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ICI's McMillan Says Plans for MMFs Outrageous, Time for SEC to Move On

Lawyers, accountants, regulators and mutual fund professionals are gathered at this week's Mutual Funds and Investment Management Conference in Phoenix, Arizona, and **money market mutual fund regulation is expected to be a hot topic**. (***Crane Data's*** **Peter Crane** will be in attendance, and a **high-powered panel on money funds will take place Monday afternoon**, so look for more coverage in tomorrow's "News".) **Karrie McMillan**, General Counsel of the Investment Company Institute, presents first with a talk entitled, "Clouds Overhead: Financial Regulation After the Crisis." The transcript of her speech says (in relation to money funds), "**Then there's the long-running saga of money market funds**. It's been 3-1/2 years since **Reserve Primary Fund** broke the dollar, and more than two years since the Securities and Exchange Commission adopted the post-crisis amendments to Rule 2a-7. **But we're still waiting for the promised "Round Two" changes**."

She says pieces of the Volcker rule can be fixed, but "I can't say the same about the second dark cloud -- the SEC's push for "structural changes" in money market funds." McMillan says, "**We'll have a panel this afternoon on money market funds, where we hope to gain a better understanding of the SEC's plans and proposals**. However, there have been enough leaks and enough public commentary that we all have a pretty good handle on where Chairman Schapiro and the staff are going. Let me cut through all the detail -- all the rhetoric -- all the arguments. **Let me just state something that should be obvious to us all: What the SEC is considering doing to money market fund investors is outrageous. Outrageous**."

She continues, "**No other mainstream financial product in this country has a regulator-imposed freeze on assets**. No other mainstream financial product has been ordered to routinely tell its customers, "You can put your money in -- but you can't get it all back when you want it." This is not a minimum account balance, where depositors pay higher fees or sacrifice interest if their balances fall. No -- this is Washington saying to investors: "You can't have your own money back" without an arbitrary delay. Not just in a crisis -- but in good times and bad. **For more than 70 years, mutual funds have operated on the opposite idea -- the principle that funds will redeem their shares -- in full -- on any day that the markets are open**. Yet the staff of the SEC now appears to be ready to say that this core principle doesn't apply for money market fund investors. Investors who depend on the stability, convenience, and liquidity of money market funds -- all the features the SEC's proposals would take away."

McMillan explains, "**Now, mix a redemption freeze that will lock up investors' assets with a capital buffer that deprives them of yield, and you have one of the reported SEC proposals. The other is that old chestnut -- floating the value of money market funds**. We've been batting that idea down for three years now. And we've won some important converts. Not among the banking regulators -- I'll grant you that. But we've certainly created doubts among many at the SEC. **The record is clear that floating the NAV of money market funds won't change investor attitudes or behavior ... won't prevent redemptions in a crisis ... and won't reduce systemic risk**. What it will do is destroy the value of money market funds for investors -- and for the economy. **If they're listening to investors, the staff and leadership at the SEC should have gotten that message loud and clear**."

She adds, "We've looked at what happened to money market funds' mark-to-market values last summer, at the height of the eurozone crisis. We looked at the prime funds with the greatest exposure to European financial institutions. We found that their "floating" value dropped by nine-tenths of a basis point. On a $1 share, that's a dollar sign followed by: 0.00009. If you're trying to follow along, that's nine one-thousandths of a penny. **That kind of "float" is not going to move a share priced at $1, and it's not going to move a $10 share**. It might -- in extreme conditions like the eurozone crisis -- move the price of a $100 share. **Forget about "breaking the buck" -- funds will have to "break the Benjamin."** But if the SEC really wants money market funds to float, our research suggests they're going to have to

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reprice them to $1,000 a share. **Otherwise, they're going to force investors to swallow all the legal, tax, and accounting burdens of floating funds -- only to discover that whatever funds are left won't actually float at all**."

McMillan also says, "I said earlier that I thought the potential damage of the Volcker Rule is inadvertent. Here, however, the damage is no accident. **Money market funds are one of the great success stories of modern financial regulation**. Throughout the history of these funds, the SEC has carefully crafted rules that balance these funds' competing objectives of stability of principal, liquidity, and yield. These rules have enabled money market funds to flourish and innovate -- to the great benefit of investors and the economy. The 2010 amendments to Rule 2a-7 built upon that success. They raised the bar for what it means to be a money market fund -- and the new model is far stronger. **These reforms were tested and proven last summer, when they made money market funds more resilient in the face of crisis. They have made investors more secure, at a reasonable price. They have reduced systemic risk. They are a success**."

She explains, "**But the SEC's "Round Two" proposals could easily destroy its "Round One" gains**. Think about it -- the 2010 amendments reduced portfolio risks; increased liquidity; empowered boards to make sure investors are treated fairly; and made these funds more transparent. By contrast, Round Two would drive billions of dollars away from of money market funds and into unregistered cash products that have no risk-limiting regulations, no required liquidity, no board governance, and no transparency. Round Two would undo Round One—and then some. **It's time for the SEC to recognize the success of its 2010 reforms -- and move on**."

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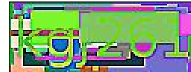

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