THE NEW ENGLAND COUNCIL

Committee Update

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Schapiro Testimony on Money Market Reform

Yesterday, Securities and Exchange (SEC) Chair Mary Schapiro testified at a Senate Banking, Housing and Urban Affairs Committee hearing, along with a number of financial services industry representatives, addressing the current state of the money market fund industry and proposed regulations. Since last fall, Chairman Schapiro has indicated that she believes there is a need for additional money market fund regulation, beyond the set of SEC regulations implemented in 2010 that introduced liquidity minimums, average maturity limits and new disclosure requirements for money market funds.

In yesterday's testimony, Schapiro argued "Although the Commission took steps in 2010 to make money market funds more resilient, they still remain susceptible today to investor runs with potential systemic impacts on the financial system, as occurred during the financial crisis just four years ago. Unless money market fund regulation is reformed, taxpayers and markets will continue to be at risk that a money market fund can 'break the buck' and transform a moderate financial shock into a destabilizing run." In blunt counterpoint, Sen. Patrick Toomey (R-PA) said, "You are telling us that this is a very vulnerable industry and that there are great threats of a run and using that to justify regulations that I think threaten the very existence of this industry."

Shapiro cited an internal SEC study that found over 300 instances over the last several decades where the sponsoring entity of a money market fund voluntarily stepped in with additional funds to support the one dollar valuation of a troubled fund. There was considerable debate among Committee members as to the validity of this data, noting that others, such as the Federal Reserve Bank, had highlighted a significantly smaller number of such voluntary backstops. Senator Twomey expressed his view that since 2008, "…we've had another round of new stresses, an ongoing terrible recession, a European credit crisis, downgrade of the U.S. government, considerable redemption pressure, and not a single problem in this whole industry."

The SEC chair emphasized her belief that "the stable $1.00 share price in money market funds has fostered an expectation of safety, although money market funds are subject to credit, interest-rate and liquidity risk." Further, in the event of a run, there are significant advantages to those that choose to redeem early. Schapiro suggested large institutional investors which have the resources to closely monitor such fund investments, would be better positioned than retail investors. As a result, Schapiro said, "…a run on a fund will result in wealth transfer from retail investors (including small businesses) to institutional investors."

Schapiro indicated that the SEC is currently examining a number of structural reforms for the money market fund industry, including one that would impose capital restrictions on the funds combined with limitations or fees on redemptions by consumers. A second would require money market funds to buy and sell shares based on the market value of the fund assets, i.e. use a “floating” net asset value.
Earlier this year, the New England Council wrote to Chairwoman Schapiro, expressing concerns about the unintended consequences of such a move to a floating net asset valuation for money market funds.
Echoing these concerns during yesterday’s hearing was Senator Jack Reed (D-RI), who said, “I’m concerned about the impact on municipal participants, at a time that they are all at a real siege because of the local and national economy,” said Sen. Jack Reed, Democrat of Rhode Island. “Many municipalities use money-market funds in a very efficient way to manage their cash.”
While Schapiro’s enthusiasm for additional money market money market fund reforms remains undimmed, most observers characterized the overall response of Senate Banking Committee members to this latest testimony as lukewarm. It is also unclear whether Chairwoman Schapiro can garner the support of a majority of her colleagues on the Securities and Exchange Commission to move forward with her reform proposals.

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