures that are simple to understand and implement. Further, the Report highlights that this policy measure is intended to address "barbell" strategies, where a fund offsets short-term assets with risker longer-term assets that enhance returns but increase the risk of portfolios. SIFMA AMG encourages further exploration of whether these strategies in fact occurred during March 2020 and caused stresses in March 2020.

d. Reforms of Conditions for Imposing Redemption Gates

While SIFMA AMG does not generally oppose certain reforms of conditions for imposing redemption gates, SIFMA AMG believes these measures will be less effective than the delinking of liquidity and fees and gates in addressing the specific issues presented in March 2020 and achieving the overall goals of money market fund reform.

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[50] *See supra* note 44 and accompanying text.

[51] Unlike imposing financial or punitive penalties upon a drop in weekly liquid assets, these types of measures are consistent with other provisions of the 1940 Act. For example, under new Rule 18f-4, if a fund is out of compliance with the applicable value at risk test for more than five business days, then certain board reporting is required. 17 C.F.R. § 270.18f-4(c)(2)(iii) (2021). In considering any additional reporting, however, SIFMA AMG cautions against imposing requirements that would add undue burden to a money market fund and its adviser during a time of stress.

The Report sets forth various reform options related to imposing redemption gates, including (1) requiring money market funds to obtain permission from the Commission or notify the Commission prior to imposing gates, (2) requiring boards to consider liquidity fees before gates, (3) lowering the weekly liquid asset threshold at which gates could be imposed (for example, 10%), and (4) implementing "soft" or "partial" gates (allowing a pro rata portion of every redemption in a given day to be redeemed while causing a portion to be gated). Requiring money market funds to obtain permission from the Commission or notify the Commission prior to imposing gates is unlikely to address the issues that occurred in March 2020. Steps that impose additional time between the determination of imposing a redemption gate and the actual implementation of such gate reduce the utility of the redemption gate, especially in a time of market stress, and are therefore unlikely to increase the resiliency of the short-term funding markets. Investors' adversity to redemption gates that drove increased redemption behavior as funds approached 30% of weekly liquid assets is rooted in a concern of liquidity and inability of being able to readily access funds. Requiring advance notice to the Commission, or permission from the Commission, does not remedy investors' concerns and is therefore unlikely to address the contributors to stresses in the market such as those experienced in March 2020. Further, under current regulatory requirements, a money market fund would supplement its prospectus through a filing with the Commission in order to notify shareholders of the imposition of a redemption gate, file on Form N-CR within one business day of imposing a redemption gate, and post on its website information required to be filed with the Commission on Form N-CR on the same business day as the Form N-CR filing. As such, while the Commission may not be notified in advance of the redemption gate, the Commission is still notified in a timely manner (through filings with the Commission) of the imposition of a redemption gate.

Conversely, lowering the weekly liquid asset threshold for considering a redemption gate (either full or partial) would enable a money market fund to use its liquidity buffer in a more meaningful way. As noted earlier, although money market funds maintained liquidity buffers entering the market stresses in March 2020, many money market funds did not employ those buffers out of fear that as weekly liquid assets reached closer to 30% investors would increase redemption activity to avoid a liquidity fee or redemption gate. Requirements to maintain a minimum level of weekly liquid assets do not serve their intended purpose if funds are not willing to use liquidity buffers in times of stress. In considering the redemption behavior in March 2020, allowing a money market fund to use 20% of the weekly liquid asset buffer while leaving the 10% level as the threshold at which the board may consider a gate merits further consideration. Because this still maintains the dynamic of a bright line threshold that may increase redemption behavior, however, SIFMA AMG maintains that delinking liquidity and thresholds for liquidity fees and redemption gates is the most essential element of any money market fund reform.

With respect to "soft" or "partial" redemption gates, SIFMA AMG highlights the complex accounting and administrative challenges this measure presents, and the costs with such challenges that would be borne by money market funds (and ultimately shareholders) in implementing "soft" or "partial" redemption gates. In this regard, SIFMA AMG also notes that "soft" or "partial" redemption gates would pose costs and burdens not only for sponsors, but also for intermediaries who would need to police "soft" or "partial" redemption gates. As such, SIFMA AMG encourages further exploration of the impact of this policy measure on all stakeholders, including the downstream impact on intermediaries, should this policy measure be further considered.

e. Swing Pricing

SIFMA AMG does not support swing pricing for money market funds as it will not address any of the overarching goals for reform stated in the Report. Further, swing pricing is not necessary for money market funds and would not result in the same benefits, or address the same issues, that swing pricing addresses in other open-end funds due to differences in how money market funds handle redemptions as compared to other open-end funds.

As explained in the Report, swing pricing adjusts a fund's net asset value downward when net redemptions exceed a threshold to pass to redeeming shareholders certain transaction costs associated with their trading activity. Many of the reasons that swing pricing may benefit other mutual funds in managing liquidity risks are less applicable to money market funds. While a bond fund may be likely to have to sell bonds to meet redemption requests, money market funds frequently handle large redemptions and typically know when to expect to such redemptions.[52] As such, money market funds typically let securities mature to meet redemptions and therefore do not incur transaction costs as bond funds do in meeting redemptions (or incur transaction costs at a much lower rate). The level of transaction costs associated with money market fund trading is much lower than transaction costs of other mutual fund trading due to the types of securities in which money market funds invest such that any swing factor is likely to be too small to achieve the stated goals of this policy measure. Based on this, the reasons and benefits for implementing swing pricing simply do not make sense for money market funds and swing pricing is therefore unlikely to address any liquidity issue that arose in March 2020. To our knowledge, swing pricing has not been tested to show that it would be helpful for money market funds given the small pricing differentials in the securities held by money market funds.

Further, a money market fund is permitted to impose a liquidity fee on redemptions in certain circumstances, and these fees serve a similar purpose as the net asset value adjustments contemplated by swing pricing by allocating at least some of the costs of providing liquidity to redeeming rather than non-transacting shareholders. These liquidity fees would also generate additional liquidity to meet redemption requests. The purpose served by liquidity fees would not be diminished even if liquidity fees are delinked from requirements related to weekly liquid asset levels. Accordingly, money market funds have tools at their disposal to accomplish similar goals as swing pricing, but such tools are fashioned in a manner that reflects the unique manner in which money market funds operate in order to still permit money market funds to provide same day liquidity.

Many money market fund investors (primarily, but not exclusively, institutional investors) use intraday and same-day settlement to move money in and out of their accounts intraday for a variety of time-sensitive business and personal transactions. This is considered a critical feature of money market funds for such investors. Same-day settlement transactions are those where the order (either buy or sell) is sent to the money market fund and the money settlement, for both purchases and redemptions, also occurs on the same day on which the money is sent for the order. Thus, the entire settlement process is completed on the same day. Swing pricing would effectively eliminate intraday settlement due to operational and timing issues, as implementing swing pricing would require net flow information at the end of the day (which would not be available for intraday movements). Same-day settlement transactions are also subject to operational timing issues and imposing a swing pricing

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[52] In fact, money market funds maintain "Know Your Customer" procedures under Rule 38a-1 of the 1940 Act to consider investor characteristics and their likely redemption behavior. *See* Money Market Fund Reform, Investment Company Act Release 29132 (Feb. 23, 2010) at 53, *available at* https://www.sec.gov/rules/final/2010/ic-29132.pdf.

requirement could significantly impair a money market fund's ability to provide same day liquidity. These concerns may be more complex for money market funds used as sweep accounts.

Additionally, unlike other open-end mutual funds, certain money market funds strike their net asset value multiple times a day. This presents additional challenges in implementing swing pricing. The other operational and implementation challenges generally applicable to other open-end mutual funds related to swing pricing are also applicable to money market funds. As noted in the Report, eligible U.S. mutual funds have yet to implement swing pricing largely because implementation would require substantial reconfiguration of current distribution and order-processing practices. Money market funds provide no exception to these challenges.

f. Bank-Like Policy Measures: MBR, Capital Buffer Requirements, LEB Membership, New Requirements Governing Sponsor Support

SIFMA AMG strongly opposes bank-like policy measures such as MBR requirements, capital buffer requirements, LEB membership, and mandating sponsor support. SIFMA highlights the role of the Commission as the primary regulator of money market funds and urges the Commission to advance market-driven regulatory solutions rather than bank-driven measures.

As explained under "The Liquidity Crisis in 2020," the market events of March 2020 were in response to a liquidity crisis, rather than a credit crisis. Accordingly, the response to the events of March 2020 should be tailored to address liquidity concerns. The Report sets forth various bank-like policy measures, including MBR, capital buffer requirements, LEB membership, and new requirements governing sponsor support, that are responsive to a credit crisis rather than a liquidity crisis. In this regard, these types of policy measures will not effectively address contributors to stress in the short-term funding markets in March 2020. For example, capital at banks does not prevent or stop bank runs. Rather, what prevents runs or mass shareholder redemptions is a high level of liquidity, and holding liquid assets in portfolio in order to meet redemptions increases liquidity (as money market funds currently do).[53] Policy measures listed in subsections (a)-(e) of this comment letter relate to a fund's liquidity. Bank-like policy measures that impose capital requirements, however, do not increase liquidity and do not achieve the stated goals for reform.

Moreover, each of these policy measures would have the effect of altering the liquidity profile of prime and tax-exempt money market funds in such a way that these products will no longer exist in a manner that is attractive to investors or would impose significant costs on sponsors — each of these outcomes would cause the size of the prime and tax-exempt money market fund industry to decrease significantly or cease to exist.[54] In this regard, we highlight the discussion under "The Important Role of Money Market Funds" and remind the Commission of the important role that money market funds, particularly prime and tax-exempt money market funds, play in the short-term funding markets.[55] Our members believe that asset management firms would be unable to provide the capital needed to

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[53] As explained under "Removal of the Tie Between Liquidity and Fee and Gate Thresholds," delinking liquidity with thresholds for imposing a liquidity fee or redemption gate would further improve the usability of liquid assets to meet redemptions. This would more effectively address the liquidity pressures experienced by certain types of money market funds in March 2020 as compared to imposing bank-like requirements.

[54] *See e.g.,* Craig M. Lewis, "The Economic Implications of Money Market Fund Capital Buffers," (Nov. 2013), *available at* https://www.sec.gov/files/rsfi-wp2014-01.pdf ("The analysis shows that, after compensating capital buffer investors for absorbing credit risk, the returns available to money market fund shareholders are comparable to default free securities, which would significantly reduce the utility of the product to investors").

[55] *See e.g., supra* note 10.

support money market funds on a comparable scale to bank regulatory capital. The cost of the firm's holding capital on a bank-like scale would either be borne by fund shareholders (who would bear higher fees and/or lower returns, making investments in these funds less attractive), or by management firms who would likely elect to exit the money market fund business. If the level of required capital cannot be sustained by the marketplace, the result of a capital requirement would be to severely curtail the availability of money market funds, eliminating an attractive cash management option for investors and eliminating a source of financing for issuers.

If investors reject reformed money market funds, a significant portion of redemptions from money market funds would most likely be deposited at banks. There would be capital implications for these additional deposits, which could increase systemic risk. It is also uncertain whether all banks could provide the requisite financing to issuers on the scale currently available through money market funds, and the cost of financing to issuers is likely to increase. As discussed earlier, policy responses that eliminate or shrink the prime or tax-exempt money market fund market may drive money into other types of cash pools that are less regulated, to markets that are outside U.S. regulatory oversight, or to products that otherwise introduce increased investment risk. This would increase risks to shareholders and to the U.S. financial markets.[56]

Any significant reduction in that source of financing or increase in its cost could significantly affect governments, bank and non-bank issuers and municipalities. In particular, as discussed above, money market funds are a significant source of short-term financing for the U.S. Treasury and Government Sponsored Enterprises (GSEs) as well as state and local governments and non-profit organizations, such as universities and hospitals.[57] Ultimately, increased borrowing costs are likely to be passed through to U.S. and municipal taxpayers and consumers, with potential negative consequences on the U.S. and broader global economies. Accordingly, policy measures that serve to significantly decrease or eliminate the prime and tax-exempt money market fund industry will not improve the resilience and functioning of short-term funding markets. In fact, such policy measures will significantly harm the resilience and functioning of short-term funding markets and undermine the overarching goals of increased resilience of money market funds and the short-term funding markets.

Further, bank-like capital requirements are inappropriate for money market funds. Unlike banks, money market funds do not use leverage or hold non-transparent assets, and they do not have operating assets, use off-balance sheet financing or have deposit insurance. It is for these reasons that banks have capital buffers that are structured to shield the Federal Deposit Insurance Corporation, depositors and other creditors. Investors in money market funds are shareholders, not creditors. They are subject to potential loss, in return for a market return on their short-term investments, and this fact is clearly disclosed in money market funds' offering documents.[58] Pursuant to Rule 2a-7, money market funds must limit their investments to short-term assets and maintain specified liquidity levels, which allow the funds to avoid certain issues experienced by banks and to meet redemptions in most situations, thereby addressing the issue of potential runs more effectively than capital requirements

[56] *See* discussion *supra* Section II "The Important Role of Money Market Funds in the Short-Term Funding Markets."
[57] *See supra* note 10.
[58] Item 4(b) of Form N-1A requires disclosure that states:

> You could lose money by investing in the Fund…An investment in the Fund is not insured or guaranteed by the Federal Deposit Insurance Corporation or any other government agency. The Fund's sponsor has no legal obligation to provide financial support to the Fund, and you should not expect that the sponsor will provide financial support to the Fund at any time.

could.

Additionally, bank-like requirements encourage a false notion that money market funds are more like bank deposits than investments, thereby increasing moral hazard from the investor perspective. For example, if investors view invested principal as either insured or protected, investors may seek funds with the highest yields without consideration of the funds' risk profile. In short, bank-like policy measures are impractical, and we expect that they would be unattractive to investors, fund sponsors and intermediaries.

In addition to the significant issues noted above, each bank-like proposal presents its own individual additional challenges which are discussed below. Further, in adopting the 2014 amendments to Rule 2a-7, the Commission already considered capital buffers, MBR requirements, and LEB membership and determined such measures were not the best approach in achieving regulatory goals. The reasons the Commission did not adopt capital buffer, MBR, and LEB requirements in 2014 apply equally today, if not to a greater extent given that the use of such measures is not responsive to the specific liquidity issues that occurred in March 2020 and therefore would not effectively address any such issues.

- MBR

Implementing MBR requirements present significant challenges with respect to transparency and complexity. The disclosure necessary to inform shareholders about the structure and ever-changing size of the MBR would be cumbersome and complex. It is unlikely that investors will be able to understand how an MBR functions. This type of policy measure introduces undue complexity to an otherwise simple product.

The complex hierarchy of share subordination under the MBR arrangement gives rise to a fundamental flaw: the arrangement punishes shareholders for exercising their right to redeem their shares. It is fundamentally unfair, and at odds with the investor protection afforded under the 1940 Act to penalize shareholders for exercising their right to access their funds.

The Report highlights that an MBR mechanism could be used in a floating net asset value fund only under certain rare circumstances, such as when the fund suffers a large drop in net asset value or is closed. In this regard, we note the existence of Rule 22e-3 under the 1940 that provides an exemption from Section 22(e) of the 1940 Act (suspension of the right of redemption or postponement of date of payment) for money market fund liquidations in certain circumstances when the fund's board has irrevocably approved its liquidation.[59] Rule 22e-3 is intended to reduce the vulnerability of investors to the harmful effects of a run on the fund, and minimize the potential for disruption to the securities markets.[60] Rule 22e-3 provides money market funds options to address a run on a fund in certain rare circumstances in a manner that is better suited to address the overarching goal of money market fund resilience than the MBR policy measure presented in the Report.

Importantly, our members expect that shareholders will object to the delayed availability of a portion of their accounts. The MBR creates uncertainty as to available account balances, which would impede the use of money market funds to fund day-to-day operations. As noted above, same-day liquidity is of primary importance to many investors. Brokers expect that many clients will urge brokers

[59] 17 C.F.R. § 270.22e-3 (2021).
[60] *See* 2014 Adopting Release, *supra* note 6 at 113.

to make available the delayed portion from other sources. Brokers may be in a position to accommodate this request from certain clients, but not others, depending on the client's other available balances and other factors. This possible differing treatment among clients is another drawback of the MBR arrangement.

Further, the technological impediments to the MBR are significant. Given the tremendous negative investor impacts of the MBR, our members expect a vast reduction in total money market fund assets if the MBR is adopted, at the same time that intermediaries and funds would need to make extensive and burdensome changes to myriad systems to implement the MBR. Accordingly, we expect that intermediaries will be unwilling to bear the costs of implementation. We expect that the cost ultimately will be passed along to shareholders. Moreover, the MBR framework also presents implementation challenges not only for fund sponsors, but also for intermediaries that establish omnibus accounts for underlying investors in money market funds. Because shares may be held in omnibus accounts, the allocation of shares and trades across underlying investors is not always available to the money market fund. Accordingly, the responsibility of implementing the MBR requirement would fall on the intermediary rather than the money market fund.

SIFMA AMG further agrees with the extensive potential drawbacks, limitations, and challenges listed in the Report, including implementation and administration challenges for funds, intermediaries, and service providers; state law limitations; unequal effects on investors in stable versus floating net asset value money market funds; investor discomfort and confusion; and issues in calibrating the appropriate size of the MBR.

In previously considering MBR requirements, the Commission expressed concern that the contingent nature of the way losses are distributed among shareholders would force early redeeming shareholders to bear the losses they are trying to avoid. The Commission also noted that an MBR requirement may cause investors who value liquidity in money market funds to shift their investments to other short-term investments with fewer restrictions on redemptions and higher yields and that "a reduction in the demand of money market instruments may have an impact on the ability of financial institutions to issue commercial paper." Further, the Commission highlighted the complexities that an MBR would introduce for what has otherwise been a relatively simple product, and that implementing an MBR could involve significant operational costs (including changes to systems and amendments to governing documents (which could require shareholder approval)). The Commission concluded that:

> [W]e continue to believe that overall, the complexity of an MBR may be more costly for unsophisticated investors because they may not fully appreciate the implications. In addition, money market funds and their intermediaries (and money market fund shareholders that have in place cash management systems) could incur potentially significant operational costs to modify their systems to reflect a MBR requirement. We believe that an MBR coupled with a [net asset value] buffer would turn money market funds into a more complex instrument whose valuation may become more difficult for investors to understand.[61]

As noted above, these conclusions and concerns apply equally today, if not to a greater degree.

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[61] *See* 2014 Adopting Release, *supra* note 6 at 687.

- Capital Buffers

Capital buffers present significant issues with respect to shareholder transparency. Were the capital buffer drawn on, disclosing that the capital buffer has been drawn upon would risk a run by causing investor alarm, similar to how redemption behavior increased when a fund's level of weekly liquid assets decreased closer to 30%. Rather than acting as a safety net and preventing a run, capital buffer deployment will produce the unintended consequence of triggering investor fear and therefore a run. Not disclosing that the capital buffer had been drawn on, however, would seemingly go against the transparency generally provided under Rule 2a-7.

SIFMA AMG further agrees with the extensive potential drawbacks, limitations, and challenges listed in the Report, including administrative difficulties, costs related to financing, issues in building adequate capital buffers, and challenges in determining the appropriate size of the capital buffer.

In adopting the 2014 amendments to Rule 2a-7, the Commission recognized significant drawbacks with respect to requiring money market funds to maintain capital buffers. Specifically, the Commission recognized the significant costs to implement capital buffers (including opportunity costs that the Commission was unable to estimate), that buffers do not protect shareholders completely from the possibility of heightened rapid redemption activity during periods of market stress, and that shareholders have an incentive to redeem shares quickly as the buffer becomes impaired and rapid redemptions could impair a fund's business model and viability. The Commission also noted that buffers may cause funds to avoid holding risker short-term debt securities and instead hold low yielding investments that may not be consistent with investor preference and would reduce the utility of the product to investors and negatively impact capital formation. The Commission highlighted that capital buffers may negatively impact capital formation through investors moving their funds to alternative investment vehicles and managers' reducing holdings in commercial paper and municipal securities, which, the Commission specifically reported, could cause an "effect on the short-term financing markets if the decrease in demand for short-term securities from money market funds results in an increase in the cost of capital for issuers of commercial paper and other securities." Accordingly, the Commission did not adopt capital buffer requirements because the buffer "would reduce yields on money market funds and would therefore render such funds to be unattractive to many investors to a greater extent than the reforms [the Commission was] adopting."[62]

As explained above, the reforms that the Commission did in fact adopt in 2014 proved successful in increasing the resiliency of money market funds. The Commission's conclusions and concerns with respect to capital buffers in 2014 apply equally today, if not to a greater degree.

The Report cites to a paper published by Craig Lewis that considers the economic implications of supporting prime money market funds with capital buffers.[63] We highlight, however, that the premise of this paper is related to a capital buffer's ability to absorb fluctuations between a fund's net

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[62] *See id.* at 682.
[63] Craig M. Lewis, *Money Market Fund Capital Buffers* (April 6, 2015), *available at* https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2687687. While recognizing the loss absorbing capabilities of capital buffers and their impact to reduce shareholder incentives to redeem during periods of stress, the paper is premised on a capital buffer's protection against possible losses to absorb credit risk (not to address a market-wide liquidity crisis). The paper also concludes that imposing capital buffer requirements on prime funds would be a costly mechanism and would effectively convert such funds into synthetic government funds.

asset value calculated using available market quotations and its amortized cost and to absorb credit risk. As discussed above, the events in March 2020 were not the result of a credit crisis, but rather a market-wide liquidity crisis. The findings in the paper by Craig Lewis provide little to no support for the ability of capital buffers to address the redemption stresses faced by institutional prime money market funds as a result of a market-wide liquidity crisis. Rather, the findings relate to the ability of capital buffers to absorb credit risk experienced by prime money market funds, an event that did not occur in March 2020. In considering policy measures in response to the events in March 2020, SIFMA AMG encourages the Commission to focus on those policy measures that directly address liquidity-related stresses. Capital buffers do not address the liquidity stresses experienced by certain types of money market funds in March 2020.

- LEB Requirements

Similar to capital buffers, LEBs present significant issues with respect to shareholder transparency were the LEB running out of capacity. Disclosing that the LEB is running out of capacity would risk a run by causing investor alarm, similar to how redemption behavior increased when a fund's level of weekly liquid assets decreased closer to 30%. Rather than acting as a safety net and preventing a run, this could produce the unintended consequence of triggering investor fear and therefore a run. Not disclosing that the LEB is running out of capacity, however, would seemingly go against the transparency generally provided under Rule 2a-7.

Also, policy measures that involve pooling liquidity resources to be shared by all members, such as the LEB policy measure, present an unfair result to money market funds that invest in safer assets or manage their portfolios more conservatively and are therefore less likely to have a need to access the LEB.

SIFMA AMG further agrees with the extensive potential drawbacks, limitations, and challenges listed in the Report, including moral hazards effects, banking law issues, access to the discount window by the LEB, and issues with building adequate capacity.

In analyzing LEB membership, the Commission expressed concern that a private liquidity facility would not have sufficient purchasing capacity in the event of a widespread run without access to the Federal Reserve's discount window and highlighted that the Commission does not have legal authority to grant discount window access to an LEB. As was raised at the Commission's roundtable on money market funds in 2011, access to the discount window would raise complicated policy considerations and likely would require legislation. Moreover, the Commission highlighted concerns about conflicts of interest inherent in an LEB managed by participants that do not all have the same interests, including related to allocating limited liquidity resources during a crisis and choosing which funds gain access. The Commission ultimately concluded that:

> These potential issues collectively created a concern that such a facility may not prove effective in a crisis and thus we would not be able to achieve our regulatory goals of reducing money market funds' susceptibility to liquidity runs and the corresponding impacts on investor protection and capital formation. Combined with [the Commission's] lack of authority to create an [LEB] with access to the Federal Reserve's discount window, these concerns ultimately have led us to not pursue this alternative.[64]

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[64] *See id.* at 693.

The Commission's conclusions and concerns in 2014 apply equally to the consideration of this policy measure, if not to an even greater extent.

- Sponsor Support

With respect to sponsor support, SIFMA AMG notes several options available to facilitate (rather than mandate) sponsor support of money market funds, which we believe is the most appropriate manner in which to govern and regulate sponsor support. For example, Rule 17a-9 under the 1940 Act permits purchases of certain securities from a money market fund by an affiliate, subject to certain conditions. In fact, without an explicit requirement regarding sponsor support, money market fund sponsors made purchases under Rule 17a-9 in March 2020 to support certain money market funds.

Many of the ways in which sponsor support may be structured require a detailed analysis of the affiliated transaction prohibitions in Section 17 of the 1940 Act and, at times, may require no-action or exemptive relief from the staff of the Commission.[65] Section 17 of the 1940 is intended to protect investors from abuses of self-dealing, a fundamental underlying policy of the 1940 Act. The Commission has issued exemptions from the prohibitions of Section 17 in order to permit funds and affiliates to enter into certain transactions, subject to various terms and conditions. However, we are not aware of situations where the Commission has mandated funds and affiliates to enter into such transactions. Doing so would be contradictory to the overarching policy of Section 17 of the 1940 Act that prohibits such affiliated transactions.

Further, certain types of sponsor support are not responsive to a liquidity crisis and would therefore not address the issues faced by money market funds in March 2020. For example, capital contributions would not provide much assistance to money market funds in a liquidity crisis. Certain types of sponsor support may also require significant tax planning to ensure the support achieves its intended effect. For example, in considering a capital contribution it is imperative to address tax provisions which may negate the restorative effect of the contribution on share value (which could require that the fund make a distribution to shareholders in the amount of the contribution).[66] These issues would need to be considered in evaluating structures governing sponsor support. Considerations related to the size of the support and most appropriate type of sponsor support should not be subject to a "one-size-fits-all" approach and may overly complicate any regulatory framework governing sponsor support.

One of the reasons for the sponsor support policy measure cited in the Report is to clarify who bears risks. Under current regulatory requirements, money market funds are required to state in their summary prospectus and in all advertisements that "[t]he Fund's sponsor has no legal obligation to provide financial support to the Fund, and you should not expect that the sponsor will provide financial support to the Fund at any time."[67] We also note that a fund's investment management contract defines the scope of the adviser's services and is publicly filed with the Commission, thereby

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65 Section 17(a) prohibits sales of securities by an affiliate to a fund and may be implicated if an affiliate enters into an agreement to provide support to the money market fund as the support agreement could be viewed as the issuance of a security to the money market fund. Further, Section 17(d) prohibits joint transactions between a fund and an affiliate.
66 *See* JOAN OHLBAUM SWIRSKY, THE GUIDE TO RULE 2A-7 (3rd ed. 2017).
67 *See* Item 4(b) of Form N-1A; 17 C.F.R. § 230.482(a)(4) (2021). This statement is required unless such support is contractually committed and the term of the agreement will extend for at least one year following the effective date of the fund's registration statement.

providing further clarity on the responsibilities of, and risks and costs borne by, the investment adviser versus the fund. As such, the current regulatory regime provides clarity to investors regarding who bears risks and that sponsors are under no legal obligation to provide financial support to the money market fund.

With respect to the benefit noted in the Report of strengthening sponsors' incentives to reduce portfolio risks, as discussed above under "The Liquidity Crisis in March 2020," institutional prime money market funds held on average 43% of their assets in weekly liquid assets although they were only required to hold 30% of their assets in weekly liquid assets. This highlights sponsors' reduction of portfolio risks under the currently regulatory framework, absent a regulatory framework requiring a sponsor to provide support. Additionally, the requirement to report a fund's level of weekly liquid assets and various other portfolio holding metrics daily on its website provides sufficient incentive to reduce portfolio risks. Moreover, the 2014 reforms implemented a requirement for money market funds to file on Form N-CR, a public filing with the Commission, upon the occurrence of certain material events, such as the provision of affiliated financial support. This public disclosure requirement encourages reduction of portfolio risks in order to avoid public disclosure of a negative event in the portfolio. This can be further evidenced by the fewer number of money market funds that received financial support from affiliates in March 2020 as compared to those that received financial support from affiliates during the global financial crisis in 2008.[68]

Accordingly, SIFMA AMG does not support making sponsor support for money market funds explicit and instead believes the current regime of providing options to facilitate sponsor support is the most appropriate manner to regulate sponsor support. To further the ability of sponsors to support money market funds, SIFMA AMG supports the Commission codifying the temporary relief issued to the Investment Company Institute to permit the purchase of money market fund securities by an affiliate where reliance on Rule 17a-9 could conflict with Section 23A and 23B of the Federal Reserve Act.[69] As noted in the Report, this could obviate the need for future Commission staff no-action letters relating to the interaction of Rule 17a-9 and certain banking law provisions, which is one way to provide more certainty with respect to sponsor support.

In conclusion, the bank-like policy measures in the Report are inappropriate policy measures to implement for money market funds and present overly burdensome operational and administrative complexities and costs on all money market fund stakeholders. These policy measures are not responsive to the issues that occurred in March 2020 and will therefore be ineffective in addressing such matters. These policy measures will eliminate or significantly decrease the prime and tax-exempt money market fund sector and therefore negatively impact the resiliency and functioning of the short-term funding markets.

g. Floating Net Asset Values for all Prime and Tax-Exempt Money Market Funds

SIFMA AMG generally opposes a requirement for all prime and tax-exempt money market funds to float their net asset value because such policy measure does not address the contributors to

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[68] In March 2020, four funds filed on Form N-CR to report financial support. Commission staff estimates that almost 20% of all money market funds received some support from affiliates from August 2007 to December 31, 2008. *See* Money Market Fund Reform, Investment Company Act Release No. 28807 (June 30, 2009), *available at* https://www.sec.gov/rules/proposed/2009/ic-28807.pdf.
[69] See Letter to Susan Olson, Investment Company Institute (March 19, 2020), *available at* https://www.sec.gov/investment/investment-company-institute-031920-17a.

stresses in the short-term funding markets in March 2020, does not improve the resiliency or functioning of the short-term funding markets, and would not decrease the likelihood that official sector intervention is needed to address a run on a fund. During the market stress in March 2020, the money market funds that saw the heaviest outflows were institutional prime money market funds. Prime institutional money market funds were required to float their net asset values beginning in 2016. Despite the requirement for institutional prime money market funds to float their net asset values, there is no evidence that floating their net asset value impacted investor redemption behavior in March 2020.[70] Rather, investor redemption behavior was driven by liquidity concerns as opposed to concerns over a money market fund's net asset value. Many of our members view imposing a floating net asset value requirement on retail prime and tax-exempt money market funds as (1) not addressing the types of money market funds that saw the heaviest outflows in March 2020, and (2) imposing a requirement that has proven unsuccessful in slowing redemptions on other money market funds.

The reasons that the Commission did not apply the floating net asset value requirement to retail money market funds still exist today. Namely, retail investors historically have behaved differently from institutional investors in a crisis, being less likely to make large redemptions quickly in response to the first sign of market stress. For example, during the March 2020 liquidity crisis, institutional prime money market funds had substantially larger redemptions than retail prime money market funds. Despite the availability of additional tools, such as liquidity fees and redemption gates and enhanced website disclosures, retail investor behavior during the COVID-19 liquidity crisis did not differ significantly from retail investor behavior during the global financial crisis. In adopting the 2014 reforms, the Commission noted that "the significant benefits of providing an alternative stable [net asset value] fund option justify the risks associated with the potential for a shift in retail investors' behavior in the future, particularly given that retail money market funds will be able to use fees and gates as tools to stem heavy redemptions should they occur."[71] Given that there was no shift in retail investors' behavior in March 2020, and retail money market funds continue to have liquidity fees and redemption gates as tools to stem heavy redemptions should they occur, many of our members see no policy reason to implement a floating net asset value for retail prime and tax-exempt money market funds at this time.

Furthermore, implementing a floating net asset value would impose additional costs on retail prime and tax-exempt money market funds and their intermediaries to implement, as retail distribution channels and operations are different than institutional channels and operations that have already implemented a floating net asset value. This policy measure would likely also cause a further decrease in the size of the prime and tax-exempt money market sector, which, as discussed more fully above, would negatively impact the resilience and functioning of the short-term funding markets.

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SIFMA AMG sincerely appreciates the opportunity to comment and your consideration of these views. We stand ready to provide any additional information or assistance that the Commission might find useful. In particular, we and our members would welcome the opportunity to work with the

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70 *See e.g.,* Lei Li et al, *Runs and Interventions in the Time of Covid-19: Evidence from Money Funds,* CENTRE FOR ECONOMIC POLICY RESEARCH COVID ECONOMICS, Issue 29 at 53, note 3, *available at* https://cepr.org/sites/default/files/CovidEconomics29.pdf (finding further no evidence that lower floating net asset values drove additional outflows during the COVID-19 crisis).

71 *See* 2014 Adopting Release, *supra* note 6 at 220.

Commission and other industry representatives to address future policy measures for money market funds. Please do not hesitate to contact either Timothy Cameron at (202) 962-7447 or tcameron@sifma.org or Lindsey Keljo at (202) 962-7312 or lkeljo@sifma.org with any questions.

Respectfully submitted,

Timothy W. Cameron, Esq.
Asset Management Group – Managing Director and Head
Securities Industry and Financial Markets Association

Lindsey Weber Keljo, Esq.
Asset Management Group – Managing Director and Associate General Counsel
Securities Industry and Financial Markets Association

Cc: The Honorable Allison Herren Lee
The Honorable Caroline A. Crenshaw
The Honorable Hester M Peirce
The Honorable Elad L. Roisman
Sarah ten Siethoff, Acting Director, Division of Investment Management