SFOF
LOOK TO THE STATES

May 27, 2022

Via Electronic Mail

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

Re: Money Market Fund Reforms, File No. S7-22-21

Dear Ms. Countryman:

This letter is to comment on the Commission's above-referenced proposal to again change Rule 2a-7, governing the operation of money market funds ("Proposal").[1]

The State Financial Officers Foundation has long sought to communicate the importance of money market funds ("MMFs") to capital markets and the economy generally; and particularly to providing financing capacity for state and local government.[2] In May 2016 testimony to the Securities subcommittee of the Senate Banking Committee that would prove remarkably prescient, then Idaho Treasurer Ron Crane (and now SFOF chairman emeritus) predicted that the Commission's 2014 rule (the "2014 Amendments"), implemented in October 2016, would trigger an exodus from prime and municipal funds.[3]

We defended MMFs in a comment letter on the December 2020 President's Working Group Report ("PWG Report").[4] Since then, inflation has exploded to a 40-year high. Thus, here, we challenge the pre-inflation, PWG Report context Chair Gensler set forth in his remarks at the

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[1] Money Market Fund Reforms, SEC, 87 Fed. Reg. 7248 (Feb. 8, 2022), available at https://www.govinfo.gov/content/pkg/FR-2022-02-08/pdf/2021-27532.pdf.

[2] To learn about the State Financial Officers Foundation or our members, please see our website at https://sfof.com/.

[3] *See Improving Communities' and Businesses' Access to Capital and Economic Development: Hearing Before the Secs., Ins., and Inv. Subcomm. of the S. Banking Comm.*, 114th Cong. (May 19, 2016), https://www.banking.senate.gov/hearings/sii-improving-communities-and-businesses-access-to-capital-and-economic-development .

[4] Letter from Derek Kreifels and Idaho Treasurer Ron Crane (ret.), State Financial Officers Foundation, to Vanessa Countryman, SEC, April 26, 2021, *available at* https://www.sec.gov/comments/s7-01-21/s70121-8716563-237021.pdf (the "SFOF Letter").

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SEC open meeting to approve the Proposal.[5] It is helpful to change the context for the Proposal in order to discern whether the prevailing President's Working Group narrative of the March 2020 government shutdown of the economy makes any sense. We would assert that in the context of a new Great Inflation, it does not.

Chair Gensler pointed to the $5 trillion of cash in MMFs and how, in March 2020, investors "ran" from MMFs seeking "first mover advantage", which is akin to campers fleeing from a "bear" of market instability. (The punchline is that the camper doesn't have to outrun the bear; just his fellow campers.) According to Chair Gensler, something needs to be done, because this is a recurrence of the 2008 Great Financial Crisis ("GFC") "run" from MMFs where Chair Gensler had a ringside seat as a charter member of the then newly created Financial Stability Oversight Council.

It's quite a different picture if you instead assess MMFs as part of the broader U.S. economy over time. Attached is a 16-year dashboard of the real, Main Street economy (as represented by GDP) that adds the Federal Reserve's ("Fed") monetary policy, Congress' fiscal policy, the banking system and interest rates, alongside MMFs.

The dashboard, through March 31, 2022, distills and organizes a tremendous amount of data depicting the economy since the eve of the GFC. One thing that jumps out at you, first and foremost, is the Fed's exponential money creation. The M2 money supply has more than tripled from $6.7 trillion to $21.8 trillion, up 224%. In 2005, the Fed's total assets were $852 billion or 6% of U.S. GDP. By March 31, 2022, total assets had increased more than 10-fold to $8.94 trillion or 37% of U.S. GDP. Look at the Fed's Quantitative Easing ("QE") alongside market interest rates over the past sixteen years.

In this context of the Fed's QE, side-by-side with rates, it's easy to see that the Fed hasn't allowed markets to function normally since Lehman Brothers ("Lehman"). The real narrative of those fourteen years is one of continuously administered markets.

Second, the dashboard clearly gives you the broader context of how the 2014 Amendments diminished MMFs. Chair Gensler begins his comments by calling MMFs a "crucial" nearly $5 trillion asset class. He said that MMFs have "grown" to be a "very important piece of investors how they manage cash (sic)" and that MMFs are "a key source of funding for business and governments." Chair Gensler noted that MMFs ("this $5 trillion dollars") competes with deposits in our banking system; and that the bank deposit numbers are $13 to $15 trillion.

The dashboard clearly shows, however, that Chair Gensler is misguided. While MMFs have grown somewhat in nominal terms, they have shrunk, dramatically, as a portion of the cash in the system since the 2014 Amendments. Contrary to Chair Gensler, total bank deposits, in fact,

[5] Video of the Open Meeting of the Securities and Exchange Commission to approve the Proposal (December 15, 2021) at https://www.youtube.com/watch?v=eTlf5fz_swU (Chair Gensler's remarks begin at the 1:51:03 time marker).

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exceed $18 trillion. Total domestic deposits have increased by $12 trillion since 2005. In other words, just the growth in bank deposits is more than two times the current total MMF assets.

Those MMF assets providing what Chair Gensler refers to as a "key source of funding for business and governments" – prime and municipal MMFs – have shrunk to approximately $500 billion over the same time that the combination of bank deposits and assets in U.S. government MMFs have grown to $22.8 trillion. The Fed oversees the U.S. banking system which used these new deposits to add nearly $4 trillion to its holdings of government securities and $3.8 trillion to its reserves stranded at the Fed. Thus, 67% of all new bank deposits over the past 16 years went to the Fed or government securities, rather than being employed in the real economy as would have been the case if the cash had been invested, instead, in prime and municipal MMFs.

Another surprising fact revealed in the dashboard is that, of the $18.4 trillion deposited in banks, $8.4 trillion is *uninsured*. Thus, the uninsured bank deposits in the system are almost 18 times the assets of prime and municipal MMFs. The amount of uninsured bank deposits has grown by over $6 trillion or 262% since 2005. In other words, just the growth in the amount of uninsured bank deposits exceeds the total assets of the "crucial MMF asset class."

Will uninsured bank depositors put on their running shoes at the first sign of trouble? At $8.4 trillion, (46% of all U.S. bank deposits), uninsured deposits are double the level of bank reserves at the Fed. If uninsured depositors flee the banking system, the banks may have to "run" on the Fed by withdrawing their reserves to make up the shortfall. At $8.4 trillion, uninsured deposits are nearly four times the level of bank equity capital ($2.25 trillion). With so little capital, is there a first mover advantage for uninsured depositors who "run"?

The reality is that, over the past sixteen years, the monetary order has been radically changed by the Fed's administering of an opioid, called "Quantitative Easing", to the real economy. In order to maximize this opioid's potency, the Fed has been intent on herding all the cash in the system into its banks.

Chair Mary Jo White's 2014 Amendments were enormously helpful to the Fed, enabling it to almost completely achieve its goal of eliminating the impediment of prime and municipal MMFs to using QE to administer markets. In 2014, Chair White sought to do the Fed's bidding. As Chair Gensler did at the open meeting to approve the Proposal, Chair White sought to create the backdrop of "enhancing the resiliency of MMFs during times of market stress." In fact, as you can see from the dashboard, the adoption of the 2014 Amendments against overwhelming opposing public comment, decimated prime and municipal MMFs.[6]

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[6] The SFOF Letter explains that because, in our free market system, investors can choose to buy products that meet their needs, the SEC effectively disabled prime and municipal (non-government) MMFs in 2014 by taking away their utility to investors. *See also*, Letter from Tyler Gellasch, Healthy Markets Association, to Vanessa Countryman, SEC, April 12, 2022, *available at* https://www.sec.gov/comments/s7-22-21/s72221-20123502-279717.pdf ; Letter from Colin Robertson, Northern Trust Asset Management, to Vanessa Countryman, SEC, Mar. 24, 2022, *available at* https://www.sec.gov/comments/s7-22-21/s72221-20121090-273263.pdf SFOF agrees with all the other commenters that swing pricing is an even more extreme poison pill for investors than mandatory redemption fees, and SFOF supports "de-linking" of required liquidity thresholds and mandatory

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At adoption of the 2014 Amendments, Republican Commissioner Dan Gallagher flipped to become Chair White's swing vote as he sought to divert attention from the SEC's (and his) responsibility for the market contagion triggered by the failure of Lehman.[7]

For the longest time, the Fed's QE opioid seemed to be a miracle drug. The Fed could just focus on ensuring robust asset markets, while seemingly disregarding the prospect of consumer price inflation ("CPI"). However, third, the dashboard shows you how QE has turned out to be the drug that is too good to be true. In the end, it did not work despite an ever-increasing dose. The Fed expanded the money supply two and a half times faster than the underlying economy. The

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redemption fees. However, even adopting de-linking without swing pricing will not make prime and municipal MMFs competitive with bank deposits and the U.S. government MMF (which continue to offer investors daily liquidity at par).

[7] One reason the SEC has submitted to the Fed's and PWG's narrative (as reiterated by Chair Gensler in the open meeting to approve the Proposal) that MMFs were "at the heart" of the GFC is because otherwise, the SEC would bear responsibility for the pain it inflicted upon markets by its Lehman regulatory failure. In 2006 and 2007, Dan Gallagher was a senior SEC staffer serving as counsel, first to Commissioner Paul Atkins and subsequently to then Chairman Christopher Cox. In 2008, Gallagher took the position of Deputy Director of the SEC's Division of Trading and Markets, which was responsible for broker-dealer regulation. Lehman was a SEC-regulated broker-dealer. Mr. Gallagher was on-site at Lehman in New York leading a SEC monitoring and inspection team on the day Lehman declared bankruptcy. Commissioners Mike Piwowar and Kara Stein voted against the 2014 Amendments.

That any MMF was holding Lehman CP when Lehman failed is not attributable to any structural vulnerability of MMFs but instead to a deliberate course of action by the SEC and the Fed. The facts are that the SEC and the Fed knew as early as May 2008 that Lehman was about to fail, but both continued to allow Lehman to issue commercial paper into the markets and took affirmative steps to conceal Lehman's insolvency through the Summer of 2008. In Re Lehman Brother Holdings, Report of Bankruptcy Examiner Anton Valukas, pp. 1482, 1498-1500 (Mar. 11, 2010), https://jenner.com/lehman/VOLUME%204.pdf (regulators were aware in May/June 2008 Lehman was about to fail).

Under the federal securities statutes, commercial paper cannot be issued unless it is "investment grade." The SEC and Fed knew that the Lehman paper did not meet that standard. Yet on July 15, 2008, the SEC issued a release affirming the financial condition of 18 specific financial institutions, including Lehman, and restricted the short sales of those companies' stock. The SEC's release labeled as "false rumors" press reports on "unwillingness of key counterparties to deal with certain financial institutions" and that certain "financial institutions are facing liquidity problems." The SEC knew that these "false rumors" about Lehman were true, and Lehman was near failure. SEC Press Release 2008-143: SEC Enhances Investor Protections Against Naked Short Selling (Jul. 15, 2008), https://www.sec.gov/news/press/2008/2008-143.htm (SEC labels investor concerns about financial health of Lehman Brothers and 18 other financial firms as "false rumors"). The government knew full well that this would expose investing MMFs (and other investors in the market) to the risk of investment losses. Minutes of Meeting of the Federal Reserve Board Open Market Committee (Sept. 16, 2008), at 4-5, 7, 51 https://www.federalreserve.gov/monetarypolicy/files/fomcminutes20080916.pdf (Federal Reserve Board discussion of failure of Lehman and its likely impact on investor MMFs).

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resulting addiction and overdose will be resolved in the form of double-digit consumer price inflation. While Wall Street feasted on record stock and bond prices, Main Street has been left holding the bag for the Fed's and SEC's Empire of Pain.

Or, to use Chair Gensler's metaphor, we're no longer in that context where Chairs Powell and Gensler can be the scoutmasters sitting at the campfire telling their stories to the encircled campers. What has happened is that the Fed created a huge haystack of money which finally met the "match" of excessive Fiscal spending and set not just the camp, but the entire forest ablaze in a CPI fire storm.

Fed governor Lael Brainard, in her April 5, 2022 "Variation in the Inflation Experiences of Households" speech, said: "Today, inflation is very high, particularly for food and gasoline. All Americans are confronting higher prices, but the burden is particularly great for households with more limited resources. That is why getting inflation down is our most important task, while sustaining a recovery that includes everyone."

On the same day (April 5), San Francisco Fed President Mary Daly told an audience that the high cost of living is causing a heavy burden on society. "I understand that inflation is as harmful as not having a job," she said, and "that if you have a job and you can't pay your bills, or I feel like I can't save for what I need to do, then that's keeping you up at night…. And our goal is to make sure that people don't stay up worrying about whether their dollar today will be the same and worth a dollar tomorrow."[8]

In his Congressional testimony, press conferences and speeches, Chair Powell is now taking responsibility for the new Great Inflation while also telling his own bear story: that of Goldilocks and the three bears.[9] He will be using his "tools" to get the porridge "just right". Chair Powell assures of a pain-free tightening.

According to the minutes from the FOMC's March 16th meeting, participants agreed to a $95 billion monthly reduction of the Fed balance sheet (about $60 billion for Treasury securities and $35 billion for agency MBS phased in over three months). If the redemptions from prime MMFs in March 2020 were a "run", does this mean the Fed is now "running"? Is the Fed now playing with fire? Certainly, Chair Gensler's capital markets troop of campers are putting on their

[8] *See* Greider, William. Secrets of the Temple: How the Federal Reserve Runs the Country, Simon & Schuster, 1987 for a comprehensive recounting of the Great Inflation.

[9] *See, e.g.,* the Q&A of Senator Richard Shelby at *The Semiannual Monetary Policy Report to the Congress of The Honorable Jerome H. Powell, Chair Pro Tempore, Board of Governors of the Federal Reserve System*, *of the Senate Banking Comm*., 117th Cong. (March 3, 2022), https://www.banking.senate.gov/hearings/02/24/2022/the-semiannual-monetary-policy-report-to-the-congress (move the time cursor to the 1:05:20 mark).

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running shoes, but the "bear" is not market instability. It's the Fed's QE opioid.[10] What if the Fed is no longer all-powerful?[11]

Ironically, the MMF was created in 1978 by the Chair Harold Williams-led SEC. Chair Williams was appointed by President Jimmy Carter. The context, then, was the Great Inflation, and Chair Williams applauded the success of MMFs in his speeches. Chair Williams had a Harvard law degree, but he was neither a Wall Street lawyer nor a Wall Street trader. His expertise was in the field of Management (of Main Street businesses). Upon departing the SEC after President Carter's re-election defeat to Ronald Reagan, Williams was the founding director of the Getty Foundation, devoting the remainder of his life to championing the arts.[12]

In summary: (1) The Fed's exponential money creation has undermined the normal functioning of financial markets; (2) As predicted, the 2014 Amendments led to a dramatic reduction of cash in the system invested in prime and municipal MMFs; (3) QE has failed and led to historic inflation.

With these facts now clear, we call upon the SEC to undo the damage to America's Main Street economy by restoring MMFs and thereby prime the economic pump of a free market economy that needs open markets, not an open taxpayer funded checkbook from the federal government.

SFOF appreciates the opportunity to comment and your consideration of these views. Please feel free to contact me if there is any additional information or assistance that the Commission might find useful.

Sincerely,

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[10] Leonard, Christopher. The Lords of Easy Money: How the Federal Reserve Broke the American Economy, Simon & Schuster, 2022. This book is a remarkable expose of how the Fed "broke the American economy" with QE. Notably, chapter 8 ("The Fixer") chronicles the career of Chair Powell, including how he made his fortune in private equity by buying, leveraging and selling Rexnord, a midwestern, industrial manufacturing company at the expense of the company's workforce. Chapter 13 ("The Invisible Bailout") recounts how the Fed intervened in the repo market in fall of 2019, bailing out leveraged hedge funds with failed "basis" trades.

[11] As yields spike higher, will Chair Gensler again blame the liquidity issues, this time in Treasuries, MBS and interest-rate hedging markets, on MMFs? Perhaps MMFs are not the problem, but instead part of the solution? Letter from Senator Pat Toomey, Ranking Member of the Senate Banking Committee, to Vanessa Countryman, SEC, April 11, 2022, *available at* https://www.sec.gov/comments/s7-22-21/s72221-20123500-279713.pdf .

12 *See* UCLA School of Arts and Architecture. "Harold Williams '46 Receives the UCLA Arts Award: Entrepreneur, Arts Advocate, Public Servant, and Philanthropist," October 28, 2015, *available at* https://arts.ucla.edu/single/harold-williams-46-receives-the-ucla-arts-award/**;** *See also*, Securities and Exchange Commission Historical Society. "Retrospective Harold M. Williams," September 2017, *available at* https://www.sechistorical.org/museum/exhibits/hm-williams/index.php .

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Financial Dashboard of the United States Economy

Economic Indicators	Dec-05	Dec-10	Dec-15	Dec-20	Dec-21	Mar-22	Change from Dec-05
GDP $B	13,332	15,241	18,379	21,495	24,008	24,383	83%
Consumer Purch. Power (1982-84 = 100)	50.4	45.4	42.2	38.2	35.9	34.6	**-31%**
Median Real Weekly Wages ($/wk)	332	341	345	377	362	362	9%
Real Per Capita Disposable Income ($/yr)	36,918	38,700	41,867	46,518	46,236	45,997	25%
Annual Inflation rate	3.34%	1.44%	0.64%	1.30%	7.10%	8.56%	n/m

Employment Indicators	Dec-05	Dec-10	Dec-15	Dec-20	Dec-21	Mar-22	Change from Dec-05
Total Employment (millions)	135.4	130.8	143.2	143.0	149.7	151.3	12%
Labor Force Participation %	66.0%	64.2%	62.7%	61.4%	62.2%	62.2%	-6%
Productivity (2012 = 100)	89.8	98.9	102.4	111.7	111.0	111.0	24% *
Unemployment Rate	4.70%	9.10%	4.80%	6.40%	3.90%	3.60%	n/m

Monetary Policy Indicators ($B)	Dec-05	Dec-10	Dec-15	Dec-20	Dec-21	Mar-22	Change from Dec-05
Federal Reserve Govt Sec. Holdings	744	1,016	2,462	4,689	5,652	5,760	674%
Federal Reserve MBS Holdings	-	992	1,747	2,039	2,615	2,715	n/m
Total QE	744	2,008	4,209	6,728	8,268	8,475	1039%
Bank Reserves at Federal Reserve	9	1,027	2,306	3,122	4,116	3,830	42208%
Total Assets of the Federal Reserve	852	2,421	4,487	7,404	8,757	8,937	949%
Reverse Repo	-	-	277	10	1,905	1,872	n/m
Money Supply - M2	6,724	8,823	12,476	19,395	21,595	21,810	224%
Velocity of Money (annual turnover rate)	1.98	1.73	1.47	1.11	1.11	1.12	-44%

Fiscal Policy Indicators ($B)	Dec-05	Dec-10	Dec-15	Dec-20	Dec-21	Dec-21	Change from Dec-05
Total US Govt Expenditures annualized	2,650	3,810	4,055	5,955	5,959	5,443	105%
Total US Govt Receipts annualized	2,387	2,515	3,512	3,815	4,446	4,280	79%
Deficit annualized	(263)	(1,295)	(543)	(2,140)	(1,513)	(1,162)	343%
Federal Debt Held by Public	4,715	9,395	13,700	21,651	23,168	23,168	391% *
Cumulative Deficit since Dec-05	-	3,895	7,619	14,342	16,637	16,738	$16.6 T

Financial Dashboard of the United States Economy

Banking Indicators ($B)	Dec-05	Dec-10	Dec-15	Dec-20	Dec-21	Mar-22	Change from Dec-05	
U.S. Bank Assets	8,831	11,805	15,504	20,589	22,760	22,754	158%	
Domestic Deposits	6,221	7,873	10,908	16,290	18,189	18,381	195%	
Insured Deposits	3,890	6,288	6,490	9,085	9,701	9,938	155%	
Uninsured Deposits	2,331	1,585	4,418	7,205	8,489	8,443	262%	
Total Bank Loans and Leases	6,718	7,375	8,839	10,864	11,247	11,359	69%	
Commercial & Industrial Loans	1,049	1,196	1,964	2,582	2,489	2,527	141%	
Bank Holdings of Govt Sec.	1,199	1,672	2,294	4,011	5,001	5,004	317%	
# of Banks	8,833	7,658	6,182	5,002	4,839	4,796	**-46%**	
% of Assets held by Banks >$250B banks	36.8%	44.5%	49.0%	56.2%	55.8%	55.8%	52%	*
% of Assets held by Banks <$250B banks	63.2%	55.5%	51.0%	43.8%	44.2%	44.2%	**-30%**	*

Money Market Indicators ($B)	Dec-05	Dec-10	Dec-15	Dec-20	Dec-21	Mar-22	Change from Dec-05
Govt and Treas Money Fund Assets	399	855	1,227	3,685	4,176	4,078	921%
Prime Money Fund Assets	1,291	1,618	1,273	543	433	425	**-67%**
Comm Paper Outstanding	1,649	972	1,057	1,021	1,087	1,062	**-36%**

Financial Asset Performance	Dec-05	Dec-10	Dec-15	Dec-20	Dec-21	Mar-22	Change from Dec-05
S&P 500 (total return) Dec 05=100	100	112	187	392	484	461	361%
Nasdaq Index (total return) Dec 05=100	100	137	269	849	985	899	799%
Vanguard LT Bond VBTIX (total return) Dec (	100	133	158	192	186	175	75%

Key Interest Rates	Dec-05	Dec-10	Dec-15	Dec-20	Dec-21	Mar-22
Fed Funds Rate	4.29%	0.17%	0.34%	0.09%	0.08%	0.20%
30 day T-Bill	4.01%	0.05%	0.08%	0.08%	0.06%	0.17%
10 yr Treasury	4.39%	3.38%	2.31%	0.93%	1.52%	2.32%

Source: Federal Reserve, FDIC, Bureau of Labor Statistics, Yahoo Finance. Compiled by The Carfang Group.

*Updates or revisions pending.