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Industry claims victory in US battle

By Alex Padalka

The SEC's proposals faced a barrage of criticism

Following months of concentrated backlash from the industry, Mary Schapiro, chairman of the US Securities and Exchange Commission, last week said the agency had abandoned plans to reform the $2.6tn money market fund industry. Opponents of the reforms say their fight is far from over.

Ms Schapiro announced the decision just a week before the agency was due to vote on the proposals, which included reforms that would either force funds to abandon their cherished fixed $1 share price and adopt a variable net asset value structure, or restrict liquidity by requiring funds to set aside a capital buffer, possibly combined with restrictions or penalties on withdrawals.

The campaign against money market fund reform, industry veterans say, has been unprecedented. After the SEC circulated early drafts of the proposals in January, major fund sponsors and industry groups such as the Investment Company Institute and the Coalition of Mutual Fund Investors, as well as 33 members of Congress, said these reforms would wipe out the industry entirely and cause states, municipalities and a myriad of businesses to be deprived of a major funding source.

Federated Investors threatened a lawsuit to block any reforms. In April, the US Chamber of Commerce unleashed a "station domination ad buy" inside Washington's Union Station Metro stop – the closest Metro station to the SEC offices – calling for money market funds to be left alone.

Charles Schwab bought a full-page ad in the Wall Street Journal and USA Today, arguing that the "campaign to scare owners of money fund shares is neither accurate nor wise".

"I have been practising law in the investment management area for over 30 years and have not seen this level of contentiousness," says Barry Barbash, partner at Willkie Farr & Gallagher and a former director of the SEC's division of investment management.

Inside the SEC, commissioner Luis Aguilar, a former mutual fund executive viewed as the swing voter, said he opposed the proposals too.

While Ms Schapiro's remarks indicate that the opponents' concerns have been taken into account, few doubt that another regulatory body will take up the issue.

"The industry may have won a battle, but the war isn't over," says Niels Holch, executive director of the Coalition of Mutual Fund Investors. "The focus is now going to shift to the Federal Reserve and to the Financial Stability Oversight Council, both of which have considerable regulatory powers to address systemic risks to the capital markets and to taxpayer interests."

Mr Barbash adds: "In some ways, I think the FSOC is the appropriate body to look at the issue. When you break down these initiatives, they were more about systemic issues than about investor protection."

Regardless of which body takes up the reform, opponents say, a careful cost-benefit analysis must still be performed, something they say the SEC has disregarded.

"Money market fund regulation should not be examined in isolation, but rather in the context of overall systemic risk," wrote David Smith, executive vice-president and general counsel for the Mutual Fund Directors Forum. "This broad principle should apply irrespective of what regulator is involved."

Robert Kurucza, partner and chair of financial services at law firm Goodwin Procter and a former assistant director of the SEC's division of investment management, says: "At the end of the day, what I don't think has occurred is a very careful analysis of the situation.

"You can't ignore what the commission put in place in 2010 [when reforms raised funds' minimum liquidity and credit quality and reduced maturity limits] and how effective those requirements were to dampen or eliminate or avoid the pitfalls that occurred in 2011."

While there is consensus that another regulatory body will spearhead the money market fund issue, it is unclear when this will materialise into rule-making.

Furthermore, while the SEC has stepped away from money market funds for the time being, a different set of commissioners, or a different set of circumstances, may easily bring these proposals back.

"One thing I've noted about regulation of the financial services sector is that ideas never go away, they are just filed away, and they come out at market disruption," says Mr Barbash.

Alex Padalka is a contributor to BoardIQ, a Financial Times service