Striving to Restructure Money Markets Funds to Address Potential Systemic Risk

by

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Today, the Commission considers amending the rules that govern money market funds to address potential systemic risks. Before I begin, I would like to recognize the efforts of the staff throughout the SEC, especially the Division of Investment Management and the Division of Risk, Strategy, and Financial Innovation. I acknowledge and appreciate the staff's good work in examining the 2010 amendments to Rule 2a-7 and the staff's report, which concluded that, among other things, the 2010 amendments would not have been adequate to prevent the systemic risks that we saw in 2008. This report has resulted in the much-improved proposal that is before us today.

The staff's work is a testament as to why the SEC should take the helm of matters that are within its jurisdiction. I appreciate that the Financial Stability Oversight Council ("FSOC") recently said as much in its 2013 Annual Report.[1] The SEC's expertise brings a clear-eyed experience and practical knowledge that can target needed change, while being mindful of unintended consequences.

I am supportive of the staff's recommendations and will first put the proposed amendments in context, and then highlight a few items.

Context

As a Commissioner who started in July 2008, I lived through the financial crisis at the SEC and remember it clearly. Because of that experience, it was very important to me that the SEC undertake reforms to strengthen money market funds and make the vehicles as transparent as possible. Accordingly, I was a strong advocate for the money market fund reforms that the SEC adopted in January 27, 2010. I particularly supported the adoption of Form N-MFP, because I was confident that the data collected would be instrumental in keeping the staff informed as to registered money market funds. The passage of time has demonstrated that Form N-MFP, and the other reforms adopted in 2010, have significantly strengthened money market funds and the SEC's oversight capabilities.

Moreover, at the time of the adoption of the 2010 amendments,[2] and in recognition of the potential for further reform, I highlighted in my public remarks two priorities that should be kept in mind. These priorities were that:

1. All contemplated proposals should take into account retail investors and ensure that they are able to continue to participate and benefit from money market funds; and

2. Any further proposals should include rigorous analysis to understand possible consequences, and that, due to the potential migration of trillions of dollars from regulated vehicles to unregulated vehicles, we should think about other necessary reforms regarding unregistered vehicles to make sure that there is no regulatory end-run.[3]

I have been consistent in highlighting these concerns for the past three years as the Commission contemplated further reforms.[4] I am pleased that the proposed amendments incorporate these priorities, and much more. The release we consider today is the result of substantial effort, and I believe it was effort well spent.

The release is the product of a confluence of factors that came together to allow us to vote on a well-researched and thoughtful set of proposed amendments.

First, on November 30, 2012, the SEC staff delivered to the Commission its report,[5] which delved deeper into the causes of investor redemptions in 2008, and analyzed the efficacy of the Commission's 2010 amendments to strengthen Rule 2a-7, and the potential impacts of future reforms on issuers and investors. This report is a direct result of the combined efforts of Commissioners Paredes, Gallagher, and myself. Although I requested that the report be conducted sooner, I am grateful for its completion. The results of the report allowed Commissioners and staff to engage in effective and productive discussions. The benefits of that process are clearly reflected in the proposed amendments we consider today.

Second, largely as a result of that report, today's release is based on significant amounts of data and analysis. The staff's report has resulted in a proposal that contains informed questions designed to elicit information and crystallize issues, rather than building on unexamined and questionable assumptions. The process leading to today's proposal has been a refreshing and inclusive process, and stands in direct contrast to the previous process.

The Proposed Amendments

The proposed amendments build on the report and offer policy choices and permutations, while incorporating the priorities I mentioned. For example, these amendments acknowledge the value of these products to retail investors and that retail investors did not constitute the "hot money" in 2008 that contributed to the perceived systemic risk and panic. As such, the proposing release recognizes the distinction between retail and institutional investors.

Moreover, the proposed amendments address the concern that registered money market fund assets could migrate to an opaque and unregulated market.[6] This issue is now discussed at length in the release, and the staff has designed a surgical amendment to Form PF to provide transparency on the possible outflows of monies to unregulated private funds that essentially operate like registered money market funds.

In addition, these proposed amendments increase the diversification of fund portfolios, enhance funds' stress testing, and increase transparency by requiring greater disclosure of registered funds.

While today's release is a vast improvement over past efforts, much remains to be decided. To that end, and as with all of our proposals, I expect that any final action by the Commission will be greatly informed by the comments and information we will receive.

Conclusion

When the SEC acts, it is important that we get it right. I acknowledge that this is always easier said than done, because "right" means different things to different people. Here, it is important to strike a balance between reducing the systemic risk that money market funds may pose as an industry, while protecting the benefits provided by registered money market funds.

Money market funds play an integral role in our economy. Investors, issuers, and intermediaries all utilize these funds. It's hard to think of another investment product that impacts so many different components of the American capital markets. This reality underscores the need to act in a careful and informed manner. Today's proposed amendments constitute a step in the right direction.

I'll end where I started – by recognizing the efforts of the SEC staff. I thank you for your hard work and dedication.

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1 Financial Stability Oversight Council, "2013 Annual Report," p. 12 (2013), http://www.treasury.gov/initiatives/fsoc/Documents/FSOC%202013%20Annual%20Report.pdf.

2 Commissioner Luis A. Aguilar, U.S. Securities and Exchange Commission, "Fortifying the Money Market Framework Upon Which Investors and Issuers Rely," Washington, DC (January 27, 2010), http://sec.gov/news/speech/2010/spch012710laa-mmf.htm.

3 See id.

4 Financial Stability Oversight Council, "Proposed Recommendations Regarding Money Market Mutual Fund Reform," (November 2012), http://www.treasury.gov/initiatives/fsoc/Documents/Proposed%20Recommendations%20Regarding%20Money%20Market%20Mutual%20Fund%20Reform%20-%20November%2013,%202012.pdf.

5 See "Response to Questions Posed by Commissioners Aguilar, Paredes, and Gallagher," a report by staff of the SEC's Division of Risk, Strategy, and Financial Innovation (November 30, 2012), http://www.sec.gov/news/studies/2012/money-market-funds-memo-2012.pdf.

6 Both Secretary Geithner and FSOC have also expressly raised the need to address the concern of money market fund assets migrating to an opaque, unregulated market as a result of structural changes to money market funds. See, Letter of Timothy F. Geithner, Secretary, U.S. Department of the Treasury, to Members of the Financial Stability Oversight Council on Necessary Money Market Reforms (September 27, 2012), http://www.treasury.gov/connect/blog/Pages/geithner-fsoc-letter.aspx.