Tax Tips

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Part of the response to the great recession was the expansion of regulation of financial instruments. One of these becomes effective in October, in response to one fund "breaking the buck" in 2008. I will start off stating that this discussion does **not** apply to money market deposit accounts at your bank, but rather to money market mutual funds held in many investment accounts. Usually money market mutual accounts are thought of as a boring place to park your cash until you decide to invest it.

Presently, a dollar invested in a money market mutual fund retains its value of $1, or what is called a stable net asset value. It is a mutual fund, invested in an array of underlying investments, depending upon the limitations placed on the fund. Some are government funds, invested almost exclusively in U.S. government and agency securities, others are municipal funds, invested mainly in debt of state and local governments, and still others are called prime funds, invested in corporate debt and some government debt. There are also different types of investors in these funds: retail and institutional. Retail funds permit investment only by individual investors or accounts where end users are individuals. Institutional funds permit investment by institutions, such as corporations, but may also permit individuals along with institutions.

One requirement under the new rule is that institutional funds must float in value, or have a variable net asset value. The dollar invested today may change tomorrow, depending upon the change in value of the underlying investments. Government funds, whether retail or institutional, are not subject to this change and will retain their characteristic of a stable asset value. Retail funds will also retain a stable asset value, but retail funds are those that permit individuals only. If institutions are permitted to buy shares, the fund is an institutional fund and will be required to have a floating or variable net asset value.

Another big change is that all money market mutual funds that are prime funds, invested in corporate or municipal debt, will be permitted to charge redemption fees if these funds come under redemption pressure during periods of financial stress. These funds may also block investors from withdrawing cash, suspension gates, during periods of similar stress.

For many investors, this change may only be nominal, at best. Many providers of these funds are converting funds to government funds or are creating separate retail and institutional funds. However, some institutional funds may offer potentially higher returns but also the risk of a variable net asset value. You may be willing to take this additional risk for the extra return, but you should be aware of it. In our trust department, we have utilized government funds for many years, so this is not much of an issue. You should review your investment account statement and the prospectus for the money market mutual fund used in your account, to determine if these new rules apply to you and review options that may be available to you.