

# Key Changes Ahead

## Implementation of money market fund regulations

The U.S. Securities and Exchange Commission (SEC) is reforming the rules for money market funds. This will have an impact on retirement plans. Money market funds (MMFs) have been used by 401(k) and 403(b) plans to provide a simple, stable and liquid source of income, despite their low returns. The new rules will require committees to re-examine the role of the MMF in their plans and determine which type of fund meets those needs.

When the SEC reforms go into effect next October, there will be three main types of these funds:

The first will be the “institutional” MMF. Unlike the current structure, these MMFs will be priced daily rather than having their net asset value (NAV) fixed at \$1. Although the day-to-day changes should be very small, this means the NAV will vary as it does with the plan’s other investments. The institutional funds impose redemption fees in certain cases and will need to suspend redemptions—in a restriction called a “redemption gate”—for up to 10 business days if the fund’s liquidity falls below certain levels.

The second type will be the “retail” MMF, in which only “natural persons” may invest. The NAV of these MMFs will not float, but the funds will be required to impose the redemption fees and gates.

The third type is the “government” MMF, which must invest 99.5% of its assets in U.S. Treasury securities. The NAV of these MMFs will not float, and the funds will not be required to impose redemption fees and gates.

These changes raise issues that plan committees should consider:

- **What type of fund should your plan have?** A government fund will avoid the required changes under the new rules, but the return will likely be lower than those produced by the other two. An alternative in a participant-directed plan would be to select a retail fund. Because a person—the participant—is directing the investment of his account, the account qualifies as a “natural person” and may hold a retail MMF. The return on retail MMFs will be better than that of the government fund, but the fund will still be subject to the possible redemption fees and gates. However, a retail fund is not available for pooled plans, such as defined benefit (DB) pension plans. An institutional fund may provide the best returns, but its value will float and, therefore, the participants may not see it as “stable.”

- **How do you explain the different types of funds to participants?** For retail funds, the redemption fees and gates should be explained. For institutional funds, the floating NAV should be explained. And, for government funds, perhaps the choice and the likely lower returns should be explained.

- **What will your current MMF provider do?** The committee cannot control the outcome, but it needs to ask the right questions of the fund manager. What kind of MMFs will it offer? If it offers a government fund, will it be one that voluntarily imposes redemption fees and gates, as is permitted under the new rules? How will it police its funds to make sure a “retail” fund has only “natural person” investors? These are not easy questions, and a committee may need help from its financial adviser to figure this out, but the questions need to be asked.

As a start, here’s what plan sponsors should be thinking about now:

First, a committee needs to work with its adviser to decide which kind of MMF is appropriate for its participants. We suspect that many committees will decide to use government funds, for two reasons.

One, plans often include MMFs to offer participants a safe investment. The floating value of institutional funds may run counter to that. Two, participants often park needed money in their plan’s MMF—for example, for a down payment on a house. What happens if a retail fund shuts off redemptions right before the money needs to be deposited in escrow?

But, that’s just our opinion. What matters is your opinion in fulfilling your fiduciary duty to act in the best interest of your participants. There is no one-size-fits-all answer.

The second step is to learn more about the MMF options on your provider’s platform. Investigate, deliberate and decide. There are questions that need to be asked, lots of answers that need to be reviewed and a number of decisions that need to be made, based on those answers. So, beginning to look at the issues now seems to be the smart choice.

.....

**Fred Reish** is a partner at Drinker Biddle & Reath LLP’s employee benefits and executive compensation practice group, chair of the financial services ERISA team and chair of the retirement income team. **Bruce Ashton**, a partner at the firm, and **Joshua Waldbeser**, an associate, contributed to this article.