



35 New Broad Street, London EC2M 1NH, UK
+44 (0) 203 009 3100 www.iciglobal.org

4 August 2017

European Securities and Markets Authority
CS 60747
103 rue de Grenelle
75345 Paris Cedex 07
France

Dear Sir or Madam:

ICI Global¹ appreciates the opportunity to comment on the European Securities and Markets Authority's (ESMA) consultation paper (CP)² on the EU's Money Market Funds Regulation (MMFR).³ The key proposals relate to asset liquidity and credit quality, the establishment of a reporting template, and stress test scenarios. Our comments focus on ESMA's proposed technical advice relating to the liquidity applicable to the collateral received as part of a reverse repurchase agreement (reverse repo) and ESMA's proposed guidelines on stress test scenarios.

Although we are not commenting on the proposed reporting template, we do not agree with ESMA's statement in paragraph 186 within that section that the "destruction of shares is not allowed under the MMF Regulation." The cancellation or "destruction" of shares is a widely-accepted mechanism that operates in accordance with the Undertakings for Collective Investment in Transferable Securities directive provisions. Also called a reverse distribution mechanism, share cancellation is an approved mechanism (often requiring a shareholder vote) that some money market funds have used effectively to deal with negative interest rates applicable for certain currencies. We are not aware of any reference in the MMFR that would prohibit this mechanism, and nor do we believe the mechanism is inconsistent with the MMFR.

¹ ICI Global carries out the international work of the Investment Company Institute, the leading association representing regulated funds globally. ICI's membership includes regulated funds publicly offered to investors in jurisdictions worldwide, with total assets of US\$26.0 trillion. ICI seeks to encourage adherence to high ethical standards, promote public understanding, and otherwise advance the interests of regulated investment funds, their managers, and investors. ICI Global has offices in London, Hong Kong, and Washington, DC.

² The CP is available at https://www.esma.europa.eu/sites/default/files/library/esma-34-49-82_cp_on_draft_technical_advice_implementing_technical_standards_and_guidelines_under_the_mmf_regulation.pdf.

³ The MMFR is available at <http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32017R1131&from=EN>.

Executive Summary

Our comments are summarized below and explained in greater detail in the remainder of the letter.

Reverse Repo Collateral Liquidity Requirements

- *Haircuts on Government Collateral Are Inconsistent with FSB Principles.* Minimum numerical floors for haircuts of governmental reverse repo collateral conflict with the FSB's regulatory framework for haircuts on non-centrally cleared securities financing transaction and creates a disproportionate and unnecessary divergence from the agreed upon international approach to transactions backed by government securities.
- *ESMA's Focus on Haircuts Is Unnecessary and Problematic.* Minimum numerical floors for haircuts of government reverse repo collateral would put money market funds at a disadvantage relative to other reverse repo buyer/cash lenders; would tend to require that money market funds conduct a collateral analysis that may have no bearing on their decision to extend credit to a seller; and are potentially higher than the haircuts prevailing in the market for some government collateral.
- *Stress Testing Collateral Liquidity Would Not be Beneficial.* The reverse repo collateral that is permitted under the MMFR generally corresponds to securities that the European Banking Authority (EBA) found to be of "extremely high liquidity and credit quality" or of "high liquidity and credit quality." Any stress testing that a money market fund performs on this collateral should replicate the EBA results, and therefore, would not enhance the quality of permitted reverse repos.
- *Recommendations on Reverse Repo Collateral Liquidity Requirements.* We urge ESMA not to adopt the minimum haircuts proposed in Option 1(ii) or the stress testing requirements for collateral under either Option 1 or Option 2.

Guidelines on Stress Test Scenarios

- *ESMA Should Adopt a Principles-Based Approach to Stress Testing.* The current US requirements, which were adopted in 2010 and refined in 2014, set forth principles for sound stress testing practices and oversight, but do not attempt to quantify specific parameters or criteria that would require irrelevant testing. Such an approach accommodates the needs and profiles of different types of money market funds. We are concerned that ESMA's proposed approach (Option 3)—which would attempt to specify certain quantitative (or detailed) criteria—would not allow for such variations and could reduce the effectiveness of the funds' stress testing. We urge ESMA to follow the SEC's principles-based approach to money market fund stress testing, which is similar to Option 1.

Reverse Repo Collateral Liquidity Requirements

Background

Under Article 15 of the MMFR, a money market fund may enter into a reverse repo provided the fund has the right to terminate the reverse repo with notice of no more than two working days and the market value of the reverse repo collateral is at all times at least equal to the value of the purchase price paid by the fund. The MMFR also stipulates that a money market fund may only receive reverse repo collateral consisting of money market instruments otherwise eligible for investment by the fund. By way of derogation from this requirement, Article 15(6) provides that a money market fund may receive reverse repo collateral other than money market instruments eligible for investment by the fund provided those assets comply with the following conditions:

- They are issued or guaranteed by the Union, a central authority or central bank of a Member State, the European Central Bank, the European Investment Bank, the European Stability Mechanism or the European Financial Stability Facility provided that a favourable assessment has been received pursuant to Articles 19 to 22;⁴
- They are issued or guaranteed by a central authority or central bank of a third country, provided that a favourable assessment has been received pursuant to Articles 19 to 22.

Moreover, Article 15(7) empowers the European Commission to adopt delegated acts specifying liquidity and credit quality requirements applicable to reverse repo collateral. For this purpose, the Commission must consider the report on appropriate uniform definitions of high and of extremely high liquidity and credit quality of transferable assets as referred to in the Capital Requirements Regulation (CRR).⁵ In a 20 January 2017 letter, the Commission asked ESMA to provide technical advice regarding the criteria and characteristics of assets referred to in Article 15(6) to ensure that the money market fund's liquidity profile is not endangered if it is forced to liquidate those assets following a counterparty's default. To this end, ESMA reviewed relevant sections of the MMFR, as well as other existing EU and US requirements on liquidity and credit quality requirements.⁶

⁴ Article 19 covers internal credit quality assessment procedures, Article 20 covers internal credit quality assessments, Article 21 covers related documentation, and Article 22 covers delegated acts for the credit quality assessment.

⁵ The CRR and Article 15(7) refer to a December 2013 EBA report on appropriate uniform definitions of extremely high quality liquid assets, high quality liquid assets, and operational requirements for liquid assets under Article 509(3) and (5) of the CRR. The EBA report is available at

<https://www.eba.europa.eu/documents/10180/16145/EBA+BS+2013+413+Report+on+definition+of+HQLA.pdf>.

⁶ As part of its review of US requirements, ESMA reviewed requirements under US Securities and Exchange Commission Rule 2a-7—the primary rule under the Investment Company Act of 1940 that regulates US money market funds—relating to criteria for reverse repos and reverse repo collateral and Rule 22e-4 relating to investment company liquidity risk management programs for US open-end management funds (including ETFs, but not including money market funds). We question the relevance of Rule 22e-4 to money market funds. The SEC specifically excluded money market funds from the scope of Rule 22e-4 because money market funds are subject to extensive requirements concerning portfolio liquidity that are more stringent than the requirements of Rule 22e-4; are subject to broad liquidity-related disclosure and reporting

ESMA's Preferred Options on Liquidity Requirements

ESMA proposes two preferred options of technical advice relating to reverse repo collateral liquidity requirements. The first option (Option 1) would require that a money market fund apply liquidity requirements to the reverse repo collateral depending on the reverse repo counterparty's risk of default and risk diversification limit. Specifically, if the counterparty is a European credit institution, European investment firm, any credit institution or investment firm subject to prudential regulation deemed equivalent to the European one, regulated central counterparties, the ECB, Member States' central banks or non-EU central banks deemed equivalent under the requirements of Article 114 (risk weight exposures to central governments or central banks) of the CRR, then no specific liquidity requirements would apply to the reverse repo collateral. The CP explains that because the risk of default is limited (based on regulations that already are applicable to the counterparty), the risk that a money market fund would be forced to liquidate the collateral is reduced and accordingly additional liquidity requirements with respect to the collateral are unnecessary.

On the other hand, to ensure sufficient overcollateralization of the reverse repo, Option 1 would require that a money market fund consider the following factors if the counterparty is not similarly prudentially regulated: (i) the time to maturity of the assets; (ii) the price volatility of the assets; and (iii) the appropriate stress-testing policy under Article 28 of the MMFR. Depending on these factors, the money market fund would apply a corresponding haircut based on an existing standardised haircut policy, such as the Basel Committee on Banking Supervision's standard approach (BCBS).⁷

The second option (Option 2) would require that a money market fund determine the reverse repo collateral's liquidity profile based on the following requirements: (i) the asset manager has reasonable expectations that within one business day the collateral can convert to cash with a marginal impact on the market value of the investment; (ii) the asset manager continuously monitors these expectations; and (iii) under both normal and exceptional liquidity conditions stress tests are run in accordance with Article 28 of the MMFR, taking into consideration various criteria, *e.g.*, the bid-ask spreads, the average daily trading volume, and the credit quality of the issuer. If the asset manager determines that one or several assets composing the collateral no longer comply with a liquid profile, the assets must be replaced with overnight liquid assets or the reverse repo must be terminated within one business day's notice.

ESMA believes that Options 1 and 2 constitute an appropriate balance between the need for additional credit quality and liquidity requirements with respect to reverse repo collateral and the existing regulatory requirements that already apply to these assets, whether as a direct consequence of other articles of the MMFR or other pieces of the EU regulatory framework. Depending on the outcome of the CP, ESMA also notes that it will consider whether its final advice will include either Option 1 or

requirements; and have certain tools (fees and gates) at their disposal to manage heavy redemptions that are not available to other US open-end funds.

⁷ See Basel Committee on Banking Supervision: Board of the International Organization of Securities Commissions, Margin Requirements for Non-Centrally Cleared Derivatives (March 2015), available at <http://www.bis.org/bcbs/publ/d317.pdf>.

Option 2 or a combination of both options. The CP includes a number of questions regarding the liquidity requirements. Our comments will focus on how money market funds typically use reverse repos; how the proposed haircut policy under Option 1 is inconsistent with FSB principles, unnecessary, and likely problematic; and why stress testing collateral liquidity is not beneficial.

Money Market Funds' Use of Reverse Repos

Money market funds use reverse repos as a type of liquid and collateralized short-term investment technique that not only improves the return on their portfolios for the benefit of their shareholders but also helps to satisfy regulations, such as the MMFR and the US SEC's Rule 2a-7, that require that money market funds hold a minimum of total assets in daily liquid assets (*e.g.*, 10 percent) or weekly liquid assets (*e.g.*, 30 percent).⁸

Reverse repos may be executed as bilateral reverse repos, where repo sellers and buyers transact directly with each other or tri-party reverse repos, in which a clearing bank handles settlement and operational issues. Tri-party reverse repos are popular among money market funds because they offer operational efficiency. To protect the buyer (*e.g.*, a money market fund) against the risk that a seller of securities (*e.g.*, a broker/dealer) will not fulfill its obligation to repurchase the securities, the securities are held as collateral in a separate account at a tri-party clearing bank, which acts as reverse repo custodian, and priced daily (marked to market) to maintain a value at least equal to the repurchase price (including accrued interest). Negotiated "haircuts" or "margin percentages" provide additional protection, which ensures that the value of the securities that the buyer holds exceeds the repurchase price by the negotiated percentage (*e.g.* the overcollateralization). If the value of the securities falls below the negotiated level of overcollateralization the seller must post additional collateral. Most of the reverse repo market is comprised of overnight investments in which the seller repurchases the securities on the next business day; however, term reverse repos, in which the seller repurchases the collateral after two or more business days, also are used.

Money market funds only enter into reverse repos with high quality counterparties. For example, SEC Rule 2a-7 imposes strict minimum standards for the credit quality, maturity, diversification and liquidity requirements of a money market fund's investments, including reverse repos. In addition, the rule requires the funds to evaluate the reverse repo counterparty's creditworthiness as a prerequisite to engaging in a reverse repo transaction. Also, since the 2008 financial crisis, the market has significantly enhanced its practices for all market participants with respect to reverse repos in the United States in ways that significantly reduce intraday credit risk, increase transparency, and mitigate counterparty credit, liquidity, and credit quality risks.⁹

⁸ The Federal Reserve Bank of New York's white paper on tri-party repo provides a comprehensive description of the repo market and the role money market funds play in it as cash investors. *See* Tri-Party Repo Infrastructure Reform (May 17, 2010), available at http://www.newyorkfed.org/banking/nyfrb_triparty_whitepaper.pdf.

⁹ ICI discussed these developments at length in its letter to the Financial Stability Board on 25 May 2012 ("25 May 2012 ICI letter"), available at http://www.fsb.org/wp-content/uploads/c_120806g.pdf. ICI also has provided its members with a checklist to assist in developing a contingency plan in the event of a dealer default. This checklist is designed primarily to

Haircuts on Government Collateral Are Inconsistent with FSB Principles

ESMA's proposal regarding haircuts for governmental reverse repo collateral conflicts with the FSB's regulatory framework for haircuts on non-centrally cleared securities financing transaction¹⁰ and creates a disproportionate and unnecessary divergence from the agreed upon international approach to transactions backed by government securities. Specifically, the FSB's framework of numerical haircut floors only applies to non-centrally cleared securities financing transactions in which financing against collateral other than government securities is provided to non-banks. Consistent with ESMA's explanation for why Option 1 would not add specific liquidity requirements to collateral from a reverse repo counterparty that is prudentially regulated, the FSB decided to exclude securities financing received by banks and broker-dealers subject to adequate capital and liquidity regulation on a consolidated basis from the scope of application because applying numerical haircut floors to those transactions may duplicate existing regulation. The FSB also explained that transactions backed by government securities are excluded from the framework because price movements in these securities generally tend not to be procyclical and haircuts on these transactions have been comparatively stable over time at zero or low levels.

ESMA's Focus on Haircuts Is Unnecessary and Problematic

We believe that ESMA would cause a number of problems by establishing minimum numerical floors for haircuts of government securities, especially at the levels suggested by the BCBS haircut policy.

Specifically, the CP's focus on haircuts is misplaced and would put money market funds at a disadvantage relative to other reverse repo buyer/cash lenders. As noted above, money market funds enter into a reverse repo based primarily upon the seller's capacity to pay the repurchase price, rather than upon the value and liquidity of the collateral. Collateral is just one factor (along with rate, term, liquidity, and other factors) when deciding what form or amount of credit to extend to an institution. Prescriptive methods for establishing haircuts, such as the BCBS haircut policy, would tend to require that buyers conduct a collateral analysis that may have no bearing on their decision to extend credit to a seller.

As such, we have consistently disagreed with any attempt to regulate the negotiated terms of market transactions such as reverse repos.¹¹ Such terms are best set by market forces, responding to current market conditions and a multitude of other factors that regulations can never adequately capture.

detail the steps that a fund investor would take to liquidate securities subject to a reverse repo with a dealer that becomes insolvent after entering into the reverse repo. It is available at http://www.ici.org/policy/current_issues/11_mmf_repo_checklist.

¹⁰ FSB, Transforming Shadow Banking into Resilient Market-Based Finance: Regulatory Framework for Haircuts on Non-Centrally Cleared Securities Financing Transactions (12 November 2015), available at http://www.fsb.org/wp-content/uploads/shadow_banking_overview_of_progress_2015.pdf.

¹¹ See 25 May 2012 ICI letter and letters dated 27 November 2013, 14 January 2013, and 25 May 2012 from ICI and ICI Global to the FSB, available at http://www.fsb.org/wp-content/uploads/c_131220n.pdf; http://www.fsb.org/wp-content/uploads/c_130129ar.pdf, and http://www.fsb.org/wp-content/uploads/c_120806g.pdf, respectively.

Haircuts are no different from other terms of a reverse repo and therefore should not be dictated by regulations.

Even more concerning, however, are regulations that would dictate specific haircut floors unique to transactions involving money market fund repo buyers. We believe that imposing floors for government collateral may create an unintended bias against collateralized financing or even preclude some creditors from providing such financing to money market funds.

Moreover, the BCBS proposed floors, are higher than the haircuts currently prevailing in the market for some government collateral. Repo transactions are typically already over-collateralized at levels ranging from 102 percent to 110 percent (depending on asset class), as demonstrated by the Federal Reserve Bank of New York's (FRBNY) monthly published collateral data.¹² More specifically, the FRBNY reports that haircuts for collateral backed by US Treasury securities (regardless of maturity) are at a median of 102, but the BCBS haircut policy would apply a 104 to all government securities with residual maturities greater than five years. Problems that could result from such floors include a negative impact on the liquidity of the reverse repo and secondary markets for the affected securities if transactions currently take place at haircuts below the required levels.

Although no one denies the need for money market funds to employ appropriate collateral management practices, we do not believe it is necessary that a sound repo liquidity regulation include specific and preset haircut floors for government collateral that would not only put money market funds at a disadvantage to other repo cash lenders but also would (in many cases) be higher than prevailing market rates.

Stress Testing Collateral Liquidity Would Not be Beneficial

Both Option 1 and Option 2 would require funds to stress test the liquidity of collateral “under both normal and exceptional liquidity conditions.” The reverse repo collateral that is permitted under Article 15(6), however, generally corresponds to securities that the EBA found to be of “extremely high liquidity and credit quality” or of “high liquidity and credit quality.” The CP’s discussion of the EBA report highlights the difficulties of performing liquidity analysis on these securities.

Indeed, any stress testing that a money market fund performs on this collateral should replicate the EBA results and, therefore, would not enhance the quality of permitted reverse repos. Although it would be possible to formulate market conditions so extraordinary as to impair the liquidity of this type of collateral, we do not believe funds would benefit from such an exercise. Such extraordinary market conditions would likely develop unexpectedly and require an immediate reassessment by fund managers, rather than stress testing.

¹² Beginning in May 2010, the FRBNY began publishing market data on the tri-party repo market on its web site. See <https://www.newyorkfed.org/data-and-statistics/data-visualization/tri-party-repo/index.html>. This data highlights the overall size of the market, collateral, concentrations, and margin requirements that exist within the market. This reporting provides greater transparency into the broader market, giving all market participants and regulators the ability to monitor repo exposures and highlight repo market trends.

On the limited occasions that a money market fund receives as reverse repo collateral money market instruments that it could hold directly, the fund likely already would have assessed the liquidity of these instruments in connection with its general stress testing. Stress testing collateral liquidity would be particularly onerous on money market funds that do not invest heavily in reverse repo. We therefore recommend that ESMA omit this aspect of the reverse repo liquidity requirements.

Recommendation on Reverse Repo Collateral Liquidity Requirements

We believe that ESMA should combine aspects of Option 1 and Option 2 in its final advice. Specifically, we believe that Option 1(i) should remain with respect to appropriately regulated counterparties and that no further liquidity requirements apply to such counterparties. We recommend that the additional liquidity requirements in Option 2(i) and (ii) be required with respect to counterparties that are not deemed to be appropriately regulated under Option (1)(i). For the reasons set forth above, we urge ESMA not to adopt the minimum haircuts proposed in Option 1(ii) or the stress testing requirements for collateral under either Option 1 or Option 2.

Guidelines on Stress Test Scenarios

Background

Article 28 of the MMFR requires each money market fund to adopt sound stress testing processes that identify possible events or future changes in economic conditions that could have unfavourable effects on the money market fund. The money market fund or its manager must assess the possible impact that those events or changes could have on the money market fund and the manager must regularly conduct stress testing for different possible scenarios based on objective criteria and consider the effects of severe plausible scenarios. Further, Article 28 requires ESMA to issue guidelines with a view to establishing common reference parameters for these stress test scenarios taking into account the following hypothetical factors:

- changes in the level of liquidity of the assets in the money market fund's portfolio;
- changes in the level of credit risk of the assets in the money market fund's portfolio, including credit events and rating events;
- movements in the interest rates and exchange rates;
- levels of redemption;
- widening or narrowing of spreads among indexes to which interest rates of portfolio securities are tied; and
- macro systemic shocks affecting the economy as a whole.

As part of its review, ESMA reviewed existing EU stress testing requirements in the asset management sector, the FSB's current work on stress testing, and recently adopted US money market fund reforms and related stress testing requirements.

ESMA's Proposed Stress Testing Guidelines

ESMA considered three different approaches to stress testing: a very high level principle-based approach that would not specify any quantitative criteria or threshold (Option 1); a very prescriptive approach that would specify quantitative (or detailed) criteria or thresholds for all factors listed in Article 28 (Option 2); or an intermediate approach that would specify quantitative (or detailed) criteria or thresholds for some of the factors listed in Article 28 (*e.g.*, changes in the level of liquidity of the assets, movements of the interest rates and exchange rates, levels of redemption) and take a more principle-based approach for other factors (Option 3). Based on its review, ESMA's preferred approach is Option 3.

As the CP acknowledges, the hypothetical factors included in Article 28 are substantially similar to US money market fund stress testing requirements under Rule 2a-7. In 2010, the SEC adopted amendments to Rule 2a-7 that, for the first time, required US money market funds to undertake periodic stress tests.¹³ Soon after these amendments, the SEC had several opportunities to assess the effectiveness of the stress testing requirements during periods of market stress—including the 2011 Eurozone debt crisis and the 2011 and 2013 US debt ceiling impasses—and observed that money market funds that had strong stress testing procedures were able to use the results of those tests to better manage their portfolios and better understand and minimize the risk associated with those events.¹⁴

Considering this experience, in 2014, the SEC adopted slight modifications, enhancements, and clarifications to the 2010 amendments to strengthen the stress testing requirements and reduce disparities in the quality and comprehensiveness of stress tests across US money market funds. Specifically, under the 2014 amendments (which became effective in April 2016), a money market fund must test its ability to maintain weekly liquid assets of at least 10 percent and to minimize principal volatility in response to specified hypothetical events, including interest rate increases, evidence of credit deterioration and widening spreads (each in combination with various levels of increases in shareholder redemptions).

Importantly, the current US requirements set forth principles for sound stress testing practices and oversight, but do not attempt to quantify specific parameters or criteria. For example, the requirements do not specify the redemption levels that funds must include in stress testing. Instead, the SEC noted that the appropriate level of redemptions to test will vary among funds, and will depend, for example, on the composition of a fund's investor bases and shareholder redemption preferences, as well as

¹³ See Money Market Fund Reform, SEC Release No. IC-29132 (February 23, 2010), available at <https://www.sec.gov/rules/final/2010/ic-29132.pdf>.

¹⁴ See Money Market Fund Reform; Amendments to Form PF, SEC Release No. IC-31166 (July 23, 2014), available at <https://www.sec.gov/rules/final/2014/33-9616.pdf>.

historical redemption activity in the fund.¹⁵ Similarly, the SEC explains that rather than define by rule which securities the portfolio should test, the fund's manager should determine which security positions would be most informative to the fund's board to test for a downgrade or default of an issuer because the most appropriate security to test for a hypothetical default will vary among funds depending on several factors, including the composition of the fund's portfolio and contemporaneous market events.¹⁶

Recommendation on Stress Testing Guidelines

Based on US money market funds' extensive experience with stress testing, we urge ESMA to follow the SEC's principles-based approach to stress testing, which is similar to Option 1. Although ESMA seems to assume that Option 3 would produce a "happy medium" for stress testing criteria, Paragraph 225 of the CP provides examples of proposed criteria that would require irrelevant testing. These examples include:

- Subparagraphs (c)(ii) and (iii) recommend testing changes in long-term interest rates or changes in the general yield curve. Since all money market funds under the MMFR will be limited to investments with residual maturities of two years or less, changes in rates for longer maturities will not affect the fund's net asset value or liquidity. Testing changes in the short-term segment of the yield curve will produce the same results regardless of whether such changes are associated with shifts or other changes in the overall yield curve.
- To the extent a money market fund invests in assets denominated in another currency than the currency of the money market fund, the fund must hedge the entire currency risk exposure. Testing changes in FX rates as recommended in subparagraph (c)(iv) therefore should not affect the fund's net asset value or liquidity. Testing spread changes in particular sectors would capture changes in short-term interest rates produced by changes in FX rates.
- The "extreme event of stress" proposed in subparagraph (b) will always push the money market fund's net asset value well beyond the permitted thresholds. Indeed, a scenario that would cause 2 to 5 percent of the portfolio to default would generally cause a fund to "break the euro" by itself. Adding an increase in spreads or general rates would make the result marginally worse. We fail to see the point of testing scenarios to reach a foregone conclusion.

The recommended liquidity criteria also assume that money market funds have ready access to data such as bid/asked spreads, trading volume, and active counterparties. Yet, when conducting its liquidity analysis, the EBA noted "an absence of evidence on market liquidity" for some asset classes.¹⁷ The EBA also recognized that although some bonds are held to maturity, the absence of turnover does not imply

¹⁵ Id. at 580.

¹⁶ Id. at 572.

¹⁷ CP at ¶56.

that the bonds are illiquid.¹⁸ Since most money market instruments are held to maturity, trading data for these instruments are not generally available for individual portfolio securities. Funds conducting liquidity stress testing must “bucket” their portfolios, as the EBA did in its analysis, and interpolate general market data for each bucket. The proposed criteria would not recognize these limitations, and any attempt to provide more specific liquidity testing guidance would veer into the “very prescriptive approach” of Option 2.

Finally, the proposed criteria for redemption testing may not be practical for all funds. Money market funds utilize different distribution channels (*e.g.*, direct sold vs. omnibus intermediaries), which provide different forms and amounts of information regarding the underlying customers. Thus, the classifications proposed in Paragraph 234 of the CP may not be feasible for all funds. Funds require more latitude to base redemption testing on other factors, such as historical trading patterns of intermediaries and general market flows.

The proposed guidelines in Section 6.2 of the CP resemble the process that US money market funds followed when developing and revising their stress testing procedures. Differences among money market funds, particularly with regard to their portfolios (prime vs. government) and means of distribution (direct sold vs omnibus intermediaries), however, have led to significant variations in stress testing to accommodate the needs and profiles of different funds. We are concerned that the proposed hybrid approach (Option 3) would not allow for such variations and could reduce the effectiveness of the funds’ stress testing.

* * * *

Should you have any questions or wish to discuss these matters further, please do not hesitate to contact me (+44 207 961 0831 or dan.waters@ici.org) or Jane Heinrichs, associate general counsel (+1-202-371-5410 or jheinrichs@ici.org).

Yours faithfully,

/s/

Dan Waters
Managing Director—ICI Global

¹⁸ CP at ¶64.