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SEC Urged to Exempt Muni MMFs From Proposed Reforms.

State and local governments are urging the Securities and Exchange Commission to either abandon proposed reforms for money market funds or exempt municipal MMFs from the reforms and clarify the rule changes are not meant to impact local government investment pools.

The latest request comes from the National Association of State Treasurers, which sent a 12-page letter to the SEC on Monday detailing its concerns about the reforms that the SEC proposed in June.

"The SEC's proposed rule changes would be detrimental to competition, efficiency, and capital formation for our members as well as cities, counties, and other municipal entities," said the letter signed by Manju Ganeriwala, NAST's president and Virginia's Treasurer.

The letter made three major points. First, the proposed reforms for MMFs to have a floating net asset value instead of the current stable NAV of $1 per share and/or liquidity fees and gating to limit redemptions could force governments to abandon local government investment pools.

LGIPs have been created by several states to help state and local entities invest public funds safely and efficiently. Generally they are designed to provide short-term investments for funds that are needed by governmental entities on a day-to-day or short-term basis. They are rated by rating agencies and operate like money market funds, only their clients are local governments. They are indirectly rather directly regulated by the SEC because the Governmental Accounting Standards Board mandates that MMF-like funds be governed by MMF rules.

LGIPs cannot tolerate even small losses for many reasons, including legal restrictions, budget constraints, investment limitations or liquidity requirements.

"To the extent that LGIPs were indirectly forced into a floating NAV, or required to abandon the use of amortized cost accounting, the usefulness of LGIPs to numerous state and local government entities would be greatly diminished," the letter said. "This would result in disruption as public sector investors sought to redirect investments with few viable alternatives."

Rhode Island Treasurer Gina Raimondo raised the same concerns in a two-page letter that said the state, along with some municipalities and quasi-public agencies, currently invest more than $500 million in the Ocean State Investment Pool on a short-term basis.

A floating rate NAV, she said "could change administrative burdens and costs, including accounting and tax complexities that would diminish the product's usefulness. It could also result in investors choosing alternative means of managing cash that could prove to be more expensive, less diversified and riskier."

NAST's second big concern is that the proposed reforms would deter states from using MMFs as an efficient tool for managing large volumes of short-term liquid assets. "MMFs that seek to maintain a stable value per share are permitted investments for many of our members, which rely on these funds to obtain ready liquidity, preservation of capital, and to provide diversification," the letter said. Generally, variable NAV MMFs are not permitted investments for states, it said.

William Dressel, Jr. executive director of the New Jersey League of Municipalities, told the SEC in a one-page letter that MMFs "hold more than half of the short-term debt that finances state and municipal governments for public projects such as roads, bridges, water and sewage facilities, and hospitals …. Without that financing, local governments may be forced to limit projects and staffing, spend more on financing by investing in lower yield products, or increase taxes. Given our current operating environment, these are not viable options."

NAST's third concern is the potential adverse impact the SEC's proposed reforms could have on MMF purchase of short-term munis from state and local governments. "NAST is also concerned that a floating NAV, if applied to municipal MMFs, could lead to an exodus of investors from those funds," the letter said.

"We do not believe additional changes to money market fund regulation are needed at this time," NAST told the SEC. "If further changes are adopted, however, we urge the commission to (a) include a comment that it is not the SEC's intent to promulgate changes to LGIPs, and (b) create an exemption for municipal money funds equivalent to that established for U.S. government MMFs under the proposal."

Geoffrey Beckwith, executive director of the Massachusetts Municipal Association, agreed, saying, "Given the highly negative consequences that would result, there is no compelling reason to regulate municipal MMFs as if they were prime MMFs, rather than regulating them similarly to the Treasury and government MMFs with which they share numerous characteristics."

The Securities Industry and Financial Markets Association also urged the SEC to exempt muni MMFs.

'SIFMA strongly believes the SEC should specifically exempt municipal money market funds from both the floating NAV and the liquidity fee and redemption gate proposals for money market funds," said Leslie Norwood, SIFMA managing director, associate general counsel and co-head of munis. "These funds have not shown susceptibility to destabilizing runs, they maintain weekly liquid assets well in excess of regulatory minimums, and they are held mainly held by retail investors. If any of the proposed changes are imposed on municipal money market funds, investors will lose an attractive cash management option while local governments will find it harder to raise the capital they need for roads, schools, hospitals, and other critical infrastructure that keep our communities running smoothly."

by: LYNN HUME