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Why Issuers Want to Undo Money Market Mutual Fund Rules.

WASHINGTON – Pending legislation that would partially roll back regulations on money market mutual funds would be good for issuers of municipal bonds, issuer groups told a Senate panel Tuesday.

The Government Finance Officers Association and National Association of Health and Educational Facilities Finance Authorities both provided testimony in support of S.1117: The Consumer Financial Choice and Capital Markets Protection Act of 2017. The bill, introduced more than a year ago by Sen. Pat Toomey, R-Pa., would allow institutional money market funds to return to a fixed net asset value after a 2014 SEC rule change required those MMFs to use a floating NAV.

The SEC rule, which took effect in 2016, allows funds investing in federal government securities, as well as "retail" funds that have policies and procedures in place designed to limit investors to "natural persons," to use a stable NAV. Natural persons means human beings, rather than business entities. Other MMFs were required to "float" their NAVs, meaning that the value of a share can fluctuate rather than remain at a fixed $1. The change was designed to prevent investors from causing a "run" on MMFs by pulling out of them in a scenario similar to one that occurred during the financial crisis in 2008.

Muni groups have said requiring a floating NAV for so many MMFs would hurt issuers by both reducing demand for their short-term debt and locking them out of the funds they use as vehicles for short-term cash flow. The result, then-GFOA president Pat McCoy told lawmakers in 2017, is that issuers pay more to finance their infrastructure.

Christopher Daniel, chief investment officer of Albuquerque, New Mexico, testified for the GFOA Tuesday, telling members of the Senate Committee on Banking, Housing, and Urban Affairs that most local governments have policies or even state or local laws on the books requiring them to invest only in funds with a stable NAV. This is to ensure that public money is properly safeguarded, he said. With the effectiveness of the SEC's floating NAV requirement, Daniel said, local governments have been forced to use lower-yielding funds investing in U.S. government securities.

"By allowing all MMFs — prime, tax-exempt and government funds accessible to both retail and institutional investors — to offer a stable NAV, S. 1117 would allow state and local governments to once again utilize suitable investments as defined by state and local elected officials, rather than by the SEC," Daniel testified.

Chuck Samuels, general counsel to NAHEFFA, submitted written testimony. He said MMFs are among the largest purchasers of the short-term notes the authorities he represents issue, and that the rule has damaged that market.

"Unfortunately, funds that purchase the variable rate notes of the institutions we serve have experienced a nearly 50% decline as a result of the SEC's floating NAV rule, thereby driving up the cost of borrowing for investments aimed at improving the quality of health care and education in our country," Samuels wrote.

Mercer Bullard, a professor at the University of Mississippi School of Law, told the committee that he didn't believe the SEC's rule change was necessary to reduce systemic risk, but that he recommended against passage of S. 1117.

Bullard said he had four reasons for opposing the bill. First, he said that there has not been enough study on the impact of undoing the rule and that passing the bill now would risk rushing into a mistake the same way the SEC did in passing the floating NAV rule. Instead, Congress should instruct the SEC to analyze what effect the bill would have, said Bullard. Next, he said he does not have faith that the SEC is equipped to manage fund risk in the absence of the rule. Bullard's third point was that banking regulators might use any future MMF failure as an excuse to impose crippling restrictions on all funds.

Lastly, the Dodd-Frank Act stripped banking regulators of the emergency powers they would need to handle another "severe liquidity event," Bullard said, explaining that Dodd-Frank restricted banking regulators' authority to extend credit to non-banking institutions. As such, he told the committee, he couldn't recommend reviving the risks that existed under the old rules.

S. 1117 has an identical companion bill in the House: H.R. 2319. Like the Senate bill, it remains pending before committee.

By Kyle Glazier

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