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BENEFITS BRIEF

SEC Money Market Mutual Fund Rules – The Impact on Retirement Plans

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In October of this year, SEC rules will require that certain types of money market funds utilize a floating net asset value (rather than the current stable $1 net asset value), require (or in some cases, permit) the imposition of redemption fees on withdrawals, and permit temporary delays before withdrawals are processed. As many retirement plans use a money market fund as a low volatility, cash-equivalent investment, these rules have the potential to create administrative problems for plans utilizing the types of money market mutual funds affected by the SEC rules. In this *Benefits Brief*, we will briefly summarize the SEC rules and suggest key actions that prudent plan sponsors and plan fiduciaries should consider.

Executive Summary

- The imposition of mandatory or permissive redemption fees or temporary withdrawal suspensions by money market mutual funds starting October 14, 2016 requires plan sponsors and fiduciaries of retirement plans with money market mutual fund investments to assess the impact of these rules on the administration of the plan. Plan sponsors and fiduciaries should promptly discuss these rules with the plan's investment advisor and investment recordkeeper.

- If a change in the plan investment line-up is warranted, significant lead-time may be needed to implement – both in dealing with the investment recordkeeper as well as required communications to participants.

- Even if a change in the investment line-up is not needed, additional communications to participants may be needed to apprise them of potential redemption fees and withdrawal suspensions.

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How Money Market Mutual Funds are Affected by the SEC Rules

The SEC rules were developed following the 2008 financial crisis and are designed to minimize the risk of a "run on the fund" in times of severe market distress. These rules are effective October 14, 2016.

The SEC classifies money market mutual funds into one of three types: government funds, "retail" funds, and institutional funds. Government money market funds are those funds that hold at least 99.5% of its assets in cash and short-term U.S. government securities. "Retail" money market funds are those funds which are not government money market funds and which limit investors to natural persons, including participants in participant-directed 401(k) or similar plans. Institutional money market funds are those money market funds that are not government money market funds or retail money market funds.

Depending upon the type of money market fund involved, the rules either require or permit the imposition of a redemption fee if certain liquidity thresholds are not satisfied. In addition, the board of any money market fund, including a government money market fund, may suspend redemptions from the fund for a period of up to 10 business days if certain liquidity thresholds are not satisfied.

Institutional money market funds will also be required to use a floating net asset value (NAV), or per share price based on the value of the underlying investments of the fund rather than the more familiar stable $1.00 per share net asset value.

The SEC rules are summarized in the following table:

Government Funds	Retail Funds	Institutional Funds
Fund must hold 99.5% of its assets in cash and U.S. Treasury securities	Investor must be a natural person or a participant in a participant – directed defined contribution plan	All other funds, including funds held by defined benefit plans and non-participant directed defined contribution plans
▪ Can maintain stable $1.00 share value	▪ Can maintain stable $1.00 share value	▪ Mandatory use of floating NAV
▪ 2% redemption fee permitted if liquid assets fall below 30% of total assets if the fund board determines it is in the best interests of the fund	▪ 2% redemption fee permitted if liquid assets fall below 30% of total assets if the fund board determines it is in the best interests of the fund	▪ 2% redemption fee permitted if liquid assets fall below 30% of total assets if the fund board determines it is in the best interests of the fund

▪ No required redemption fees but they are permitted to the extent applicable to the other fund types	▪ Required 1% redemption fee if liquid assets fall below 10% of total assets – unless the fund board determines that the fee is not in best interests of the fund or a different redemption fee (of up to 2% should be imposed)	▪ Required 1% redemption fee if liquid assets fall below 10% of total assets – unless the fund board determines that the fee is not in best interests of the fund or a different redemption fee (of up to 2% should be imposed)
▪ Fund may suspend redemptions for up to 10 business days in a rolling 90-calendar day period if liquid assets fall below 30% of total assets – if the fund board determines doing so is in the best interests of the fund	▪ Fund may suspend redemptions for up to 10 business days in a rolling 90-calendar day period if liquid assets fall below 30% of total assets – if the fund board determines doing so is in the best interests of the fund	▪ Fund may suspend redemptions for up to 10 business days in a rolling 90-calendar day period if liquid assets fall below 30% of total assets – if the fund board determines doing so is in the best interests of the fund

Considerations for Plan Sponsors and Fiduciaries

These new rules have the potential to cause havoc with retirement plan administration. It is worth noting that these rules apply to money market mutual funds in all types of retirement plans and is not limited to participant-directed retirement plans. A retirement plan with a fund to which the redemption fees and/or temporary withdrawal restrictions apply could find itself unable to timely make required withdrawals, for example, minimum required distributions or refunds required to correct nondiscrimination testing failures, or even participant-initiated transactions, such as withdrawal requests or investment election changes.

Investment Recordkeeper Limitations

Plan sponsors and fiduciaries should discuss the implications of retaining a money market fund subject to these rules with its investment recordkeeper to ascertain the ability of the recordkeeper's automated systems to accommodate the potential restrictions, which could be especially problematic in daily-valued plans.

Reporting and Disclosure Issues

Even if the recordkeeping system will handle this, satisfaction of the participant fee and expense disclosure requirements, which generally require at least a 30-day advance notice for changes in fees and expenses, and revision of other participant disclosures to assure participants understand the risks of their investment elections, must also be considered. Plan sponsors and fiduciaries of plans that retain a money market fund subject to withdrawal suspensions will also need to determine how the participant blackout notice requirements can be satisfied with respect to those suspensions.

Impact on Default Investment Alternative Requirements

Plan sponsors and fiduciaries of plans which utilize a default investment option that consists of a model portfolio that includes a money market fund will also want to confirm that the investment still satisfies the requirements to be a "qualified default investment alternative" so the plan fiduciaries remain insulated from liability from liability with respect to such investments.

Use of a Government Money Market Fund

Plan sponsors and fiduciaries should also consider the prudency of replacing a money market fund subject to these rules with a government money market fund that chooses not to impose the permissive restrictions, provided, of course, that such a change is consistent the plan's investment policy. A drawback to that strategy is that government funds usually yield a lower rate of return than other money market funds, which themselves are at historic lows. Should a replacement be made, the plan sponsor and fiduciaries must determine whether a "blackout" period is necessary to implement the fund change and whether 30-day advance notice to participants of the change is required, either as a consequence of a required blackout period or to assure that amounts transferred to the successor fund continue to be treated as "participant-directed" for purposes of the fiduciary responsibility rules.

Use of a Stable Value Fund

Plan sponsors and fiduciaries should also consider whether replacing a money market fund with a stable value fund provides an acceptable level of risk under the plan's investment policy. Generally speaking, a stable value fund is an investment vehicle that invests in a diversified portfolio of high-quality short- to intermediate-term fixed income investments that is "wrapped' by an insurance contact to offer a stable NAV. Aside from addressing the administrative burdens caused by the SEC rules, such a change may otherwise be a prudent course of action due to the differences in the rates of return between money market funds and stable value funds; there have been a number of lawsuits against large retirement plans recently in which utilizing a money market fund instead of a stable value fund was claimed to be imprudent given the fairly comparable risk level and the higher rates of return historically earned on stable value funds relative to money market funds. Should a change be determined to be desirable, the replacement of the money market fund could also implicate the blackout rules and the necessity of 30 days' advance notice to participants.

Concluding Thoughts

The expectation is that these new redemption fees and temporary suspensions of withdrawals will only be applicable in times of severe market stress and that under normal circumstances they will have no application. That said, the October 14, 2016 effective date for the rules will soon be here so a prudent sponsor and fiduciary will want to consider the actions needed to address these potentialities even if the likelihood of their application may be small. Considering the advance notice requirements that may apply to changes in fund offerings, plan sponsors and fiduciaries in plans with money market fund investments would be well-advised to promptly contact their investment advisor and investment recordkeeper to determine the appropriate strategy for the plan to address these contingencies.

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