The Bond Buyer

The Daily Newspaper of Public Finance

Wednesday, May 30, 2012

Treasurers: Proposed SEC Money Fund Regs Bad For Municipalities

By Kate Marshall,
Manju Ganeriwala and Richard Ellis

As stewards of our states' coffers, state treasurers are tasked with managing and protecting the financial resources of our taxpayers.

In carrying out these responsibilities, like many individuals and families in this country, we rely heavily on money market mutual funds. We use money funds because they are an important investment tool as they provide ready liquidity, preservation of capital and diversification of credit exposure.

That is why state treasurers are so concerned about proposals in Washington that would sharply reduce the ability of money market funds to help manage our states' day-to-day finances, and could spell the end of this product.

In 2010, the Securities and Exchange Commission adopted regulations that enhanced the liquidity of money market funds while greatly reducing interest rate and credit risks. The National Association of State Treasurers applauded these changes as appropriate in the wake of lessons learned from the financial crisis.

However, recent reports indicate the SEC may issue additional proposals that would change the nature of money market funds by mandating that the funds adopt a daily floating net-asset value rather than the current stable $1 per share value.

Money market funds are able to maintain this $1 per share stable value by making a wide range of very low risk, short-term investments whose value is unlikely to decrease.

But under the SEC's proposal, money funds would be required to "float," or modify the price of the funds every day, so with a $100 investment, on some days you may get a little bit less than $100. While the variations would be small — less than half a penny per dollar — it would cause most investors who rely on getting every dollar back to stop using money funds.

Simply put, this proposal could have very negative consequences for already cash-strapped state governments.

The stable net-asset value is a fundamental feature of money market funds that lets us know that practically speaking, for each dollar we place in these funds we will get at least $1 back when we withdraw public monies. This simple and direct valuation method has made money market funds a critical investment tool for state treasurers and U.S. investors for more than four decades.

A second SEC proposal would require holding back some of the taxpayers' funds invested in money market funds for 30 or more days before we could retrieve those funds. We move money in and out of money market funds on a daily basis. A required hold-back of invested funds reduces or eliminates the efficiency of these as an investment tool and would impose significant accounting and regulatory burdens while offering no further reduction in the risks of money market funds.

Many state treasurers also manage state pooled investment funds and local government investment pools, which resemble money market funds and function as safe and essential short-term investment of funds for both state and local governments. If these funds are required to conform to new regulations, the additional costs of compliance will be borne by the states or passed on to local governments.

If adopted, these proposed changes may well shrink the money fund industry and the participants who rely on it due to the uncertainties of daily mark to market and full liquidity.

If so, an important part of the investing and financing market will disappear, with investors left to search for other, perhaps riskier alternatives and borrowers forced to obtain credit at more expensive rates.

We appreciate the continual efforts to learn from and work to avoid a repetition of all aspects of the 2008 financial crisis. But we have an obligation to speak out when regulation goes too far.

For these reasons, at its 2012 Legislative Conference in Washington, D.C., the NAST unanimously adopted a resolution opposing these additional changes and will continue to work with the SEC to support appropriate regulation of money market funds.

We fully supported the 2010 regulations that helped make these investment vehicles the highly regulated, low-risk products that they are today. Those reforms fostered transparency, mandated higher credit quality and enhanced liquidity, thereby ensuring funds can weather periods of extreme market turbulence. In so doing, the new regulations have already achieved the effect of minimizing pricing fluctuations due to changes in interest rates and credit quality.

The proposed changes by the SEC add nothing to this but an undue regulatory burden.

Kate Marshall is the treasurer of Nevada and president of the National Association of State Treasurers. Manju Ganeriwala is the treasurer of Virginia and senior vice president of NAST. Richard Ellis is the treasurer of Utah and secretary-treasurer of NAST.

©2012 SourceMedia Inc. and The Bond Buyer. All rights reserved. SourceMedia, One State Street Plaza, New York, N.Y. 10004 (800) 367-3989