IDC Independent Directors Council
Promoting Excellence in Fund Governance

Group of Thirty Money Market Proposals Will Harm Investors, Economy

Opinion: Group of Thirty Money Market Proposals Will Harm Investors, Economy

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(as published in the opinion section in BoardIQ on March 17, 2009)

As independent directors of money market funds, we would like to point out the many benefits of these funds and warn of the dangers of the Group of Thirty's proposals to change the legal structure of these funds.

Money market funds provide incomparable benefits to U.S. investors and this country's capital markets. For more than 25 years, these funds have provided shareholders with a safe, liquid cash-management vehicle and the capital markets with a vital source of funding.

As Congress grapples with reforms to financial services regulation, we are concerned about any proposal that would significantly diminish the benefits provided by money market funds as they are currently structured and regulated. This would be precisely the result if the Group of Thirty's recommendations relating to money market funds were implemented. (Our comments relate only to money market funds regulated by SEC rule 2a-7.)

The Group of Thirty has proposed that money market funds offering services such as check writing should reorganize as special-purpose banks. If the funds want to remain as money market funds, Group of Thirty proposes they should no longer be allowed to use amortized cost pricing, and should carry a fluctuating net asset value.

As mutual fund independent directors, we strongly oppose the dramatic overreaction by the Group of Thirty to impose bank-style regulation on money market funds. Because of the fundamental differences between the way banks and money market funds operate and are regulated, subjecting money market funds to bank-style regulation would likely deprive investors of daily liquidity, high standards of safety and competitive yields and would deprive our country's capital markets and many state and local governments of a critical source of funding.

Money market funds already are among the most regulated financial products available today. They operate under strict SEC requirements regarding the investments they are permitted to make and how much they may invest in any one issuer.

These restrictions make sense. Limiting money market fund investments to high-quality, short-term securities and subjecting these investments to strict diversification standards help ensure their safety and liquidity. Overlaying this stringent regulatory structure is the independent oversight provided by a fund's board of directors. These attributes of safety make money market funds an important investment option for many investors in their retirement plans.

In addition to liquidity, safety, and competitive yields, most money market funds offer check-writing features. These attributes provide a variety of benefits to fund shareholders. Many retail investors use them as a place to "park cash" between investments or to fund a major purchase, such as a car or home.

Institutional investors use these funds primarily as a cash-management tool. Even though two money market funds "broke the buck," more than $300 trillion has moved in and out of all other money market funds for almost three decades with no loss of principal. No other financial product or service comes remotely close to meeting this impressive record of safety.

Money market funds also are a critical source of liquidity in America's capital markets. This nearly $4 trillion industry of some 800 funds buys the commercial paper, municipal securities and other financial products that U.S. companies, financial institutions, and state and local governments rely upon to finance their operations.

How vital is this source of funding?

As of December 2008, taxable money market funds held 40% of the total outstanding commercial paper, a dramatic example of the importance of money market funds as an intermediary of short-term credit and liquidity. And, as of year-end, tax-exempt money market funds had close to $500 billion under management, nearly all of which is invested in short-term state and local government debt. Without a doubt they are playing an indispensable role in public infrastructure and municipal service initiatives.

The current credit crisis has highlighted some issues that need to be carefully examined regarding money market funds. The lack of liquidity experienced in the commercial paper market, for example, was unprecedented. Accordingly, we strongly support a top-to-bottom review by the industry and the SEC of the regulatory requirements that govern money market funds to determine whether changes are warranted.

With almost $4 trillion invested in money market funds, investors have spoken; they prefer this product over bank certificates of deposit, passbook savings accounts and other comparable products. Clearly, Congress needs to focus on the benefits to investors and the capital markets as it considers whether to make changes to the legal framework governing money market funds. We think the Group of Thirty's proposals, if enacted, would do far more harm than good.
