Federated Hermes

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October 26, 2022 (revised)

Director William Birdthistle
Division of Investment Management
Securities and Exchange Commission
100 F Street, NW
Washington, DC 20549

VIA EMAIL & OVERNIGHT MAIL

Re: Federated Hermes, Inc.'s Response to Comments of Director Birdthistle on the Proposed Amendment to Rule 2a-7 Requiring the Use of Swing Pricing in Institutional Prime and Tax-Exempt Money Market Funds (SEC File No. S7-22-21)

Dear Director Birdthistle:

We read with interest your July 26, 2022, remarks at the PLI Investment Management seminar[1] on swing pricing and the pending proposal the amend the rules governing money market funds ("MMFs") and wanted to respond on five key points.

First, your remarks reference swing pricing as something that is used in Europe. While your remarks did not suggest that European money market funds use swing pricing, because swing pricing is part of the aforementioned proposal, let me make it clear, European MMFs have never used swing pricing.[2] The use of swing pricing for MMFs is untested, unprecedented and its use would be an experimental application of this pricing methodology. This is an extremely important point that should not be glossed over in the pending MMF rulemaking. Application of this pricing methodology to MMFs for the first time would have unanticipated, costly, and disruptive results.[3] Your observation that "[w]hen some insist on moving fast and breaking things, sometimes that just leaves things broken" also applies to regulatory actions.

Second, you comment about how swing pricing will somehow "modernize" the money fund industry analogizing it to "vacuum tubes and reel to reel computing". First and foremost, there is no data supporting the need for swing pricing to deal with potential material dilution caused by redeeming shareholders.[4] The fact is that use of MMFs for cash management is an evolutionary leap over the days when, for example, bank trust departments, manually rolled T-bills on a monthly basis and wheeled carts filled with pass books from the trust department to the savings and loan down the street at the end of each day to invest cash in order to earn an extra quarter point of interest for their clients or, worse, left cash uninvested at the end of the day. MMFs greatly simplified cash management, not only for bank trust departments but for institutional investors as well. For individuals, MMFs gave investors a true market rate of return rather than an administered rate from a bank. Today, MMF portals ensure that investors can access a range of money market funds multiple times a day and earn a market rate of return on their cash

[1] https://www.sec.gov/news/speech/birdthistle-remarks-pli-investment-management-2022-072622
[2] Comment Letter of EFAMA (Mar. 23, 2022), https://www.sec.gov/comments/s7-22-21/s72221-20121032-273211.pdf.
[3] Comment Letter of Investment Company Institute (Apr. 11, 2022), https://www.sec.gov/comments/s7-22-21/s72221-20123254-279522.pdf; Comment Letters of Federated Hermes, Inc. (Apr. 11, 2022), https://www.sec.gov/comments/s7-22-21/s72221-20123730-279989.pdf, https://www.sec.gov/comments/s7-22-21/s72221-20123456-279701.pdf.
[4] SEC, Proposed Rule, Money Market Fund Reforms, SEC Rel. No. IC-34441 (Dec. 15, 2021) at 185, 87 Fed. Reg. 7248, 7303 (Feb. 8, 2022).

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which at times may be significantly higher than what is available on deposit products. The Commission's proposed "experiment" with swing pricing would potentially turn the clock back with institutions re-creating their old cash management departments and/or capital markets desks. It could also result investors being forced to use deposit products while watching inflation erode the value of their savings.

Third, you also repeat the long-discredited Paul Volcker apocrypha that attributes the existence and growth of MMFs to Federal Reserve Regulation Q. While MMFs did get their start when interest on deposits was subject to Regulation Q, as with most of the Federal Reserve's mythology around MMFs, this is one rooted in a non-linear view of time. Regulation Q, under which price competition in the banking industry for deposits was forbidden and consumers were forced for 50 years to subsidize banks through below-market returns on deposited cash, was repealed in stages more than forty years ago by the Depository Institutions Deregulation and Monetary Control Act of 1980 (the "DIDMCA").[5] Almost all of the growth of MMFs occurred after the enactment and implementation of the DIDMCA.[6] The last vestige of Regulation Q (forbidding the payment of interest on demand deposit accounts owned by businesses) was repealed in 2010 as part of the Dodd-Frank Act. Regulation Q clearly did not cause MMFs to succeed and grow.

Fourth, you further state that the "Commission has a responsibility to protect for financial stability and to increase the resilience of our financial system." These are the statutory responsibility of the Federal Reserve and are not among the statutory directives to the Commission in conducting a rulemaking under the Investment Company Act. If the Commission chooses those as its basis for a rulemaking it would run afoul of the "major questions doctrine" in a review of the agency's action.[7] The statutory directive to the Commission is instead to consider the impact of the rulemaking on competition, investor protection, capital raising and market efficiency.[8] Adopting a rule that will reduce competition for cash balances, harm investors, negatively impact capital raising and impede market efficiency, would be clearly contrary to the statutory directive.

Fifth, your remarks repeat the Federal Reserve's demonstrably false lines that MMFs caused the Financial Crises of 2007-2009 and March-April 2020, are inherently unstable, and are tantamount to "shadow banks," to which we have responded at length multiple times earlier in this and prior Rule 2a-7 rulemaking processes.[9] In fact, from the Financial Crisis Inquiry Commission Report,[10] to the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (which did not call for amendments to MMF regulation or identify MMF as a cause of the 2007-2009 Financial Crisis), to the myriad books and

[5] P.L. 96-221 (1980).
[6] As of December 31, 1980, immediately after the repeal of Regulation Q, MMFs aggregated to approximately $76 billion in assets, and after that repeal was fully phased in on December 31, 1986, aggregated to approximately $292 billion in assets. As of December 31, 2021, MMFs aggregated to approximately $5 trillion in assets. See FRED Economic Data, Federal Reserve Bank of St. Louis, Money Market Funds, Total Financial Assets, Level.
[7] *West Virginia v EPA, U.S Slip Op. 20-1530* (June 30, 2022).
[8] Investment Company Act Sections 1, 2, 6(c), 38; Securities Act of 1933 Sections 2(b), 3; Securities Exchange Act of 1934 Section 3(f).
[9] See, e.g., Two Comment Letters of Federated Hermes (Apr. 11, 2022), https://www.sec.gov/comments/s7-22-21/s72221-20123456-279701.pdf; https://www.sec.gov/comments/s7-22-21/s72221-20123730-279989.pdf.
[10] Financial Crisis Inquiry Committee, Financial Crisis Inquiry Report (Jan. 2011), https://www.govinfo.gov/content/pkg/GPO-FCIC/pdf/GPO-FCIC.pdf.

countless articles that have been written divining the causes of the Financial Crisis,[11] numerous culprits have been identified, including subprime mortgage leading, the Federal Reserve's accommodative monetary policy, the related housing market bubble, inadequate oversight of broker/dealer leverage, and inadequate disclosure of financial risk of certain financial institutions. Very few sources mention MMFs, except to identify the impact of the ensuing panic caused by these other culprits. The same is true for the March 2020 Crisis which was set off as investors reacted to the government shutdowns in response to pandemic.[12]

A rulemaking by the Commission must be based on analysis of the facts and data in the rulemaking docket, not the Federal Reserve's mythology of MMFs, and the final rules must be grounded in the statutory directives in the Investment Company Act, not on policy goals drawn from outside the federal securities laws.

Respectfully,

Peter J. Germain
Chief Legal Officer

Cc: Chair Gary Gensler
Commissioner Hester M. Peirce
Commissioner Caroline A. Crenshaw
Commissioner Mark T. Uyeda
Commissioner Jaime Lizarraga
Secretary Vanessa Countryman

[11] Erin Coghlan, Lisa McCorkell and Sara Hinkley, What Really Caused the Great Recession?, University of California Berkeley Institute for Research on Labor and Employment (Sep. 19, 2018), https://irle.berkeley.edu/what-really-caused-the-great-recession/; John Weinberg, the Federal Reserve Bank of Richmond, The Great Recission and its Aftermath (Nov. 22, 2013), https://www.federalreservehistory.org/essays/great-recession-and-its-aftermath; https://www.sec.gov/comments/s7-01-21/s70121-8662821-235311.pdf; Martha L. Cochran, David F. Freeman & Helen Mayer Clark, Money Market Fund Reform: SEC Rulemaking in the FSOC Era, 2015 Colum. Bus. L. Rev. 861.

[12] ICI, A Study of the Performance of Money Market Funds and the Short-term Funding Markets During March 2020 (Apr. 29, 2021), https://www.ici.org/system/files/2021-05/21mmfroundtablesummary.pdf; ICI, Report of the COVID-19 Market Impact Working Group: Experiences of US Money Market Funds During the COVID-19 Crisis (Nov. 2020), https://www.ici.org/doc-server/pdf%3A20_rpt_covid3.pdf; Comment Letter of Federated Hermes Inc. on Presidents Working Group Report on MMFs at pp 7-18 (Apr. 12, 2021).