



Wells Fargo & Company



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April 12, 2021

***Via email to: rule-comments@sec.gov***

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

**RE: File No. S7-01-21—Request for Comment on Potential Money Market Fund Reform Measures in President’s Working Group Report**

Dear Ms. Countryman:

On behalf of Wells Fargo & Company and its subsidiaries, Wells Fargo Funds Management, LLC (“Funds Management”) appreciates the opportunity to respond to the request by the U.S. Securities and Exchange Commission (“Commission” or “SEC”) for comments on potential money market fund (“MMF”) reform measures, as outlined in a recent report of the President’s Working Group on Financial Markets (“PWG”).<sup>1</sup>

Funds Management serves as the investment manager to the Wells Fargo Funds®. Our fund family offers a diverse set of government, prime and tax-exempt MMFs across multiple distribution platforms that include retail and institutional investors (“Wells Fargo Money Market Funds”). Assets under management in the Wells Fargo Money Market Funds totaled approximately \$194 billion as of March 31, 2021. In managing the Wells Fargo Money Market Funds, we emphasize conservative investment choices and make preservation of capital and liquidity our highest priority.

## **I. Introduction**

Despite the MMF reforms adopted by the Commission in 2010 and 2014 in response to the 2008 global financial crisis, prime and tax-exempt MMFs experienced stresses in March of 2020 as market disruptions caused by the novel coronavirus (“COVID-19”) pandemic led to significant outflows, particularly from institutional prime MMFs. As such funds experienced heavy redemptions, their weekly liquid asset (“WLA”) levels declined, and some funds’ WLA levels approached (and one fell below) the 30% minimum threshold established by Rule 2a-7 under the Investment Company Act of 1940, as amended (the “1940 Act”), which led to more investor redemptions as

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<sup>1</sup> Request for Comment on Potential Money Market Fund Reform Measures in President’s Working Group Report, Investment Company Act Release No. 34188 (February 4, 2021); President’s Working Group on Financial Markets: Report on Recent Events and Potential Reform Options for Money Market Funds (December 2020), *available at* <https://home.treasury.gov/system/files/136/PWG-MMF-report-final-Dec-2020.pdf> (“PWG Report”).

institutional investors feared that MMF boards would impose liquidity fees and/or redemption gates.<sup>2</sup> Due to stresses in the short-term funding markets, which pre-dated the heavy redemptions from MMFs, prime MMFs faced challenges selling securities, notably commercial paper and CDs, to accommodate investors' redemptions, which exacerbated the problem as WLA levels further declined.

On March 18, 2020, the U.S. Board of Governors of the Federal Reserve System ("Fed"), with the approval of the Secretary of the Treasury, authorized the Money Market Mutual Fund Liquidity Facility ("MMLF"), which provided non-recourse loans to U.S. depository institutions and bank holding companies to finance their purchases of specified eligible assets from MMFs under certain conditions. Following the announcement of the MMLF, prime and tax-exempt MMF outflows subsided and short-term funding market conditions improved.

We think it important to note that prime and tax-exempt MMFs functioned largely as intended following the reforms of 2010 and 2014; specifically, the floating net asset value ("FNAV") requirement for institutional MMFs provided the price discovery that reforms intended to produce, while ensuring shareholders bore the cost of their liquidity needs. However, the events of March 2020 demonstrated that, despite the FNAV, such funds may still be susceptible to "runs." While the runs experienced during the 2008 global financial crisis were precipitated by credit events, March 2020 demonstrated that runs may also be caused by liquidity events, as investors, particularly institutional investors, became concerned that redemption gates would be imposed and that they would be subsequently unable to access their money for a period of time. These investor concerns likely were fueled by the perception that permitting funds the *option* of imposing liquidity fees and redemption gates if their WLAs fell below the minimum 30% threshold was a *requirement* that they do so. In this sense, the 2014 reforms, which were in large part enacted in order to reduce the risk of runs, may have simply swapped one kind of trigger event for another, as a fund's WLA level replaced a fund's shadow NAV as the trigger which causes institutional investors to redeem. We believe that this phenomenon illustrates that it may be more challenging, if not impossible, to solve for or eliminate run risks entirely. Rather, regulators and the industry should focus on solutions which mitigate redemption risk as much as possible, while ensuring that any additional reforms that are introduced do not threaten the viability of prime and tax-exempt MMFs in the future or impose unnecessary operating costs on MMF sponsors. Properly functioning short-term markets are important for economic growth; they provide a means for companies, municipalities, and the Federal government to finance short term needs. Prime and tax-exempt MMFs are an important tool in providing that financing, and any goal of regulatory reform should be undertaken with a view to ensuring such MMFs can continue to operate in an effective manner.

Following the March 2020 market dislocations, regulators have increasingly focused on the necessity of reforming "structural vulnerabilities that can create or transmit stress in short-term funding markets."<sup>3</sup> When discussing the impact of the events of March 2020 on MMFs, and what actions should be taken as a result, we think it is important to keep in mind the significant differences between March 2020 and the events of the 2008 global financial crisis, which precipitated the last two rounds of MMF reform in 2010 and 2014. While it is true that the patterns of prime and tax-exempt MMFs' flows on a percentage basis during both crises were similar,<sup>4</sup> the reasons for such heavy redemptions were very different. The global financial crisis of 2008 was a credit crisis, as money market investors, spooked by the bankruptcy filing of Lehman Brothers and other events such as the "breaking of the buck" by the Reserve Primary Fund, began to question the creditworthiness of various money

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<sup>2</sup> See Investment Company Institute, "Experiences of US Money Market Funds during the COVID-19 Crisis", *Report of the COVID-19 Market Impact Working Group* (November 2020) at 30-34, available at [https://www.ici.org/pdf/20\\_rpt\\_covid3.pdf](https://www.ici.org/pdf/20_rpt_covid3.pdf) ("ICI Report").

<sup>3</sup> PWG Report at 4.

<sup>4</sup> PWG Report at 14-15; ICI Report at 17.

market instruments held by MMFs and whether other funds would also ultimately “break the buck.” This led to credit-related runs as investors sought a first-mover advantage in redeeming their shares. The problems were exacerbated by a breakdown in the commercial paper market also caused by the default of Lehman Brothers and the subsequent inability of issuers to roll over maturing commercial paper. In contrast, the dislocations in March 2020 were a liquidity event caused by a flight to liquidity and quality by all investors as they raced to raise funds in the face of the uncertainty presented by the pandemic and lockdowns. Many markets, not just the money markets, were impaired, including equity, bond, Treasury and currency markets. With respect to the short-term funding markets, unlike 2008, the immediate creditworthiness of commercial paper and CD issuers was not a concern, as banks, which are the primary issuers of commercial paper held by prime MMFs, were well-capitalized and far stronger than they previously had been as a result of banking reform.<sup>5</sup> Rather, the stress in the short-term financial markets and the eventual freeze was instead due in part to market structure, which we note, is an issue that cannot be addressed through MMF reform. We therefore believe that any additional changes to the structure of MMFs should be narrow in scope, and tailored specifically to address the issues experienced in March 2020.

**a. Scope of Comments**

In our comments, we do not intend to address all potential policy measures highlighted in the PWG report. In our view, some measures do not address either the functioning of short-term markets or enhance the operation of FNAV MMFs; examples of such measures would be liquidity buffers, the minimum balance at risk, FNAVs for all prime and tax-exempt MMFs, and capital buffers. Other measures, such as swing pricing, a liquidity exchange bank, and new guidelines regarding sponsor support, in our view, present financial, operational, or regulatory challenges that would make them unworkable. With respect to the potential policy measures noted above, we participated in the development of and largely support the comments and recommendations made by the Investment Company Institute (“ICI”) in its comment letter.<sup>6</sup>

We intend to focus our comments on three potential policy measures highlighted in the PWG report, namely (1) the removal of the tie between MMF liquidity and fee and gate thresholds, which we would support, (2) MMF liquidity management changes, which we would not support, and (3) countercyclical weekly liquid asset requirements, which we would not support.

**II. Potential Policy Measures from the Report of the President’s Working Group**

**a. Removal of the Tie between MMF Liquidity and Fee and Gate Thresholds**

In its February 23, 2010 release of its final rule amendments to Rule 2a-7 under the 1940 Act, the SEC stated that it was adopting the requirement for MMFs to hold 30% of their assets in securities maturing or puttable within one week (*i.e.*, WLA) in order to provide MMFs “a sufficient degree of liquidity necessary to meet reasonably foreseeable redemption requests and reduce the likelihood that a fund will have to meet redemptions by selling portfolio securities into a declining market.”<sup>7</sup> The Commission further noted that this liquidity threshold was estimated to have been sufficient for “approximately 90 percent of retail and institutional funds [to] satisfy the level of redemption demands during individual days as well as the week of greatest redemption pressure in the

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<sup>5</sup> ICI Report at 19.

<sup>6</sup> See Comment Letter of Investment Company Institute, *available at* <https://www.sec.gov/comments/s7-01-21/s70121.htm> (“ICI Comment Letter”).

<sup>7</sup> Money Market Fund Reform, Investment Company Act Release No. 29132 (February 23, 2010) at 49-50 (“2010 Final Rule”).

fall of 2008 (September 15-19).<sup>8</sup> Indeed, this new liquidity threshold was likely sufficient to satisfy the level of redemption demands during the events of March 2020 as well. According to data from Form N-MFP, for the 2-week period ended March 20, 2020, outflows from institutional prime funds totaled \$90 billion, or approximately 27% of the assets of such funds.<sup>9</sup> We believe that maturing securities and putting variable rate demand notes (which qualify for the WLA bucket) were sufficient to allow our institutional prime and tax-exempt Wells Fargo Money Market Funds to satisfy their redemption requests during March 2020. Given industry averages, we believe that this was likely the case for most other MMFs as well.

Despite MMFs having sufficient levels of WLAs to meet redemption requests during the market dislocations of March 2020, MMFs, including the Wells Fargo MMFs, were hesitant or unwilling to use this liquidity. This is because of certain unintended consequences from the 2014 amendments to Rule 2a-7 requiring a fund board to consider the option of imposing liquidity fees or redemption gates, if the fund drops below the WLA minimum threshold, to stem a run on funds. Specifically, the amendments seemingly had the effect of transferring the trigger event of the first-mover advantage for redeeming shareholders from the \$1.00 stable NAV to the WLA minimum threshold, incenting shareholders to redeem in times of market stress before fees or gates could be imposed by the funds and before shareholders' ability to liquidate their positions in the funds could be impaired.<sup>10</sup> This effectively precluded fund managers from using weekly fund liquidity to meet redemption requests due to fears that a drop in WLA, causing the fund to approach the 30% WLA level, would lead to even greater or accelerated redemption requests. Indeed, as noted in the ICI Comment Letter, rather than let their funds' WLA levels drop below 30%, two fund sponsors purchased securities from three of their respective affiliated institutional prime MMFs so as to avoid the uncertainty associated with dropping below this threshold.<sup>11</sup>

While we believe that a fund's ability to impose fees and gates can serve as an important tool that should be preserved, we support delinking the permissible imposition of fees and gates from the WLA minimum threshold and instead providing a fund board with the ability to impose fees or gates when doing so is in the best interests of the fund, without reference to any specific threshold, in the exercise of the board's business judgment consistent with its fiduciary duty to the fund. We note that the Commission, in the release adopting the 2014 amendments to Rule 2a-7, stated that, "given the role of independent directors, a fund's board is in the best position to determine whether a fee or gate is in the best interests of the fund."<sup>12</sup> The Commission also stated that the 1940 Act and the rules thereunder "require many other fund fees and important matters to be approved by a fund's board, including a majority of independent directors, and we do not believe that liquidity fees and redemption gates should be treated differently."<sup>13</sup> Many, if not most, of these "other fund fees and important matters" are not tied to bright-line regulatory thresholds.

Under this reform, it is possible that a subset of institutional investors may still regard the 30% WLA level as a type of "floor" that causes them to redeem when a fund's WLA approaches this level out of fear that the fund's board may decide to impose fees or gates. However, we believe this reform would reduce the incentive for a large percentage of shareholders to engage in pre-emptive runs, as well as increase market liquidity without impacting the overall size and functioning of short-term markets. Accordingly, on balance, we believe the benefits of this reform would significantly outweigh any potential downsides and this reform could materially improve the

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<sup>8</sup> 2010 Final Rule at 63.

<sup>9</sup> PWG Report at 14 n.21.

<sup>10</sup> See ICI Report at 30-31; ICI Comment Letter.

<sup>11</sup> *Id.*

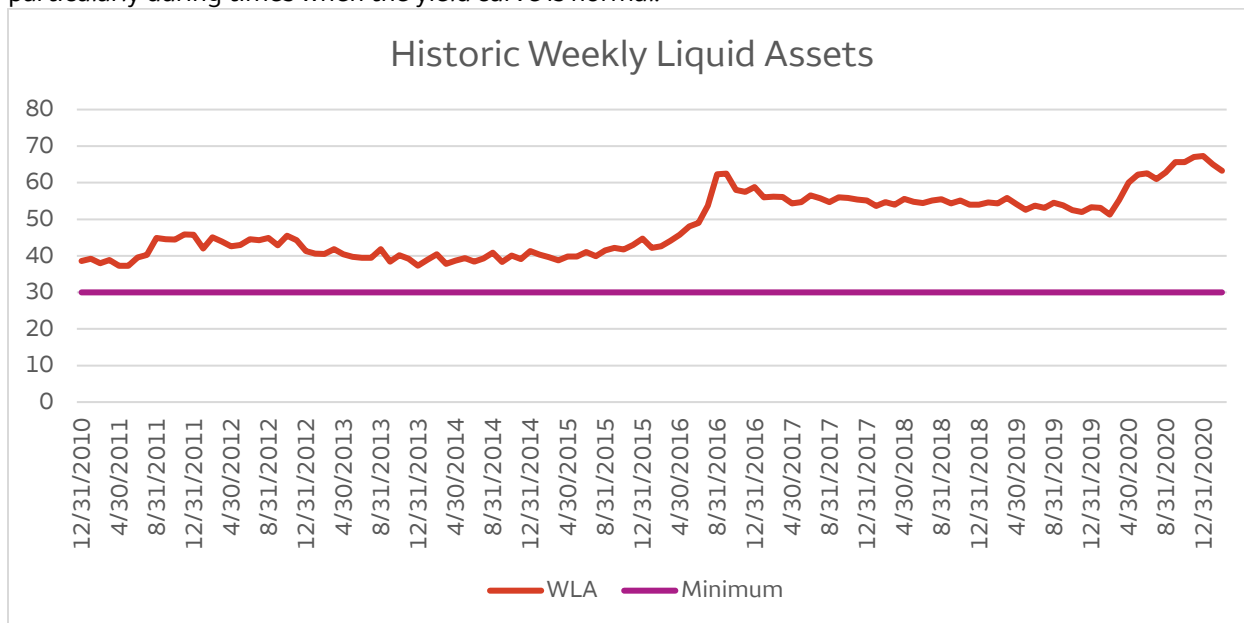
<sup>12</sup> Money Market Fund Reform; Amendments to Form PF, Investment Company Act Release No. 31166 (July 23, 2014) at 94.

<sup>13</sup> *Id.*

functioning of MMFs should a similar liquidity event happen in the future. It could also be easily implemented within the existing regulatory framework.

**b. Money Market Fund Liquidity Management Changes**

We do not support either an increase in the level of the WLA minimum threshold, or a requirement for an additional layer of liquid assets with a slightly longer maturity profile, such as biweekly liquid assets. Absent a decoupling of fees and gates considerations from the WLA threshold, these changes might enhance the liquidity *profile* of a MMF, but would not enhance actual liquidity because, as discussed above, managers likely would be unwilling or unable to use it during periods similar to March 2020. Even if paired with a decoupling of fees and gates considerations from the WLA threshold, however, we do not believe these changes would be advisable. First, with respect to biweekly liquid assets, as the ICI notes in its comment letter, commercial paper, which comprises a large portion of prime MMF portfolios, is not issued with 14-day maturities, so MMFs could only meet a biweekly requirement by purchasing longer-dated securities and letting them mature into a two-week bucket.<sup>14</sup> Even if such issuance existed, a biweekly liquid asset requirement or an increase in the minimum level of a fund’s WLA would have added no benefit during the March 2020 market dislocations. As noted above, during the two-week period ended March 20, 2020, the WLA levels of prime institutional MMFs exceeded the current WLA thresholds and were sufficient to allow such MMFs to meet total outflows during this period. Furthermore, as illustrated in the chart below, prime MMFs<sup>15</sup> historically have held WLAs in excess of the 30% minimum threshold, so mandating a higher level is unnecessary. While prime MMFs as a whole often have held a higher percentage of WLAs than the minimum regulatory threshold, mandating a higher level absent a compelling justification would unfairly restrict the flexibility that individual MMFs may wish to employ, such as, for example, carrying levels of liquidity tailored to the volatility profile of the shareholder base, or to take advantage of investment opportunities, particularly during times when the yield curve is normal.



<sup>14</sup> ICI Comment Letter.

<sup>15</sup> The chart shown includes both retail and institutional prime WLA levels prior to the implementation of the 2014 MMF reforms. Periods shown following 10/31/16 are WLA levels only for institutional prime MMFs.

*Source: Money Market Fund Statistics: Form N-MFP data, 12/31/10 – 12/31/20, Division of Investment Management Analytics Office, <https://www.sec.gov/divisions/investment/mmf-statistics.shtml>*

**c. Countercyclical Weekly Liquid Asset Requirements**

We believe the introduction of countercyclical WLA requirements is both unnecessary and counterproductive. Rule 2a-7 already contains remedial steps that MMFs and their managers must take in the event a fund's WLA level falls below 30%. As a stand-alone reform measure, countercyclical WLA requirements are unlikely to be effective because, just as with requiring increased WLA levels, requiring specific levels of liquidity that are tied to levels of redemptions would not be helpful if managers are unwilling or unable to access this liquidity, which will only happen if WLA levels are decoupled from fee and gate thresholds. Furthermore, if WLA levels are decoupled from the fee and gate thresholds, then countercyclical WLA requirements will serve no purpose, as MMF managers would feel free to manage their MMFs below the 30% WLA threshold as necessary or appropriate.

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We appreciate the opportunity to provide comments on the potential MMF reform measures as outlined in the PWG report and welcome the Commission's consideration of our comments.

Very truly yours,

/s/ Andrew Owen  
Andrew Owen  
President  
Wells Fargo Funds Management, LLC