

Provisions for negative interest rates

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On July 12, 2023, the Securities and Exchange Commission (SEC or the Commission) adopted certain amendments related to the [money market fund](#) industry.¹

A key takeaway from the adopted amendments was the creation of a framework by the Commission for handling a **negative interest rate environment** for retail and government money market funds, which typically operate with a constant net asset value (CNAV).

The Commission provided that in addition to these funds being able to convert to a floating net asset value (FNAV), as the current rules already permit, these funds now have the ability to reduce the number of their shares outstanding to maintain a constant net asset value per share, also known as a **Reverse Distribution Mechanism** (RDM).

In a negative interest rate environment, the gross yield of a money market fund's portfolio may turn negative.

Under such circumstances, it may be challenging for a CNAV fund to maintain a stable share price under the current Rule 2a-7 of the Investment Company Act of 1940 (the Rule).

The Commission's ruling now enables CNAV funds two potential alternatives to account for this scenario:

1

Reverse Distribution Mechanism

Use of a RDM which allows a fund to maintain a CNAV through share cancellation.

2

Constant NAV to Floating NAV

Convert from a CNAV per share to an FNAV per share.

Source: 1. [Money Market Fund Reforms: Form PF Reporting Requirements for Large Liquidity Fund Advisers; Technical Amendments to Form N-CSR and Form N-1A](#)

Reverse Distribution Mechanism

Should the fund's Board of Directors determine the fund's net yield is unable to maintain a CNAV per share, then the Board may, if it is in the best interests of the fund and shareholders, cancel from each fund class such number of shares by an amount that equals the amount required for that fund class to maintain a CNAV per share.

The shares will be cancelled, and the value attributable to those shares will be retained by the relevant fund class to offset the negative net yield attributable to that fund class – enabling the NAV per share class to remain stable.

The shares of each shareholder within the relevant fund class will be cancelled on a pro-rata basis.

Investors would observe a stable share price as well as a declining number of shares for their investment, when a negative gross yield is applicable.

Investors would be losing money during this time.

Appropriate disclosures would be provided to shareholders describing this share reduction and the impact it has on the shareholder's holdings.

Constant NAV to Floating NAV

Should the fund's Board of Directors determine that the fund may not be able to maintain a stable NAV per share due to a negative yield event, the Board may allow the fund to convert to an FNAV per share, if such a conversion is determined by the Board to be in the best interests of the fund's shareholders.

If a conversion is implemented, the fund's share classes affected by the negative yield event would be amended as follows:

- The shares would become FNAV shares
- The negative income will be accrued into the NAV
- The NAV per share for these share classes will not remain stable and capital may be eroded

If a CNAV fund converts to an FNAV, **the fund's losses will be reflected through a declining share price.**

Please reach out to your relationship manager to learn more about this important change.

Want to know more?

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