J.P.Morgan
Asset Management

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April 12, 2021

Vanessa Countryman
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: Potential Money Market Fund Reform Measures in President's Working Group Report (File No. S7-01-21)

Dear Ms. Countryman:

J.P. Morgan Asset Management ("JPMAM")[1] is pleased to respond to the Securities and Exchange Commission's (the "SEC" or the "Commission") request for comment[2] on potential money market fund ("MMF") reform measures set forth in the December 2020 Report of the President's Working Group on Financial Markets ("PWG Report").[3]

JPMAM is one of the largest managers of MMFs, with over $710B in assets under management globally. In the US, we manage over $460B in MMFs, across government and treasury MMFs (~$360B), institutional prime MMFs (~ $77B), retail prime MMFs (~$11B), and tax-exempt MMFs (~$12B).

Like many other MMFs, JPMAM's institutional prime and, to a lesser extent, tax-exempt funds saw meaningful redemptions in March 2020 as a result of the financial market's reactions to the coronavirus pandemic and government efforts to combat it.[4] We are therefore supportive of the SEC's efforts to consider potential policy measures to improve the resilience of MMFs and short-term funding markets in the United States. We have considered each of the options set forth in the PWG Report, as well as additional ideas. To aid in our evaluation of policy options, we also

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[1] J.P. Morgan Asset Management is a marketing name for the investment management subsidiaries of JPMorgan.

[2] Request for Comment on Potential Money Market Fund Reform Measures in President's Working Group, Release No. IC-34188 (Feb. 4, 2021), 86 Fed. Reg. 8938 (Feb. 20, 2021).

[3] Report of the President's Working Group on Financial Markets: Overview of Recent Events and Potential Reform Options for Money Market Funds, Dec. 2020, available at https://home.treasury.gov/system/files/136/PWG-MMF-report-final-Dec-2020.pdf.

[4] These market forces have been well explored elsewhere. *See, e.g.,* "The Impact of COVID-19 on Economies and the Financial Markets," Report of the COVID-19 Market Impact Working Group, ICI, October 2020, available at https://www.ici.org/pdf/20_rpt_covid1.pdf; Financial Stability Board, "Holistic Review of the March Market Turmoil," Nov. 17, 2020, available at https://www.fsb.org/wp-content/uploads/P171120-2.pdf.

conducted an informal survey of our largest clients to understand their considerations for managing their MMF holdings during the March volatility.

We believe that a number of incremental changes to Rule 2a-7 under the Investment Company Act of 1940, building on the SEC's prior reforms to MMFs in 2010 and 2014, can substantially enhance the resilience of MMFs while preserving the important role they play as intermediators of short-term borrowers and lenders. Conversely, we are concerned that some of the more far-reaching options under consideration could make prime and tax-exempt MMFs undesirable to investors and/or not cost-effective for sponsors to offer, which could have knock-on impacts to the financial markets globally.

Below we provide a perspective on the importance of MMFs to the US markets; review the impacts of previous MMF reforms; describe JPMAM's experiences during March 2020; summarize feedback received from our clients; and offer observations on other areas of the short-term markets that bear examination. We then suggest incremental changes to Rule 2a-7 to enhance the resilience of prime and tax-exempt MMFs. Our recommendations include:

- Remove the tie between a MMF's weekly liquid assets (WLA) and the obligation for a board to consider imposing a fee or gate;
- Impose corrective requirements when MMFs fall below 30 percent WLA, to incentivize MMFs to maintain at least 30 percent WLA in the ordinary course while making it easier for them to utilize the WLA buffer when market conditions dictate; and
- Require MMFs to develop detailed policies and procedures that identify the circumstances under which a board should implement redemption fees (*i.e.,* a "playbook").

Finally, we review the other options set forth in the PWG Report and explain why we do not support them.

I. Background

a. The Role of Money Market Funds in US Financial Markets

The US financial market is the broadest, deepest, and most efficient in the world. Its equity market represents approximately 40 percent of global capitalization,[5] and approximately 40 percent of the international debt market is denominated in US dollars.[6] For public or private entities looking to

[5] US market capitalization represented by portion of Bloomberg World Exchange Market Capitalization Index, as of Dec. 31, 2020.

[6] Bank for International Settlements, Summary of debt settlements outstanding by residence and sector of issuer, available at https://stats.bis.org/statx/srs/table/c1; Bloomberg Barclays Multiverse Index as of Dec. 31, 2020.

raise funds for equity, debt or trade finance, the United States offers the largest and most accessible supply of capital. MMFs play an important role in the functioning of the US financial market and the global economy.

Liquidity is critical to the efficient functioning of the market. Liquidity provides rapid price discovery and lowers transaction costs, which in turn facilitates trade. Virtually all international wholesale banks utilize the United States as their secondary market (their home country is typically their primary market). At year-end 2020, these international banks had approximately $1.1 trillion in dollar-denominated commercial paper (CP) and certificates of deposit (CDs) outstanding,[7] much of it held by prime MMFs. Absent this funding, these banks would be compelled to use central bank swap lines to hedge currency risk, or else reduce their lending and investing in dollar-denominated US assets (*e.g.,* corporate and municipal loans or US treasuries), which would reduce dollar-based liquidity.

With $918 billion in assets under management (AUM) and investing nearly $500 billion into the $1.6 trillion short-term credit securities market[8] at YE 2020, prime MMFs provide a substantial source of liquidity for the US dollar-denominated markets. In addition to funding international banks' dollar loan and investment books, they are an important access point for industrial companies,[9] allowing highly rated companies to raise billions in funds swiftly and cheaply.

As an investment option, prime MMFs serve as an alternative to bank deposits for cash investors who value the same-day liquidity, diversification, and returns these funds offer. Banks frequently position MMFs with deposit customers as a means to help manage their balance sheets more effectively. Providing an alternative to deposits is likely to be even more important following the expiration, on March 31, 2021, of temporary changes to the Federal Reserve's supplementary leverage ratio rule (SLR) made during the crisis. The temporary relief had made it easier for banks to absorb substantial deposit growth driven by unprecedented monetary and fiscal expansion. With its expiration, banks may need to turn away customer deposits, or retain earnings or issue securities to raise additional capital.[10] Prime MMFs will play an important role in absorbing and redirecting these assets. If these assets migrated solely to Government MMFs, the modestly negative interest rates seen today in the markets for repurchase agreements and treasuries would become more

[7] JP Morgan Commercial Paper Credit Market Update, Q4 2020.

[8] In addition to the $1.1 trillion in CP and CDs issued by international banks, US banks and non-financial companies issue approximately $500B in short-term credit.

[9] JP Morgan Commercial Paper Credit Market Update, Q4 2020.

[10] *See, e.g.,* Peter Coy, "Jamie Dimon May Soon Turn Away Deposits, and He's Not Happy," *Bloomberg Businessweek,* Mar. 22, 2021 (quoting JP Morgan Chase & Co. Chief Executive Officer Jamie Dimon's comments, prior to the Federal Reserve's announcement, that if the temporary provisions expired, the bank would have a financial incentive to turn away deposits, and noting that the bank had reduced deposits by $200 billion within months after a previous change to the SLR).

pervasive, which would necessitate further Fed action to keep short-term markets liquid and rates in the desired band (and not negative).

Municipal issuers such as schools, hospitals, and highway administrations also rely heavily on the short-term markets. When long-term rates are high, short-term borrowing allows municipal issuers to benefit from a lower cost of capital for infrastructure projects. In many cases, municipal issuers need to access the short-term market as temporary financing to begin infrastructure projects while they put overall project financing in place. This is a particularly useful tool for municipalities when the revenues from the financed project will help service the debt. Short-term borrowing for annual cash flow needs also allows municipal issuers to plan for the natural timing mismatch between revenues (*e.g.*, property taxes) and expenditures. As of June 2020, tax-exempt (municipal) MMFs held approximately 45 percent of outstanding short-term municipal debt ($114 billion)—which included $88 billion in variable rate demand notes (VRDNs) and tender option bonds; prime and government MMFs held another $17 billion.[11]

b. The Impact of 2010 and 2014 Money Market Fund Reforms

As the PWG Report observes, following the 2008 financial crisis the SEC implemented reforms to MMFs in 2010 and 2014 to make MMFs more resilient to credit and liquidity stresses. These reforms included reducing credit, liquidity and interest rate risk in MMF portfolios; requiring portfolio stress testing; enhancing transparency into portfolio holdings; requiring institutional prime and municipal MMFs to operate with a floating net asset value (NAV), and permitting MMF boards to consider imposing liquidity (redemption) fees and/or suspending redemptions ("gating" a fund) at specified portfolio liquidity levels.

Taken together, these reforms substantially enhanced the structural integrity of MMFs, and reduced the risk they might transmit to the broader financial system. Since the implementation of the 2010 reforms, numerous credit, liquidity and interest rate volatility events have impacted MMFs. The multi-year Eurozone sovereign debt crisis and the US debt limit crisis and resulting downgrade of the US Government credit rating in 2011, for example, directly impacted issuers in the short-term markets as well as flows into MMFs. Prime MMFs were significantly exposed to Eurozone credits at the onset of credit stress in the region, but the 120 day limitation on Weighted Average Life (WAL), introduced in 2010, limited the impact of widening bank and financial credit spreads and helped position Prime MMFs with more liquid portfolio maturity structures. The 30 percent WLA requirement ensured robust liquidity levels to meet client redemptions as some chose to exit funds with exposures to certain issuers and countries.

[11] *See* Investment Company Institute, Report of the COVID-19 Market Impact Working Group, Experiences of US Money Market Funds during the COVID-19 Crisis, Nov. 2020, available at https://www.ici.org/pdf/20_rpt_covid3.pdf at 6 ("ICI MMF Report").

In addition, the tighter parameters on second tier issuers introduced in the 2010 reforms helped to constrain and shorten prime MMF exposures to the particularly troubled issuers and regions in the Eurozone (*e.g.*, Portugal, Ireland, Spain). Portfolio holdings disclosure enhancements brought transparency to the Prime MMF industry that was highly valued by MMF customers eager to understand Eurozone exposures in the funds they owned. The 2010 rule changes also helped ensure that funds were well-positioned for the eventual migration of assets from prime to government MMFs in 2016, following the 2014 reforms. Finally, the segregation of retail and institutional assets in 2014 effectively insulated retail investors from the heavier outflows in institutional MMFs in March 2020.

In our view, however, one element of the 2014 reforms was particularly problematic in the recent crisis: the provision that MMF boards may consider imposing redemption fees and/or gates if a fund's WLA falls below 30 percent. In creating this "bright line," the 2014 reforms essentially nullified the intended benefit of the 30 percent WLA minimum.

As the 2010 Adopting Release explained, the WLA requirement was meant to ensure that "a fund should be able to use those assets to pay redeeming shareholders even in market conditions (such as those that occurred in September and October 2008) in which money market funds cannot rely on a secondary or dealer market to provide immediate liquidity."[12] Although the 2014 amendments made clear that such a move is optional and at the discretion of the board,[13] we understand that in response to the 2014 amendments many clients implemented daily monitoring of MMF liquidity levels, and now treat the 30 percent level as a "floor" rather than a buffer.[14] Redemption data from

[12] Money Market Fund Reform, Final Rule, SEC Release No. IC-29132 (Feb. 23, 2010) at 57, 75 Fed. Reg. 10060, 10076 (Mar. 4, 2010).

[13] "If, at any time, the money market fund has invested less than thirty percent of its total assets in weekly liquid assets, the fund *may* institute a liquidity fee…if the fund's board of directors, including a majority of the directors who are not interested persons of the fund, determines that the fee or suspension of redemptions is in the best interests of the fund." Rule 2a-7(c)(2)(i) (*emphasis added*).

[14] Indeed, a number of commenters, including JPMAM, raised this concern during the comment period for the 2014 amendments. *See, e.g.,* Letter from John T. Donohue, Chief Investment Officer and Head of Global Liquidity, J.P. Morgan Asset Management, to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, dated Sept. 17, 2013, available at *https://www.sec.gov/comments/s7-03-13/s70313-156.pdf* at 2 ("A specific trigger that requires board action may cause investors to redeem as a MMF gets close to the trigger, which may accelerate the run that gates and liquidity fees are designed to prevent."). The adopting release explained the Commission's view that allowing the board to exercise discretion "should mitigate the risk of pre-emptive redemptions." Money Market Fund Reform; Amendments to Form PF, Final Rule, SEC Release Nos. 33-9616, IA-3879, IC-31166 (July 23, 2014) at 60, 79 Fed. Reg. 47736, 47753 (Aug 14, 2014) ("2014 Adopting Release").

March 2020,[15] as well as our informal client survey and related discussions with clients,[16] confirm that clients perceived this 30 percent threshold as a "bright line" to be avoided. As discussed in more detail below, clients' concern about a breach of the 30 percent WLA influenced our trading decisions (and those of other MMFs), likely exacerbating the March 2020 market stress.

c. Events of March 2020; JPMAM experience

In contrast to the 2007-08 global financial crisis, which unfolded over 15 months prior to Lehman's failure, the March 2020 market chaos came suddenly. China recorded its first Covid-19 death on January 11; the World Health Organization declared a pandemic on March 11, and much of the developed world—including the United States—shut down concurrently. In the face of the cash flow uncertainty precipitated by the shutdown, many companies – even those on strong financial footing – accumulated as much cash as they could by drawing down credit lines, issuing debt, selling marketable securities, and redeeming from MMFs. Commercial and industrial loans in the United States grew by 21 percent during March, from $2.36 billion to $2.86 billion, while institutional prime MMFs saw AUM decline by $116 billion—nearly 20 percent.[17]

Fortunately, short-term credit remained strong despite a poor industrial outlook, because the cash credit markets are largely comprised of bank debt. Banks spent the past eleven years building capital and reducing their reliance on wholesale funding, and the banking sector entered the pandemic in the best possible fiscal health. Thus, the challenge in this crisis was not creditworthiness, but rather market liquidity.

Nonetheless, investor demand for cash required prime MMFs to raise liquidity. As noted above, this need was magnified by concerns about funds falling below the 30 percent WLA buffer. Rather than rely on those assets to meet redemptions, prime MMFs sought to sell longer-dated commercial paper and certificates of deposit in the secondary markets. Two MMF sponsors even purchased securities from their prime MMFs to ensure that the funds' WLA remained above 30 percent.[18]

Dealers, meanwhile, were limited in the amount of such instruments they could intermediate, due to the lack of buyers and balance sheet constraints. Moreover, as clients redeemed from prime MMFs, these MMFs necessarily limited purchases to overnight instruments to manage their own liquidity, constraining credit and curtailing liquidity for issuers trying to roll or raise short-term debt.

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[15] *See* ICI MMF Report, *supra* note 11, at 30-35 (showing that prime funds whose WLA fell below 35 percent experienced significantly higher outflows than those with higher WLA).

[16] *See infra* §I.d. for a summary of our client survey.

[17] Federal Reserve H8 data available for download at: https://www.federalreserve.gov/releases/h8/20200410/.

[18] ICI MMF Report, *supra* note 11, at note 66 and accompanying text.

Like other MMFs, JPMAM's institutional prime and municipal MMFs experienced significant outflows in March 2020. During the period of March 9th through March 30th, our institutional prime MMF experienced a 31 percent decline in AUM; our US dollar offshore prime MMF saw a similar decline (29 percent). While we typically manage these funds to maintain a WLA of 40 percent or greater, during March our WLA fell as low as 35 percent. We determined that under the circumstances it was in the best interests of these funds and their shareholders to maintain our WLA at or above 35 percent. To accomplish this while meeting investor redemptions, we sold longer-dated (non-WLA) instruments such as CP and CDs. In spite of the high credit quality and short duration of these positions, we took significant loses on many of our sales in the secondary market. This selling, together with similar activity from other market participants, created further downward pressure on the prices of these securities, despite their creditworthiness.

d. JPMAM client feedback on March 2020

To help us assess the impact of previous and potential future changes to MMFs, we conducted an informal survey of JPMAM clients with substantial holdings in our institutional prime MMF. We received responses from about 25 percent of those surveyed. Approximately 35 percent of the respondents reported redeeming more than 25 percent of their balance in prime MMFs during March 2020. Our survey attempted to identify these investors' reasons for redeeming and, where there were multiple reasons, to assess the relative importance of each.

Sixty percent of these investors (*i.e.,* those who redeemed more than 25 percent of their holdings) identified the potential imposition of fees and gates as one primary reason for redeeming; this was by far the most heavily selected option. Approximately 45 percent identified general risk reduction or declining NAVs as additional reasons. And finally, when respondents were asked to assign a level of importance from 0 to 5 to a range of factors affecting their decisions to redeem, the potential for gates to be implemented received the highest average score (4.43). Investment risk and declining NAV were next (4.0), followed by the potential for fees (3.71).

e. Observations on the short-term markets

While we recognize the need to examine the resilience of MMFs following the experiences of March 2020, it is important to note that the challenges were not isolated to prime and tax-exempt MMFs. As market participants demanded cash, a number of market forces, some of them self-perpetuating, caused liquidity to tighten. We urge the SEC and other regulators to consider whether modifications elsewhere in the short-term market ecosystem are warranted.

For example, as noted above, dealers were limited in their ability to intermediate trading in short-term, high-credit-quality assets in March 2020, due to the volume of assets being sold relative to the size of dealer balance sheet capacity. The supplementary leverage ratio (SLR) and liquidity coverage ratio (LCR) calculations have been frequently cited by market participants as factors limiting bank participation.[19] While these standards clearly enhanced the stability of the banking sector, as evidenced by banks' resilience during March, the constraints banks faced in deploying that capital and liquidity during times of market stress limited their ability to alleviate volatility in March. These calculations could be reexamined with the goals of maintaining banks' resilience while enhancing their ability to intermediate during times of crisis.

As an alternative to altering the SLR or LCR calculations, policy makers could consider changes to their crisis management toolkit to make it easier and less balance sheet intensive for primary dealers to facilitate liquidity in secondary markets during liquidity stress events that are not credit-driven. For example, the Primary Dealer Credit Facility (PDCF) would have likely stemmed the need for launching the Commercial Paper Funding Facility (CPFF) and Money Market Mutual Fund Liquidity Facility (MMLF) if the PDCF had been structured with the balance sheet neutrality (no risk-weighted capital or leverage capital charges) of the MMLF. A swift uptake in usage of the PDCF to add liquidity to short-term debt markets would have been beneficial to all holders and issuers of such instruments (not just MMFs).

Some market participants have also suggested enhancements to the market infrastructure for CP and other high-credit-quality short-term debt.[20] These markets are currently highly dependent on dealer intermediation. Given limited balance sheet capacity and risk management limits adapted to the prevailing market conditions, when dealers did bid on these assets, they frequently did so at substantial discounts; those prices then were applied in vendor pricing models that are used by MMFs and other market participants, driving asset prices down further. Taking steps to enhance liquidity in this market could have the dual benefit of adding buyers and improving vendor pricing, thereby reducing "panic" selling.

Another factor driving a liquidity shortfall during March was the margin required by derivatives central counterparties (CCPs), particularly for exchange-traded derivatives.[21] While CCPs generally remained resilient, it became apparent in March that their initial margin (IM) models were excessively procyclical. As a result, the period of market volatility triggered a significant number and

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[19] *See, e.g.,* BlackRock Viewpoint, "Lessons from COVID-19: Market Structure Underlies Interconnectedness of the Financial Market Ecosystem," Nov. 2020, available at https://www.blackrock.com/corporate/literature/whitepaper/viewpoint-lessons-from-covid-19-market-structure-november-2020.pdf, at 11; ICI MMF Report, *supra* note 11, at 20.

[20] *See, e.g.,* BlackRock Viewpoint, "Lessons from COVID-19: US Short-Term Money Markets," July 2020, available at https://www.blackrock.com/corporate/literature/whitepaper/viewpoint-lessons-from-covid-19-us-short-term-money-markets-july-2020.pdf.

[21] *See* Securities and Exchange Commission, Division of Economic and Risk Analysis, "U.S. Credit Markets Interconnectedness and the Effects of the COVID-19 Economic Shock," Oct. 2020, available at https://www.sec.gov/files/US-Credit-Markets_COVID-19_Report.pdf, at 27 (observing that "incremental IM is a net drain of liquidity from the markets into CCPs").

magnitude of IM breaches and subsequent IM increases, creating a procyclical demand for cash by derivatives market participants;[22] much of this cash was held in MMFs. We understand that global standard-setters including IOSCO, CPMI and BCBS are examining margin dynamics and we are supportive of this work; a key focus should be on whether enhancements are required to the anti-procyclicality measures within CCPs' margin models.

It is important to note that, while we would support further discussion of these potential changes, we do not believe that any of the proposed market structure changes in isolation would have alleviated the liquidity challenges faced by MMFs in March 2020. We now turn to our recommendations for prime and tax-exempt MMFs.

II. Potential policy measures to increase the resilience of prime MMFs – JPMAM recommendations

JPMAM believes that the redemption pressure experienced by prime and tax-exempt MMFs in March 2020 was driven primarily by two factors in addition to cash flow uncertainty as a result of the economic shutdown. First and foremost, we believe investors were concerned about the possibility of gates being imposed as MMFs' WLA approached 30 percent. Secondly, some investors were concerned about deteriorating market conditions and declining prices, causing them to seek to stem losses.

Based on these observations, we recommend 1) de-linking the 30 percent WLA threshold from the obligation for boards to consider imposing fees and/or gates; 2) revising the consequences for breaching the 30 percent WLA threshold; and 3) modifying redemption fees to facilitate their use, when appropriate, to compensate remaining investors for declining prices caused by redeeming investors. Each of these is discussed in more detail below.

a. Removing the tie between MMF liquidity and fee and gate thresholds

As discussed above,[23] clients perceived the 30 percent WLA buffer as a "bright line" not to be crossed, and were particularly concerned about the risk of gates. To avoid falling below the 30 percent threshold while meeting investor redemptions, JPMAM, like other MMF sponsors, sold assets into the secondary market, creating further downward pressure on the prices of those assets and exacerbating stresses in both the secondary markets and on MMFs specifically. This clearly runs

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[22] *See, e.g.,* Bank for International Settlements, "The CCP-bank nexus in the time of Covid-19," BIS Bulletin No. 13, May 11, 2020, available at https://www.bis.org/publ/bisbull13.pdf (discussing the effects of procyclicality in margining).

[23] *See supra* §I.d; notes 15-16 and accompanying text.

counter to the SEC's intention that the 30 percent WLA serve as a mechanism to ensure redemptions are met during stressed markets.[24]

We therefore recommend that the SEC revise or delete section (c)(2)(i) of Rule 2a-7 to remove the reference to the 30 percent WLA threshold. The Commission could provide the fund's board of directors with the discretion to impose gates at any time if they deem it in the best interest of the fund. Alternatively, we note that Rule 22e-3 under the Investment Company Act permits a MMF to suspend redemptions under limited circumstances in order to facilitate the orderly liquidation of the fund.[25] Given MMF investors' strong aversion to gates, we believe a MMF that imposed a gate would ultimately need to liquidate in any event; therefore, eliminating broader board discretion regarding the imposition of gates from Rule 2a-7 and relying on the existing framework in Rule 22e-3 may be sufficient.

To address the concern that this approach could cause MMFs to maintain inadequate WLA levels, in the next section we recommend alternative consequences for falling below 30 percent WLA. We also recommend modifications to the application of redemption fees to make them more effective.

b. Revising the consequences for breaching the 30 percent WLA threshold

As the PWG Report observes, removing the tie between the WLA threshold and the consideration of fees and gates could lead MMFs to maintain lower levels of liquid assets, leaving them less equipped to manage redemptions should market stresses arise. We believe the ideal approach would create strong incentives for a fund to maintain liquidity safely above the 30 percent threshold in the ordinary course, while making it possible for a MMF to fall below the threshold to meet redemptions in times of stress, so as to avoid selling into a stressed market. This approach is conceptually similar to countercyclical WLA requirements, while avoiding the risk of incentivizing preemptive redemptions by investors.[26]

We believe the existing transparency requirements provide strong incentives to maintain a WLA in excess of 30 percent, even without a link to board consideration of fees and gates. Nonetheless, the SEC could strengthen these incentives by requiring a MMF to overcorrect if it fell below the 30 percent threshold. For example, a fund could be prohibited from acquiring securities other than WLA until its WLA was repaired to 35 percent. A fund could also be required to report to the SEC, as well as the board, if it breaches this level; repeated breaches would presumably draw scrutiny

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[24] *See supra* note 12 and accompanying text.

[25] Under this rule, a MMF may suspend redemptions in order to effect an orderly liquidation if WLA has fallen below 10 percent or, for a stable NAV fund, the price rounded to the nearest one percent has deviated from the stable price established by the board, and the board has approved the liquidation of the fund.

[26] *See infra* §III.c.

from both.[27] Taken together, these measures would incentivize a fund to manage above the 30 percent threshold whenever possible, while not being so punitive as to cause a fund to sell less liquid assets into a stressed market to avoid a breach.

c. Modifying redemption fees

Although not specifically explored by the PWG Report, one potential reform option that we believe merits consideration is a modification to redemption fees. Under the current rules, fees are treated as essentially interchangeable from gates in the first instance, *i.e.,* as an option for boards to consider when a MMF breaches the 30 percent WLA. At 10 percent WLA, when a liquidity fee is required unless the board determines otherwise, fees become a blunt instrument to disincentivize redemptions and recoup liquidity costs. We believe a more nuanced approach to fees could be beneficial, drawing on certain elements of swing pricing.[28]

As a preliminary matter, we observe that fees are a more tolerable intervention than gates, from an investors' perspective.[29] Investors in institutional prime MMFs, which have floating NAVs, clearly recognize that these funds do not maintain a stable value, and that they may experience a loss if they redeem at a NAV lower than when they subscribed. By contrast, gates deny clients access to their cash, which is highly problematic when a client has cash flow demands. Thus, it is worth considering an approach to fees as a remediation tool separate from, and to be used earlier than, gates. Importantly, we believe the existence of such a tool could be useful in educating clients away from viewing the 30 percent WLA as a bright line.

Moreover, while fees in the current rules are somewhat arbitrary,[30] we believe there is an opportunity to incorporate a framework similar to that used for swing pricing, to make fees more dynamic and reflective of the true cost of liquidity to those demanding it. Such an approach is likely to be more palatable to investors than a static 1 or 2 percent fee, imposed at the board's discretion. And, while swing pricing as currently used by mutual funds is operationally infeasible and conceptually

[27] In our experience, the board monitors our management of WLA closely; we expect that violations of the 30 percent threshold other than in times of market stress would draw scrutiny, and repeated violations would likely be raised during the board's annual evaluation of the investment adviser under Section 15(c) of the Investment Company Act of 1940.

[28] As discussed below, *infra* §III.e., we believe swing pricing as currently used by mutual funds is not workable for MMFs.

[29] *See* §I.d (JPMAM clients ranked the risk of gates as substantially more influential than fees in their decision to redeem assets in March 2020).

[30] While the board retains discretion to adjust the default liquidity fee under current rules, there is little specific guidance as to how they might do so.

problematic for MMFs,[31] MMFs have already built an operational framework for the implementation of fees.[32]

We therefore recommend that the SEC consider requiring funds to maintain detailed policies and procedures (*i.e.,* a "playbook"), reviewable by the SEC, that provide the board with clear direction on when to impose redemption fees and how to calculate them. We believe MMF sponsors are better positioned than boards to assess both when a fee should be imposed, and the right level of the fee; and further, that it is preferable to conduct this analysis ahead of time and have a decision tree prepared for the board, rather than expecting the board to make difficult determinations during periods of market stress.[33] While we envision that the playbook would provide clear direction to the board on when to act, we expect the board would retain the discretion to decline imposing a fee if it found that doing so was not in the best interest of shareholders.

If the SEC were to take this approach, it could provide a non-binding list of suggested factors to consider, similar to those provided in the 2014 Adopting Release.[34] For example, in considering when to impose a fee, a fund might consider a multi-factor approach,[35] including factors such as net redemptions (single day, rolling average, cumulative, or other); WLA and other portfolio-specific characteristics (investor concentration, diversification of holdings, etc.); and market-based liquidity metrics (*i.e.,* indications that non-WLA might not be readily sold). Similarly, a fund might look to such liquidity metrics to determine how much the fee should be. The fee could be adjusted up or down daily based on market conditions (assuming the test for imposing a fee continues to be met).

Finally, the SEC must carefully consider the appropriate disclosure to clients regarding the fee. Ideally, clients would understand the fee sufficiently to accept the risk, while not having enough information to attempt to redeem preemptively (before a fee was imposed). Fund sponsors' swing

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[31] *See infra* §III.e.

[32] We acknowledge that fees continue to present operational challenges. However, unlike swing pricing, which would impose such challenges on a daily basis, the approach we are proposing would only be implicated in distressed market conditions, and so would permit intraday redemptions in the ordinary course.

[33] We also would not support a "dictate" approach, whereby the SEC or other external party would determine when MMFs should impose fees. Not all funds are managed the same; what may necessitate a fee in one fund may not be the case in others. Additionally, such an approach could create moral hazard, if funds knew that risky management on their part would result in the entire industry being penalized.

[34] *See* 2014 Adopting Release at 90-91.

[35] In Europe, low volatility NAV (LVNAV) fund boards must consider gates using a 2-factor approach: 1) WLA falls below 30 percent, *and* 2) net redemptions exceed 10 percent of the fund's AUM in one day.

pricing disclosures for Luxembourg-based UCITS, which provide a general description of the approach and factors considered, could serve as a useful template.[36]

III. Analysis of other recommendations set forth in PWG report

JPMAM's primary recommendations for enhancements to MMFs incorporate elements of several measures set forth in the PWG Report, most notably those addressing gates (removal of tie between MMF liquidity and fee and gate thresholds, and reform of conditions for imposing redemption gates). While we also incorporated elements of countercyclical WLA and swing pricing in our recommendations, we do not recommend their adoption as described in the PWG Report. Below we share our reservations with respect to these and other options.

a. Minimum balance at risk

Under a minimum balance at risk (MBR) approach, a portion of each shareholder's MMF shares would be available for redemption only with a time delay; in the event the fund experienced losses during the period after an investor redeemed but within the holdback period, that investor would still share in those losses through a reduction in value of the holdback. Such an approach would create enormous operational challenges for MMFs, and would likely substantially decrease the desirability of these funds for investors. Further, to the extent investors did remain, we believe such an approach could actually create a heightened level of restlessness among investors, who might seek to anticipate the market scenarios that could cause them to lose their MBR, and exit the funds at the earliest signs of distress. For these reasons, we do not support the MBR.

From an operational perspective, MBRs would require significant structural changes to MMFs, which would be costly and challenging to implement. Specifically, transfer agents would need to develop technology that could compute and reset average account balances, and restrict applicable shares in investor accounts that are held direct at funds and through financial intermediaries. MBR data would also need to be integrated in transfer agent recordkeeping systems, shareholder servicing interfaces, and transaction processing, as well as for other servicing interfaces utilized by clients.

Moreover, we believe that an MBR approach would dramatically reduce the appeal of MMFs to investors. Investors use MMFs in large part because they are deemed a "cash equivalent" under US

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[36] *See, e.g.,* Swing pricing: The J.P. Morgan Asset Management approach in the Luxembourg domiciled SICAVs JPMorgan Funds and JPMorgan Investment Funds, Sept. 23, 2020, available at https://am.jpmorgan.com/content/dam/jpm-am-aem/emea/lu/en/communications/lux-communication/swing-pricing-ce-en.pdf (explaining how swing pricing works and listing generally the factors considered in determining the appropriate level of the swing factor); *see also* Franklin Templeton, Investor Education, Swing Pricing, available at https://www.franklintempleton.lu/investor/resources/investor-tools/swing-pricing.

generally accepted accounting principles.[37] An MBR holdback could call that designation into question. Fiduciaries such as retirement plans, trustees, and investment advisers may be legally prohibited from using MMFs with these embedded redemption restrictions for their clients; similarly, sweep programs, which rely upon the ability to move all investors' cash on daily basis, would not be able to leverage MMFs with MBR guidelines. To the extent investors did elect to remain in MMFs that employed an MBR, we believe these investors might seek to anticipate market stress and redeem before an MBR holdback was declared.

b. MMF liquidity management changes

Another option presented in the PWG Report is to add additional liquidity requirements to the existing daily and weekly requirements, such as a category of "biweekly liquid assets," or potentially an extra band of WLA (*e.g.,* an additional 10 percent) that carries a lesser consequence for breach. As discussed above, we support maintenance of the 30 percent WLA requirement, and further recommend that, if that level is breached, a MMF should have to cure back up to 35 percent. We do not, however, support adding another band of liquidity requirements.

Requiring a band of biweekly liquid assets makes intuitive sense as a way of ensuring a more even distribution of maturities ("laddering"). However, MMFs typically already hold assets with a well-distributed range of maturities, with longer-dated positions constantly rolling down towards maturity. Moreover, there is a very limited issuance market for assets in the biweekly maturity range, nor do we expect that new demand from MMFs would enhance issuance, because such offerings are not desirable from an issuer's perspective.

Most short-term credit instruments purchased by MMFs are issued by banks, which are subject to strict liquidity requirements. The Liquidity Coverage Ratio (LCR), which requires banks to maintain sufficient assets to meet outflows over a 30 day stressed period, creates incentives for banks to issue longer-dated securities. Conversely, instruments that mature within 30 days count *against* their LCR. Given that banks would therefore be unlikely to issue securities with this duration, the only meaningful way to acquire them would be in the secondary market (*i.e.,* by purchasing longer-dated issuance that is nearing maturity), which we expect would inflate the price of these securities, ultimately causing them to provide no more yield than overnight or weekly assets. Moreover, these biweekly assets would roll into the WLA bucket after a week, creating continual pressure to source new biweekly assets.

[37] Under these principles, cash equivalents are "short-term, highly liquid investments that are readily convertible to known amounts of cash and that are so near their maturity that they present insignificant risk of changes in value because of changes in interest rates."

Ultimately, we expect that MMFs would meet a biweekly requirement by simply increasing their WLA, implicating the alternative suggestion in the PWG Report – an additional band of WLA. We believe this would create unnecessary complication and confusion. JPMAM institutional clients pay close attention to our WLA levels. As discussed above, investor concern about gates led to acceleration of redemptions as WLAs declined.[38] Adding a biweekly liquid asset requirement, and therefore another potential decision point for clients, would simply increase the complexity of MMF reporting and client monitoring, with no additional benefit.

Finally, perhaps the simplest approach would be to simply raise the existing WLA minimum. As reflected in our recommendations, we do not believe that the challenges MMFs encountered were caused by insufficient WLA, but rather by a practical inability to use those assets to meet redemptions due to investor fears about gates.[39] Thus, increasing the WLA seems unnecessary; and doing so without de-linking the threshold from the risk of fees and gates could actually increase the risks to MMFs, by causing investors to consider preemptive redemptions even earlier.

c. Countercyclical weekly liquid asset requirements

The concept of countercyclical WLA requirements was embedded in the SEC's 2010 reforms. As discussed above,[40] the SEC intended that funds would use WLA assets to meet redemptions when conditions in the secondary markets have deteriorated. We agree with this approach, and our recommendations in Sections II.a-b are designed to facilitate the use of WLA in such circumstances while preserving the 30 percent minimum in the ordinary course.

The PWG Report, however, takes the concept of countercyclical requirements a step further, suggesting that WLA requirements could decline automatically in certain circumstances or when the SEC provides temporary relief. We are concerned that such an approach would create a new "bright line" that would signal market stress to MMF investors and other market participants, potentially increasing redemption activity. Additionally, it is unclear how the trigger would be established, monitored and, if necessary, invoked. We believe the same beneficial result, *i.e.,* MMFs using their WLA buffer to meet redemptions during times of stress, will occur if gates and fees are not linked to the 30 percent threshold, *i.e.,* if MMFs do not risk accelerated redemptions as they approach 30 percent due to investor fear of gates or fees.

[38] *See supra* §I.d; notes 15-16 and accompanying text.

[39] *See supra* §I.b-c.

[40] *See supra* note 12 and accompanying text.

d. Floating NAVs for all prime and tax-exempt MMFs

Another option set forth in the PWG Report is to require retail prime and tax-exempt MMFs, which currently may be offered at a stable NAV, to instead use a floating NAV. We recognize that doing so could be beneficial by reducing a potential first mover advantage caused by shares being sold for more than they are worth. As the PWG Report indicates, however, outflows in these funds were substantially lower than in institutional funds. This suggests that retail investors were not actually capitalizing on any such advantage; meanwhile, the outflows from institutional funds demonstrates that floating NAVs do not prevent runs.

Moreover, requiring retail prime and tax-exempt MMFs to float their NAVs would likely substantially reduce the desirability of these funds, as retail investors expect them to maintain a stable NAV. Additionally, a substantial proportion of JPMAM's AUM in tax-exempt and retail prime funds are held in sweeps. Rather than making the technological and operational changes to facilitate the sweep of client cash balances at a variable NAV, we believe that most retail sweeps would be redirected to government MMFs. While this would not represent a material change to returns for end retail investors in the current interest rate environment, there could be a meaningful impact to returns (and the tax efficiency of those returns) over the long run as rates normalize. In addition, this migration of assets would be problematic for issuers of short-term municipal securities, for which tax-exempt MMFs are the primary buyer.[41]

e. Swing pricing

JPMAM employs swing pricing on the vast majority of our Luxembourg- and UK-domiciled long-term (non-MMF) UCITS funds, and we have been supportive of the SEC's efforts to encourage the use of swing pricing in mutual funds in the US.[42] As discussed above,[43] certain elements of swing pricing can and should inform how we might reimagine redemption fees for MMFs. In particular, the swing factor, which is a dynamic adjustment to the cost to an investor of selling fund shares, and is designed to impose transaction costs experienced by the fund on the redeeming investor, could translate into a fee. However, swing pricing itself, as currently employed in Europe, does not make sense for MMFs for several reasons.

As a preliminary matter, the concept of a swing threshold is not meaningful for MMFs. A swing threshold is the level of net flows at which a fund would determine to swing the NAV (*e.g.*, a fund

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[41] *See supra* note 11 and accompanying text.

[42] *See, e.g.,* Letter from George C.W. Gatch, CEO- Global Funds Management & Institutional, J.P. Morgan Asset Management, to Brent Fields, Secretary, Securities and Exchange Commission, dated Jan. 13, 2016, available at https://www.sec.gov/comments/s7-16-15/s71615-67.pdf (supporting the SEC's proposal to permit US-registered mutual funds to employ swing pricing).

[43] *See supra* §II.c.

might swing the NAV if a fund experiences a net 5 percent inflow or outflow). This makes sense in the context of long-term funds, because while such funds typically maintain some cash and overnight assets with which to meet redemptions, a larger flow will require transactions in the underlying portfolio, imposing the costs swing pricing is intended to address.

MMFs, on the other hand, routinely hold substantial amounts of short-term and maturing assets, and regularly see predictable, high levels of inflows and outflows (*e.g.,* at month and quarter end); indeed, JPMAM maintains a "cash flow calendar" that tracks expected subscriptions and redemptions, with input from client-facing representatives, to assist in cash flow management. Moreover, given the short duration of MMF assets generally, portfolio managers can plan for these redemptions by allowing portfolio assets to mature, rather than transacting in the secondary market. Thus, tying the execution of a NAV adjustment to net flows, as with swing pricing, does not make sense.

Additionally, to assess daily net flows for purposes of determining whether the swing threshold has been met, MMFs would likely need to suspend intraday settlement, a feature of MMFs that is highly valued by investors. Same-day settlement (once per day) could also be compromised. This is because all daily flows must be received, and the NAV calculated, before a price can be swung, meaning that intra-day pricing could not incorporate a swing. The end-of day operational process would also likely take several hours,[44] so unless a fund stopped accepting transactions early (*i.e.,* before 4 p.m.), it would be unlikely to meet the 6:45 p.m. Fedwire deadline for same-day settlement.

Finally, we expect sweep platforms would experience significant operational complexities with swing pricing. Certain types of sweep products such as round-trip sweeps would not be able to invest in a MMF that settled on a T+1 basis. Additionally, cash and cash equivalent status, a coveted feature for corporate treasury investors, could be impacted if settlement were to shift to T+1 from T+0.

f. Capital buffer requirements

Under a capital buffer approach, MMF sponsors would be required to hold assets alongside a fund to absorb losses. In the past, discretionary use of sponsor capital has been effective in preventing idiosyncratic credit risk in a fund from causing broader issues in MMFs and/or the short-term funding markets. In addition to reducing transmission risk from MMFs, requiring sponsors to hold capital could further incentivize them to minimize portfolio risks. However, meaningful capital buffers are costly to finance, and in the current low rate environment would take a substantial amount of time to accumulate. As the PWG Report observes, the cost of such an approach would likely drive further industry consolidation, and could potentially make prime MMFs economically unviable even for the largest managers. We therefore do not support this approach.

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[44] Based on JPMAM's use of swing pricing in Luxembourg, we estimate this process would take at least 3 hours.

Indeed, contrary to the PWG's hypothesis that a capital requirement may favor bank-sponsored funds, we believe the cost of capital would quickly become prohibitive for JPMAM. Additionally, if the capital buffer were to trigger applicable accounting rules requiring consolidation of MMFs onto the sponsor's financial statements, many MMF sponsors – especially bank-affiliated sponsors – would likely find it cost-prohibitive to offer MMFs.

g. Require liquidity exchange bank membership

The concept of a liquidity facility or liquidity exchange bank (LEB) for MMFs received strong industry attention and support after the 2008 financial crisis, including from JPMAM.[45] The existence of a liquidity backstop could provide investors with assurance that liquidity will be available when needed, potentially reducing preemptive redemptions. This effect would be even more pronounced if the LEB had accesses to the Federal Reserve liquidity through the discount window.

However, further exploration of the LEB concept exposed substantial challenges. As a preliminary matter, the regulatory requirements associated with establishing such a facility would be extremely complex. Perhaps more importantly, as a stand-alone facility (*i.e.,* without access to the discount window), the LEB would struggle to raise capital from its members (MMFs) in a timely fashion. Even once fully capitalized at the same ratio proposed in 2011 (1.3 percent of prime assets),[46] such a facility would have only had a nominal ability to absorb assets in March 2020. At this ratio, the LEB would have held approximately $12B; in order to maintain a consistent WLA against shrinking AUM,[47] prime MMFs needed to raise an additional $100B in WLA during March 2020.

An LEB could have a more meaningful impact if it were able to borrow from the Federal Reserve. Again looking at the 2011 proposal, if it were capitalized at the same ratio today and could leverage that capital, the LEB would have had a capacity of approximately 3.3 percent of prime AUM, or $30B. However, this still represents only about one third of the non-WLA sold by prime MMFs in 2021. To the extent any permissible policy option could implicate borrowing from the Fed in times

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[45] *See, e.g.,* Letter from George C.W. Gatch, Chief Executive Officer, IM Americas, J.P. Morgan Asset Management, to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, dated Jan. 10, 2011, available at https://www.sec.gov/comments/4-619/4619-45.pdf ("We believe that the Liquidity Facility is the best single option presented in the Report to address the objective of further mitigating the risk of runs on money market funds…"). *See also* Letter from Paul Schott Stevens, Investment Company Institute, to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, dated Jan. 10, 2011, available at https://www.sec.gov/comments/4-619/4619-49.pdf.

[46] *See* Letter form Paul Schott Stevens, *supra* note 45, at Appendix p. 18 (showing notes and equity of approximately $24B against $1.65T in prime AUM).

[47] AUM in prime MMFs declined from $1.1T at YE2019 to $936B Mar. 31, 2020.

of stress, we would observe that the MMLF, which has now been utilized twice to great effect, could achieve a similar outcome with far less cost and complication.[48]

h. New requirements governing sponsor support

The PWG report observed that in times of stress, sponsor support has been a tool for stabilizing MMF share prices and providing liquidity. It noted, however, that the discretionary nature of sponsor support contributes to uncertainty about who will bear risks in periods of stress. While this is true, JPMAM does not support explicit requirements regarding sponsor support.

Requiring sponsor support raises many of the same challenges as capital buffers. Indeed, as a bank-affiliated MMF sponsor, we expect that JPMAM would be required to hold capital against any potential support obligation. As discussed above, the cost of capital could be prohibitive, causing sponsors to exit the market, and resulting in increased concentration among remaining MMF sponsors. Meanwhile, the funds that remain could be incentivized to take on additional risk, both to recoup the cost of capital and because they could rely on sponsor support as a backstop, creating moral hazard.

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JPMAM appreciates the opportunity to comment on the PWG Report. We would be pleased to provide any further information or respond to any questions that the Commission or the staff may have.

Very truly yours,

/s/ John T. Donohue

John T. Donohue
CEO, Americas

Cc: The Honorable Allison H. Lee, Acting Chair
The Honorable Hester M. Peirce, Commissioner
The Honorable Elad L. Roisman, Commissioner
The Honorable Caroline A. Crenshaw, Commissioner
Sarah ten Siethoff, Acting Director, Division of Investment Management

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[48] At its peak, the MMLF had $53B outstanding. *See* Daleep Singh, "The Fed's Emergency Facilities: Usage, Impact, and Early Lessons," Federal Reserve Bank of NY, July 8, 2020, at exhibit 7.7, available at https://www.newyorkfed.org/medialibrary/media/newsevents/speeches/2020/sin200708/Singh_HVPP_exhibits_7.7.pdf.