United States Senate

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS

WASHINGTON, DC 20510–6075

April 11, 2022

The Honorable Gary Gensler
Chair
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: Money Market Fund Reforms, File No. S7-22-21

Dear Chair Gensler,

Money market mutual funds ("MMFs") are a valuable investment option for retail investors, an essential cash management tool for institutional investors, and a vital source of funding for governments and corporations. As you stated during your confirmation process, regulations should "ensure access to investors" for MMFs "while also ensuring stability in our financial system."[1]

I support the proposed removal of the arbitrary threshold linking 30% weekly liquid assets ("WLA") to the imposition of fees and gates ("fees and gates linkage"). However, the proposed requirements for swing pricing, enhanced liquidity risk, and adoption of policies for negative interest rates are not justified. Instead, the Securities and Exchange Commission ("SEC") should allow all types of MMFs to adopt measures the funds think best ensure their resiliency, including a stable Net Asset Value ("NAV").

I. Fees and Gates Linkage

The SEC should repeal the 30% WLA fees and gates linkage because the COVID-19-related market disruptions in March 2020 showed that this requirement is a flaw in the MMF regulatory regime. The March 2020 events do not justify any further costly and prescriptive MMF regulations. Any insistence otherwise misinterprets the March 2020 events so severely that issuing a final rule by the SEC under this pretense may be arbitrary and capricious.

MMFs were not the principal cause of pressure on the short-term funding markets in March 2020. These market disruptions primarily came from the unprecedented COVID-19 pandemic and government-imposed business shutdown orders. Even the Treasury markets showed significant deterioration as bid-ask spreads for Treasuries widened dramatically.[2] However, the fees and gates

[1] Responses by the Honorable Gary Gensler to Questions for the Record from Ranking Member Pat Toomey (Mar. 2021), at 125-26, available at https://www.congress.gov/117/chrg/CHRG-117shrg45766/CHRG-117shrg45766.pdf.
[2] Michael Fleming and Francisco Ruela, *Treasury Market Liquidity During the COVID-19 Crisis*, New York Fed's Liberty Street Economics (Apr. 17, 2020), available at https://libertystreeteconomics.newyorkfed.org/2020/04/treasury-market-liquidity-during-the-covid-19-crisis/.

linkage may have caused investors to treat the 30% WLA like a "hard liquidity floor,"[3] causing those with an "anticipatory, risk-mitigating perspective" to "further accelerate[] redemptions"[4] to avoid the risk of a gate being imposed.

Because the 30% WLA fees and gates linkage served as a floor, it could not serve as a counter-cyclical liquidity cushion. Even though impacted MMFs saw redemptions, they "divested longer-dated securities," not their WLA, and only one dropped below the 30% WLA threshold during the crisis.[5] Without this threshold, MMFs may have drawn down their liquid assets to weather the market distress instead of hoarding them, which also may have been less disruptive to the market.

II. Swing Pricing

The SEC should not force institutional prime and institutional tax-exempt MMFs to adopt swing pricing, which would require redeeming shareholders to take a haircut from NAV to reflect liquidity and other costs to the fund.[6] These MMFs offer "(i) a T+0 settlement structure and (ii) multiple NAV strikes in a day;"[7] swing pricing could make both features impossible. The SEC analysis on this issue is significantly incomplete. While acknowledging that MMFs may have to impose earlier order cut-off times to retain T+0 and drop the number of NAV strikes per day,[8] the proposal does not analyze or quantify the costs of this change, including the attractiveness of MMFs if yields drop. Instead, the proposal merely asserts, without evidence, that these costs (again, uncalculated) are acceptable in order "to address investor harm and dilution" from redemptions that would make a fund less liquid.[9]

There is little to no meaningful experience implementing swing pricing for U.S. MMFs offering T+0 settlement and multiple NAV strikes in a day.[10] Requiring swing pricing under these circumstances would subject a nearly $650 billion investment product to an unproven and experimental regulatory regime that may very well make MMFs critically unappealing to investors who may need timely redemption opportunities.

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[3] Letter from the Investment Company Institute ("ICI") (Apr. 12, 2021), at 12, available at https://www.sec.gov/comments/s7-01-21/s70121-8662926-235321.pdf ("ICI Letter"); *see also* Letter from the Committee on Capital Markets Regulation (May 24, 2021), at 2, 13, available at https://www.sec.gov/comments/s7-01-21/s70121-8828379-238191.pdf.
[4] Money Market Fund Reforms, 87 FR 7248, 7258 (Feb. 8, 2022).
[5] ICI Letter at 12.
[6] Swing pricing would reflect spread and certain other transaction costs of selling a "vertical slice" of the fund's portfolio and also include an estimate of market impact costs when net redemptions exceed a specified threshold.
[7] Letter from BlackRock (May 12, 2021), at 8, available at https://www.sec.gov/comments/s7-01-21/s70121-8662484-235306.pdf.
[8] 87 FR at 7269.
[9] *Id.*
[10] *See* Letter from PIMCO (Apr. 19, 2021), at 2, available at https://www.sec.gov/comments/s7-01-21/s70121-8687378-235664.pdf ("Swing pricing works in Europe because of early cut-offs for receiving subscription/redemption orders prior to NAV timing for European funds. In the U.S., however, subscriptions and redemptions historically have been accepted until the NAV cut-off, including by intermediaries, who typically report flows to funds with a delay – often 12 hours or more.").

III. Liquidity

Currently, MMFs are required to hold at least 10% of total assets in daily liquid assets and at least 30% of total assets in WLA. Under the SEC's proposal, these requirements would increase to 25% and 50%, respectively. The SEC's argument that most MMFs already have liquidity levels near these proposed thresholds is unpersuasive.

First, the SEC concludes that up to 15% of affected MMFs may have to increase their daily liquid assets and half of affected MMFs may have to increase their WLA.[11] The SEC does not quantify how much this would cut MMF yields, or the costs of dampening demand for MMFs and potentially introducing more market instability. Second, the SEC has not established that funds would hover around the proposed liquidity requirements. MMFs may retain much higher liquidity levels during normal economic conditions as they did with the 30% WLA threshold.[12]

Finally, the SEC's use of hypothetical stress tests based on "redemption patterns of prime institutional funds from March 16 to 20, 2020" to set liquidity levels is similarly unpersuasive as the fees and gates linkage partly drove redemptions during this period. Instead, the SEC should have evaluated liquidity levels using a scenario that estimated redemption levels under an MMF regulatory regime without the fees and gates linkage, as a study conducted by the ICI did.[13]

IV. Negative Interest Rates

The SEC has not provided a coherent rationale for its proposal on negative interest rates, failing both to explore fully the proposal's costs and to point to meaningful benefits. The proposal fails to establish that a negative interest rate environment *may* even occur, much less how long it would last. Proving this is vital to estimating the proposal's benefits. While the SEC points out that "[t]wice during the past 15 years, the Federal Reserve established the lower bound of the target range for the federal funds rate at 0%,"[14] the range was never set below 0%.

Even if negative interest rates occur, the SEC fails to show how investors benefit from these amendments. The SEC asserts that prohibiting a reverse distribution mechanism to maintain a stable NAV avoids "mislead[ing] investors about the value of their investments,"[15] but the *sole* evidence is a three-sentence submission from Jose Joseph, a self-identified "investor." It is not clear if Mr. Joseph is a retail investor or why he believes investors would be confused.[16] The lack of benefits is noteworthy given the costs. According to the SEC, its proposal on negative interest rates "may

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[11] 87 FR at 7301.
[12] *See* Letter from SIFMA Asset Management Group (Apr. 12, 2021), at 18 n. 44, available at https://www.sec.gov/comments/s7-01-21/s70121-8664048-235345.pdf.
[13] *See* Letter from ICI to the Financial Stability Board (Aug. 13, 2021), at 3, available at https://www.ici.org/system/files/2021-08/21ltrfsbmmfs.pdf.
[14] 87 FR at 7277. Although the SEC claims "other regulators and academics, including prior Federal Reserve leaders" have praised negative interest rates, the sole evidence cited is a Ben Bernanke speech in 2016 when he no longer was Federal Reserve Chairman. *Id*. at 7277-78.
[15] *Id*. at 7306.
[16] *See* Comment of Jose Joseph (Apr. 13, 2021), available at https://www.sec.gov/comments/s7-01-21/s70121-8668370-235441.htm. Similarly, Mr. Joseph does not explain why an MMF could not maintain a stable NAV fairly and transparently by clearly indicating to investors when they are performing a reverse distribution and what that means.

present operational difficulties for intermediaries" and impose other costs like upgrading processing systems, which may "adversely impact the size of [some] intermediary distribution networks."[17]

V. A Better Alternative

Rather than narrowly prescribing how MMFs must operate to remain resilient during market disruptions, the SEC should consider broadly authorizing MMFs to determine how to ensure their funds' resiliency. An MMF could appropriately tailor measures based on fund-specific factors, such as its investor base, asset mix, and how it is distributed. As Commissioner Hester Peirce noted, this regulatory approach "would allow for market choice, enable us to see what works, and make the financial system more resilient by diminishing the likelihood that problems at one money market fund would spill over to other funds, which in turn might reduce the urge of those in government to rush in with industry-wide rescues."[18] In other words, it would reduce systemic regulatory risk.

This flexible approach must allow *all* funds to adopt a stable NAV. The U.S. economy faces sustained high inflation and will see the money supply decrease to combat this inflation. Given these conditions, the need for a product that allows investors to obtain a higher return on investment while facilitating the provision of much-needed capital to municipalities and corporations is as vital as ever. Allowing MMFs to again adopt a stable NAV would restore an essential feature of their use as a cash management tool and level the playing field for MMFs investing in private companies and municipalities.

Furthermore, the SEC and other financial regulators should consider to what extent the market disruptions in March 2020 stemmed from factors unrelated to MMF regulations and how to address these factors. As ICI has noted, MMFs "are just one participant in the short-term funding markets," and even the elimination of MMFs "would not make these markets more resilient, and the short-term funding markets will continue to be a source of stress to the financial system."[19]

Thank you for your consideration.

Sincerely,

Pat Toomey
Ranking Member

cc: The Honorable Hester M. Peirce, Commissioner
The Honorable Allison Herren Lee, Commissioner
The Honorable Caroline A. Crenshaw, Commissioner

[17] 87 FR at 7307.
[18] Commissioner Hester M. Peirce, Statement on Money Market Fund Reforms (Dec. 15, 2021), available at https://www.sec.gov/news/statement/peirce-statement-money-market-fund-reforms-121521.
[19] Letter from ICI (May 12, 2021), at 8, available at https://www.sec.gov/comments/s7-01-21/s70121-8790454-237801.pdf.