

# Regulatory Alert

Regulatory Insights for Financial Services

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## SEC Money Market Fund Reforms & Customer Protection Rule Proposal

### *KPMG Insight:*

- *Final rule and rule proposal closely align with the SEC's broader efforts to improve the resilience of financial markets and decrease financial stability risks during periods of market stress.*
- *Money market fund reforms are substantially the same as previously proposed except the SEC did not adopt the proposed swing pricing requirement but rather adopted a liquidity fee framework. The final reforms are wide-ranging—encompassing liquidity requirements, fees, and reporting requirements—and could have significant impacts on funds' operations.*
- *The separate proposal for carrying broker-dealers is similarly aimed at strengthening customer/investor protections, liquidity, and market stability in the event the broker-dealer fails.*

The SEC adopts [amendments](#) to certain rules under the Investment Company Act of 1940, including Rule 2a-7, that govern money market funds. Citing the susceptibility of these funds to heavy redemptions and a lack of liquidity in times of stress, the SEC states the amendments are intended to improve the resilience of money market funds. The final rules are substantially the same as previously proposed, except for the adoption of a liquidity fee framework rather than the proposed swing pricing requirement (see KPMG Regulatory Alert, [here](#).) In a related [statement](#), the SEC Chair said the switch was based on public feedback and that “liquidity fees, compared with swing pricing, offer the same benefits and fewer of the operational burdens.”

In a separate action, the SEC proposes [amendments](#) to the broker-dealer customer protection rule to require certain broker-dealers to compute their customer and broker-dealer reserve deposit requirements on a daily rather than weekly basis.

Highlights of each of the actions follow.

### **Money Market Fund Reforms**

**Redemption fees and gates.** With a goal of reducing the risk of investor runs during periods of market stress, the amendments to Rule 2a-7 will remove:

- The ability of money market funds to impose temporary gates to suspend redemptions.
- The regulatory tie that permits money market funds to impose liquidity fees if their weekly liquid assets fall below a certain threshold.

**Liquidity fees.** Rather than adopting the proposed swing pricing requirements, the SEC adopted a liquidity fee framework that is similarly designed to protect remaining fund shareholders from dilution and to “more fairly” allocate the costs from redemptions in stressed market conditions to the redeeming shareholders. The amendments will require:

- Institutional prime and institutional tax-exempt money market funds to impose mandatory liquidity fees when they experience daily net redemptions that exceed 5 percent of net assets unless the fund's liquidity costs are

de minimis (i.e., less than one basis point). The fee has no upper limit.

- Non-government money market funds (prime and tax-exempt money market funds) to impose a discretionary liquidity fee if a fund’s Board determines that a fee is in the best interest of the fund. The fee is limited to 2 percent of the value of the shares redeemed.

**Portfolio liquidity requirements.** Rule 2a-7 requires money market funds to hold at least 10 percent of their total assets in daily liquid assets and at least 30 percent in weekly liquid assets. The amendments, which are intended to better equip money market funds to manage redemptions by providing a more substantial buffer, increase the portfolio liquidity requirements to:

- At least 25 percent of total fund assets in daily liquid assets.
- At least 50 percent of total fund assets in weekly liquid assets.

**Negative interest rates.** The amendments also enable retail and government money market funds (or “stable NAV funds”) to handle a negative interest rate environment either by:

- Converting from a stable share price to a floating share price, or
- Reducing the number of shares outstanding to maintain a stable net asset value per share, subject to certain board determinations and disclosures to investors.

**Weighted average maturity and weighted average life.** The SEC, citing consistency across funds, also amended rule 2a-7 to specify standard calculations of “dollar-weighted average portfolio maturity” (WAM) and “dollar-weighted average life maturity” (WAL), which are key metrics in determining portfolio risk:

- Money market funds will be required to calculate WAM and WAL based on the percentage of each security’s market value in the portfolio.

**Reporting requirements.** The amendments also revise the reporting requirements for money market funds in:

- **Form N-CR:** In addition to current filing requirements when portfolio securities default or insolvency events occur, funds will be required to:
  - File, within one business day, when the fund’s daily or weekly liquid assets decline by more than 50 percent below regulatory minimums (i.e., 12.5 percent and 25 percent, respectively).

- Submit in structured data language.

— **Form N-MFP (Monthly Schedule of Portfolio Holdings):**

- New information will be required for:
  - *Shareholder concentrations:* In a change from the proposal, disclosure of names of beneficial owners will not be required; rather, disclosure of the *types* of beneficial or record owners who hold 5 percent or more of the relevant share class will be required. Types of owners include retail investors, non-financial corporations, pension plans, non-profits, state or local governments, registered investment companies, private funds, depository institutions, sovereign wealth funds, broker-dealers, insurance companies, and other.
  - *Shareholder composition:* Money market funds that are not government money market funds or retail money market funds must disclose the percentage of investors in various categories (e.g., non-financial corporations, pension plans, state or municipal government entities, non-profits).
  - *Prime money market funds’ selling activity:* Disclosure of the gross market value of portfolio securities a prime money market fund sold or disposed of during the reporting period.
  - *Liquidity fees:* In alignment with changes to the liquidity fee framework, disclosure of the date on which the liquidity fee was applied, the type of liquidity fee, and the amount of the liquidity fee applied by the fund. Additionally, the amendments remove existing reporting requirements on Form N-CR related to the application of liquidity fees.
  - *Share cancellation:* Disclosure, by stable NAV funds, about the use of share cancellation, including if share cancellation was used during the reporting period and, if so, the dollar value of shares cancelled, the number of shares cancelled, and the dates on which the fund used share cancellation.
- Other amendments address information about repurchase agreement transactions, daily reporting for certain data points, website postings, and identification of fund registrants and series.

- **Form PF:** Amendments to Form PF, the confidential reporting form for certain SEC-registered investment advisers to private funds, are applicable to “large liquidity fund advisers”, which the SEC states are generally SEC-registered investment advisers that advise at least one liquidity fund and manage, collectively with their related persons, at least \$1 billion in combined

liquidity fund and money market fund assets. The amended reporting requirements (see related KPMG Regulatory Alert, [here](#)) address:

- Operational information.
- Asset and portfolio information.
- Repo reporting.
- Subscriptions and redemptions.
- Financing information.
- Investor information.
- Disposition of portfolio securities.
- WAM and WAL.

owed to customers and to other broker-dealers (referred to as “PAB account holders”) from weekly to daily.

In particular, the proposal would require carrying broker-dealers with average total credits (generally the amount of cash owed to customers and to PAB account holders) of greater than or equal to \$250 million to compute the amounts required to be deposited in customers’ and PAB account holders’ reserve bank accounts on a daily basis, as of the close of the previous business day.

- Average total credits” would be defined as the arithmetic mean of the sum of total credits in the customer reserve computation and PAB reserve computation reported in the twelve most recently filed month-end FOCUS Reports.
- Compliance with the daily computation requirement would be required no later than six months after having average total credits that greater than or equal to \$250 million.
- A carrying broker-dealer performing daily computations, whose average total credits falls below the \$250 million threshold, could elect to perform weekly computations 60 calendar days after notifying its designated examining authority of the intended switch.

SEC states the proposal is intended to assist carrying broker-dealers in more dynamically matching the net cash owed with the amount on deposit in customers’ and PAB account holders’ reserve bank accounts and safeguarding those account by lessening the potential for large mismatches to build over time.

**Comment Period.** The public comment period on the proposal will remain open for sixty (60) days following publication on the SEC website, or thirty (30) days following publication in the Federal Register, whichever is longer.

**For more information**, please contact [Matt Giordano](#).

**Effective Date and Compliance Period.** The final amendments adopt a tiered approach to provide appropriate transition periods for affected funds.

- The effective date for amendments to Rules 2a-7 is sixty (60) days following publication in the Federal Register.
- The compliance date for the mandatory liquidity fee framework is twelve (12) months after the effective date of the amendments to Rule 2a-7. The discretionary liquidity fee framework is subject to a six (6)-month compliance date.
- The compliance date for the increased daily and weekly liquid asset minimum liquidity requirements is six (6) months after the effective date of the amendments to Rule 2a-7.
- The effective and compliance dates for amendments to Forms N-CR, N-MFP, and PF are June 11, 2024.

### Proposed Enhancements to Broker-Dealer Customer Protection Rule

In a separate action, the SEC also proposes [amendments](#) to Rule 15c3-3 (the Customer Protection Rule) that would require certain carrying broker-dealers (i.e., broker-dealers that maintain custody of customer securities and cash) to increase the frequency with which they compute the net cash

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