Federated Hermes, Inc.
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February 15, 2023

Mr. Michael E. Clements
Director, Financial Markets and Community Investments
U.S. Government General Accountability Office
441 G. Street, N.W.
Washington, D.C. 20548

Dear Mr. Clements,

At Federated Hermes, Inc. ("FHI" or "Federated Hermes")[1] we read with interest the February 2, 2023 report of the General Accountability Office ("GAO") on money market mutual funds' performance during the Spring 2020 COVID-19 induced financial panic (the "Report"). [2] As you are aware, FHI was one of the three MMF sponsor firms that was interviewed by the GAO staff in researching the Report. As described further below, Federated Hermes agrees with most of the key conclusions in the text of the Report, but notes that certain important points that we raised were omitted from the Report. We also note that the press release and summary that accompany the Report, and certain of the bold headings in the Report, do not track the findings described in the body of the Report regarding the performance of MMFs in 2020.

The Report reaches several central conclusions that should limit and focus the SEC's currently pending MMF rulemaking proposal:

- the SEC has not gathered or analyzed any cost/benefit data in support of swing pricing, four digit pricing of government securities MMFs or retail MMFs, or other aspects of its proposal, only anecdotes;[3]

- retail prime MMFs, tax exempt MMFs and government securities MMFs did not suffer material redemptions during the 2020 crisis;[4]

- the weight of the data does not indicate that MMFs had a detrimental impact on the short term credit markets or the financial system during the 2020 crisis;[5] and

[1] Federated Hermes, Inc. (NYSE: FHI) is a global leader in active, responsible investment management, with $669 billion in assets under management as of December 31, 2022. We deliver investment solutions that help investors target a broad range of outcomes and provide equity, fixed-income, alternative/private markets, multi-asset and liquidity management strategies to more than 8,400 institutions and intermediaries worldwide. Our clients include corporations, government entities, insurance companies, foundations and endowments, banks and broker-dealers.
[2] GAO-23-105535 Money Market Mutual Funds (Feb. 2, 2023).
[3] Report at pp. 24-25 and cover summary.
[4] Report at pp. 15-16 (showing net redemptions at retail prime MMFs and tax exempt MMFs during the entirety of the 2020 COVID-19 panic at less than a third of their regulatory DLA levels, and net investment in US government securities MMFs).
[5] Report at pp. 18-20.

- there is consensus that the linkage of gates and fees to regulatory daily liquid asset ("DLA") liquidity levels by the SEC's 2014 MMF rule amendments drove redemptions from prime institutional MMFs during the 2020 COVID-19 crisis.[6]

These conclusions in the Report make clear that the only aspect of the SEC proposal[7] that is supported by the record is to decouple the consideration of redemption gates and fees from DLA or other regulatory minimum liquid asset levels.

The objective data does not support a conclusion that prime MMFs created or added to the 2020 COVID-induced financial crisis, or were destabilizing to the short term credit markets. There is simply no "systemic risk" to MMFs evidenced by the data in the 2020 crisis. Without that, there is not even an extraneous policy argument for the SEC to depart from its statutory mandate in the federal securities laws under which this rulemaking is conducted - investor protection, capital formation, market efficiency, and competition - to further damage the utility of MMFs by imposing swing pricing or four digit pricing of retail MMFs or US government securities MMFs.

Without a rigorous cost/benefit analysis, these aspects of the SEC MMF proposal cannot proceed.[8] And without a basis in the statutorily required considerations of investor protection, capital formation, competition and market efficiency, the SEC MMF rulemaking cannot proceed.[9]

We were one of the three MMFs selected by the GAO for an interview based on "our involvement in the [SEC MMF rulemaking] comment process and expertise" as described in the Report.[10] There are points we made to the GAO, and in the administrative record of the currently pending SEC MMF rulemaking, which are not reflected in the GAO Report. These are the most important among them:

- SEC rulemakings that will further damage MMFs do not benefit or protect investors. MMFs are higher yielding as a short-term cash investment for investors than are bank deposits. As we write this, prime MMFs are yielding roughly four hundred basis points more for investors than are bank cash balance deposits (demand deposit accounts ("DDAs") and money market deposit accounts ("MMDAs"), and US government securities MMFs are yielding more than three hundred basis points more than bank

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[6] Report at pp. 14-17.
[7] SEC, Money Market Fund Reforms (SEC File No. S7-22-21), 87 Fed. Reg. 7248 (Feb. 8, 2022).
[8] *See Michigan v. Environmental Protection Agency*, 576 U.S. 743 (2015); *Business Roundtable v. SEC*, 647 F.3d 1144 (D.C. Cir. 2011). (requiring rigorous cost/benefit analysis in rulemaking).
[9] See Investment Company Act 2(c), 15 U.S.C. 80a-2(c) (statutory considerations in rulemakings under the Act); Securities Exchange Act of 1934 3(f), 15 U.S.C. 78c(f) (same).
[10] Report at p. 3.

deposits. On average, bank DDAs and MMDAs are yielding 0.06% and 0.44% respectively per annum, the effective federal funds rate is averaging 4.33%,[11] prime MMFs at year-end 2022 had a seven-day net yield of 4.35% (institutional) and 4.31 (retail)[12] and US government securities MMFs had a seven-day net yield of 4.03%.[13]

- SEC rulemaking could have the effect of supporting the inefficient operation of banks by further shrinking MMFs as an alternative for cash investors and borrowers and are anti-competitive, contrary to the promotion of efficient markets, and degrade capital formation by increasing borrowing costs to businesses and state and local governments.

- As noted in passing by the SEC in its proposing release, the majority of redemptions (approximately 56%) from prime MMFs during the COVID-19 financial panic were from a few MMFs advised by very large G-SIFI banks, despite the fact that those MMFs represented only 28% of prime MMF assets at the time.[14] Rather than a "run" on prime MMFs, it likely was the result of those few global banks moving their clients' cash balances as part of prudent balance sheet management process to fund a large upsurge in lending (drawdowns on lines of credit by existing client borrowers, for example).[15] Nor are MMF redemptions comparable to bank "runs."[16]

Although the stated purpose of the GAO is to assess the performance of MMFs during the 2020 COVID-induced financial panic, the Report devotes nearly as much ink to discussing the 2007-2009 Financial Crisis as it does on the March-April 2020 COVID panic. And where it describes the performance of MMFs in 2020, it relies heavily on old descriptions of the 2008 performance of MMFs[17] prior to the 2010 and 2014 amendments to MMF rule 2a-7 that greatly increased portfolio liquidity, credit quality, transparency, diversity, and reduced risk, to describe the performance of MMFs in 2020.[18] That is a significant analytic error. Prime MMFs in 2020 were very different both in being much smaller in absolute size and size relative to the short-term funding markets, and had much more portfolio liquidity and resiliency than in 2008. The 2020 Federal Reserve emergency funding facilities mentioned in the report did not lend directly to MMFs but instead included a secured non-recourse credit facility provided to depository

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[11] FDIC National Rates and Rate Caps, data as of Jan. 17, 2023, [FDIC: National Rates and Rate Caps](#) (visited Feb. 6, 2023).
[12] SEC, Division of Investment Management Analytics Office, Money Market Fund Statistics (Jan. 20, 2023; data as of Dec. 31, 2022) at p. 2. https://www.sec.gov/files/mmf-statistics-2022-12.pdf .
[13] *Id.*
[14] SEC 2020 MMF Release, 87 Fed. Reg. 7248, 7255, n.52.
[15] See Comment Letter of FHI (Apr. 11, 2022), at p 10, available in SEC MMF rulemaking docket.
[16] See Supplemental Comment Letter of FHI (Nov. 1, 2022), available in SEC MMF rulemaking docket.
[17] Report at nn 12, 28 (citing 2012 reports from FSOC and SEC regarding MMFs in Fall 2008 for the proposition that MMF redemptions are disruptive).
[18] Report at pp. 12-13.

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institutions and bank holding companies to purchase specified assets from MMFs including commercial paper (the Money Market Fund Liquidity Facility, "MMFLF"),[19] as well as a primary issuer commercial paper funding facility, were dramatically smaller than analogous facilities established in 2008[20] as well as by comparison to the other federal emergency funding facilities established to address the 2020 COVID financial panic, and were fully paid off very quickly at a substantial profit to the government. The MMFLF was also small relative to the aggregate size of prime MMFs and their liquid assets, demonstrating that the MMFLF was not a main source of liquidity for MMFs. The Federal Reserve's MMFLF aggregate balance peaked at slightly over $51 billion in financing in mid-April 2020, which total was approximately 10% of the aggregate amount of weekly liquid assets (WLAs) of prime MMFs at that time.[21] The ability to use WLAs unfettered from consideration of fees and gates might have reduced or eliminated the need for the MMFLF in 2020.

Finally, we note that the summary press release and summary that accompany the Report and some of the bold headings in the report suggest conclusions that are not backed up by the accompanying text of the Report. For example, the Report is captioned "Pandemic Revealed Unresolved Vulnerabilities" and the summary states that

> "[t]he types of MMFs that were vulnerable to runs—prime and tax-exempt MMFs as described below—hold around $1 trillion in assets. During periods of market stress, MMF shareholders may be motivated to redeem shares to avoid potential losses or redemption-related costs. If MMFs sell securities at reduced prices to meet such redemptions, the sales can contribute to stress in the underlying short-term funding markets and affect the ability of financial and nonfinancial firms to raise capital in such markets." [22]

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[19] Report at pp. 17-18; FHI Comment Letter (Apr. 11, 2022) at pp. 22-23, available in SEC MMF rulemaking docket.

[20] Providing emergency funding in the short-term credit markets (including commercial paper markets) is and has been a central statutory role of the Federal Reserve since its creation by Congress in 1913. This role is reflected in the full name of the 1913 legislation that created the Federal Reserve System: "An Act To provide for the establishment of Federal reserve banks, to furnish an elastic currency, to afford means of rediscounting commercial paper, to establish a more effective supervision of banking in the United States, and for other purposes."

[21] *Compare* Federal Reserve Periodic Report: Update on Outstanding Lending Facilities Authorized by the Board under Section 13(3) of the Federal Reserve Act (Apr. 23, 2020) (showing total outstanding amount of MMFLF financing at $51 billion as of April 14, 2020) *with*, SEC Division of Investment Management Analytics Office, Money Market Funds Statistics, period ending March 31, 2020 (Apr. 2020) (tables 2 and 7 showing aggregate AUM of prime funds at $984.8 billion (comprised of $558.9 billion in institutional prime MMFs and $425.9 billion in retail prime MMFs) and percentages of that total consisting of WLAs (55.2% WLAs at institutional prime MMFs and 45.3% WLAs at retail prime MMFs).

[22] Report at p. 1.

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But the text of the Report states that "MMFs in March 2020 were not the primary cause of disruptions in certain short-term funding markets or … they had a limited impact on such markets…"[23] and that the "report also found that prime MMFs sold commercial paper to meet redemptions but that the amount of the sales was unlikely to have been the primary source of stresses in the commercial paper market."[24] In other words, MMFs in 2020 were neither the source nor an amplifier of systemic risk.

Thus, although the summary and some of the headings suggest more regulatory intervention on MMFs is needed, the actual findings of the Report and its text document that the only aspect of the SEC's pending MMF rulemaking for which there is evidentiary support is the de-linking of consideration of redemption gates and fees from compliance with DLA levels. The Report does not find that MMFs were destabilizing in 2020 and concludes that the SEC has brought forth no cost/benefit data and conducted no cost/benefit analysis on other aspects of its proposal, including swing pricing and imposition of four-digit pricing capability requirement on retail MMFs and US government securities MMFs. We applaud that the GAO's report provides factual context to the events of March 2020 as it relates to prime and tax-exempt money market funds. It would have been even more helpful in advancing the goal of better regulatory policy if both the title and summary of the report had noted that the only unresolved vulnerability of MMFs, as supported by hard data in the Report, was the problematic linkage of WLAs to consideration of fees and gates as required by the 2014 amendments to Rule 2a-7.

In sum, other than de-linking gates and fees from DLA levels, there is no basis for the SEC's currently proposed MMF rulemaking.

Respectfully,

/s/ Peter J. Germain

Peter J. Germain
Chief Legal Officer

cc: The Honorable Sherrod Brown
Chairman
Committee on Banking, Housing and Urban Affairs
United States Senate

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[23] Report at p 19.
[24] Report at pp. 19-20.

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The Honorable Patrick McHenry
Chairman
Committee on Financial Services
House of Representatives

The Honorable James Comer
Chair
The Honorable Jamie Raskin
Ranking Member
Committee on Oversight and Accountability
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