ICI VIEWPOINTS

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Fact Checking SEC Statements on Money Market Fund Reform

By Eric J. Pan

For more than 80 years, our part of the financial industry – mutual funds, ETFs, and money market funds – has been one of the most well-regulated and transparent in the world, which is appropriate given our central role in managing money for hundreds of millions of Americans.

It is therefore expected that policymakers and academics spend a lot of time thinking about us, and we appreciate the healthy dialogue we have always had with the dedicated and hard-working SEC staff about how to improve our regulatory framework. We also depend on SEC leadership having deep expertise about how funds and the markets work so that we can trust that they are exercising the right judgment to achieve the SEC mission: to protect investors; maintain fair, orderly, and efficient markets; and facilitate capital formation.

One place where we need to make sure the SEC has its facts right is in its open Rulemaking on Money Market Funds (MMFs).

Like regulators, funds want financial markets that are resilient to shocks – the question is how best to get there.

ICI has written extensively, based on industry-leading data, about the liquidity events of March 2020, includingour comment letter to the SEC. We show, through a comprehensive analysis of data, that MMFs were not the cause of market instability as COVID was spreading around the globe. If you missed our roundtable last year on the topic, it's worth taking a look at what we discussed *here* and *here*.

In its proposal, the SEC wants to mandate swing pricing for prime institutional money market funds. What the SEC does not appear to realize (or has not said is its intent) is that swing pricing would cut off prime money market funds at the knees, to the detriment of investors. The products would be stripped of their cash-equivalent features, such as same-day settlement and multiple NAV strikes per day. And investors would be hit with unpredictable costs for redeeming.

Recent statements by SEC leadership suggest that they think their proposal on swing pricing is appropriate because they believe that MMFs in Europe already use swing pricing. That fact is that European MMFs *do not* use swing pricing. There is neither a regulatory mandate to use swing pricing for MMFs in Europe, nor do any European MMFs voluntarily use swing pricing. In fact, we're unaware of swing-pricing for MMFs being used anywhere in the world. There's simply no parallel in the Europe for what the SEC is proposing, and the SEC is wrong to suggest that as a justification for its rulemaking.

I've also seen suggestions by the SEC leadership that any adverse impact on MMFs would not harm investors because they would just shift their money to ultrashort bond funds. Such a conclusion seems flawed given the nature of the markets. Ultrashort bond funds are not a substitute for MMFs. Ultrashort bond funds hold riskier portfolios, can't be considered as cash equivalents by businesses, and don't have intraday liquidity since they settle tomorrow rather than today.

And the SEC leadership knows that MMF investors cannot easily go to MMFs' closer substitute: bank deposits. Only MMFs offer a market rate of return. This becomes even more important as the Fed continues to raise interest rates. And under current banking regulations, banks won't take large amounts of new deposits like these.

The fact is that MMFs are vital to our capital markets. They are ingrained in the daily economic life of our country, and that success would be very difficult to replicate. The SEC needs to be extremely careful as it considers changes here.

All to say, this is a good time to measure twice, and cut once.

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