

ICI Details Plans for a Private Liquidity Facility to Further Strengthen Prime Money Market Funds

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In Comments on PWG Report Options, Institute Proposes More Investor Transparency, Continues to Oppose Floating NAV as Harmful to Investors, Economy

Washington, DC, January 11, 2011 - A new, private facility to provide a liquidity backstop for prime money market funds is the most promising solution to bolster the resilience of these funds in times of severe market stress, the Investment Company Institute (ICI) said in a letter submitted to the Securities and Exchange Commission. The letter responds to an SEC request for comments on the options for money market fund reform outlined in the [President's Working Group on Financial Markets \(PWG\) Report on Money Market Fund Reform Options](#) (Report).

"We commend all the members of the PWG for their thoughtful and thorough work on the Report, which affirms the crucial role money market funds play for investors and the U.S. economy," said ICI President and CEO Paul Schott Stevens. "A liquidity facility would build on the important reforms, including higher liquidity requirements, put in place by the SEC in 2010. The blueprint for a liquidity facility reflects the strong support of ICI and many of its members. We believe this approach, an option first suggested by the Treasury Department in mid-2009, holds the most promise for further strengthening money market funds in times of severe market stress, with the least negative impact."

The [Institute's letter](#) reiterates ICI's commitment to working with policymakers to strengthen and preserve money market funds to ensure their continued ability to serve as an effective cash management tool for investors, and as an indispensable source of short-term financing for the U.S. economy. The \$2.8 trillion invested in money market funds finance business payrolls and inventories; federal, state and local government operations; and credit card, home equity and car loans.

"Money market funds' role in the broader economy cannot be overstated," said ICI Chief Economist Brian Reid. "Short-term financing for the U.S. economy depends to a very significant extent upon the existence of money market funds."

ICI Supports Establishing Private Liquidity Facility; Outlines Details of Proposed Facility

Of the several money market fund reform options discussed in the Report, a liquidity facility (LF) is the best proposal to meet policymakers' goal of further strengthening money market funds while preserving the key characteristics that make these funds so important to the U.S. economy and valued by institutional and retail investors.

Under ICI's blueprint for a LF, all prime money market funds—those that invest in high-quality, short-term money market instruments, including commercial paper—would be legally required to participate in the LF, which would be structured as a state-chartered bank or trust company regulated by state banking authorities and the Federal Reserve. The LF would be capitalized through a combination of initial contributions from prime fund sponsors and ongoing commitment fees from member funds. In the third year, the liquidity facility would begin to issue time deposits to third parties to further build its balance sheet. Like other banks, the LF would also have access to the Federal Reserve discount window.

During times of unusual market stress the LF would buy high-quality, short-term securities from prime money market funds, which would enable funds to meet redemptions while maintaining a stable \$1.00 net asset value (NAV), even when markets are frozen. This would also protect the broader money market from a downward spiral in the market prices of money market instruments that could be caused by money market funds selling their securities into a challenging market. The very existence of such a liquidity

backstop could provide reassurance to investors and thereby limit the risk that liquidity concerns in a single fund might spur increased redemptions in all prime money market funds.

Importantly, the LF will not provide credit support, such as by buying distressed instruments. Rather, it is intended to meet liquidity needs brought on by market stresses through the acquisition of high-quality instruments. Further, the LF is designed to provide a liquidity backstop only after a money market fund has used a substantial portion of the large liquidity buffer each fund is required to maintain under SEC rules implemented in 2010.

ICI Proposes Additional Reform to Increase Investor Transparency

In addition to commenting on the options discussed in the PWG Report, ICI proposes that the SEC pursue new rules to ensure greater transparency about the investors who own money market funds through brokers and other intermediaries.

“A new rule requiring intermediaries to provide information to money market funds about their investors would make it easier for the funds to comply with ‘know your investor’ procedures required by the SEC in its money market reforms in January 2010,” said ICI General Counsel Karrie McMillan. “Different investors have different needs for redemptions and thus have different effects on funds’ need to maintain liquidity. Greater transparency will help funds identify factors that could affect their liquidity needs.”

Other Options Outlined in the Report, Including a Floating NAV, Do Not Serve Investors or Economy

ICI continues to oppose proposals that would force money market funds to abandon the stable \$1.00 NAV. There is compelling evidence that many money market fund investors would be unable or unwilling to use a floating NAV money market fund. In turn, many investors are likely to use less regulated products that seek to maintain a stable NAV and this development could lead to increased systemic risk.

ICI comments in detail on the other options in the Report—including mandatory redemptions in kind, insurance programs for money market funds, a two-tier system of funds with enhanced protections for stable NAV money market funds, reserving stable NAV funds for retail investors only, regulating stable NAV funds as special purpose banks, and enhanced constraints on money market funds substitutes—finding that they all have drawbacks ranging from potential detrimental impacts on money market funds, the market and investors, to possibly increasing rather than decreasing systemic risk.

The ICI comment letter, appendix, fact sheets and other related materials can be found in the [Money Market Fund Resource Center](#).