May 26, 2012

Via Electronic Mail (MoneyMarket@iosco.org)

Mr. Mohamed Ben Salem
General Secretariat
International Organization of Securities Commissions (IOSCO)
Calle Oquendo 12
28006 Madrid
Spain

Re: Public Comment on Money Market Fund Systemic Risk Analysis and Reform Options

Dear Mr. Ben Salem:

ICI Global (“ICIG”) is pleased to comment on the consultation report, Money Market Fund Systemic Risk Analysis and Reform Options, issued by the Technical Committee of IOSCO (the “Report”).

ICIG is the global association of regulated funds publicly offered to investors in leading jurisdictions worldwide. ICIG seeks to advance the common interests and promote public understanding of global investment funds, their managers, and investors. Members of ICIG manage total assets in excess of US $1 trillion. With respect to assets under management attributable to money market funds outside the United States, a majority of ICIG member assets are money market funds that seek to maintain a stable net asset value (“NAV”); however, ICIG members also manage money market funds described as having a variable NAV.

The Report generally describes the size of the money market fund industry based on available data.


3 We note that the absence of a global definition presents challenges for comparing and analyzing data across jurisdictions.
substantial majority of worldwide money market fund assets and that stable NAV money market funds constitute the majority of worldwide money market fund assets. IOSCO states that the Financial Stability Board (“FSB”) has asked it to undertake a review of potential regulatory reforms of money market funds that would mitigate their susceptibility to runs and other systemic risk, taking into account national initiatives, and develop policy recommendations by July 2012. The Report states that the FSB seeks a review of whether money market funds must (1) be encouraged or required to implement a variable NAV; (2) be subject to capital and liquidity requirements if they seek to maintain a stable or constant NAV; and/or (3) whether there are other possible reforms.4

As an initial matter, we believe IOSCO (and the FSB) provided too short a time period to fully evaluate and respond to this consultation, and particularly to evaluate national initiatives, if implemented. Some jurisdictions may still be considering reforms and others may not feel the need for sweeping change. Further, there is limited information regarding the impact of reforms, specifically the costs and benefits of any changes.

Consequently, we believe it is imperative that (1) an extension be provided or (2) any observations, conclusions or proposed recommendations by IOSCO to the FSB be available for comment. Any final recommendations by IOSCO to the FSB must be public. We also urge the FSB to provide greater transparency regarding its deliberations and the formulation of any recommendations regarding money market funds to allow market participants adequate opportunity to provide input to inform such work.

Fund issues are highly complex on a national level; we submit that consideration of regulatory changes to funds on a global level presents especially difficult challenges and serious risks of unintended consequences. From a range of perspectives, funds, including money market funds, are not homogenous when considered globally. A one-size-fits-all approach is simply unsuitable and unworkable. Accordingly, we urge IOSCO and the FSB to proceed with extreme caution and deliberation.

We have the following broad comments on the Report and address them in more detail below:

- The lack of a clear, global definition of a money market fund is highly problematic when crafting a universal recommendation. As reflected in the Report, there are tremendous differences globally among funds that would fall within the Report’s general description of a money market fund. Without such a definition, the goal of global recommendations raises genuine and serious risks, both locally and globally. There could be exceptionally troubling consequences if reforms were only implemented in some places and not others, or for some so-called money market funds but not others. Rather than seeking global regulatory reforms, we believe an exercise to identify features that have improved the operation of these types of funds would provide meaningful benefits to investors and markets and remain consistent with IOSCO’s history and mission. This work would also contribute to efforts to seek a common definition.

4 Report at pages 2-3.
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• The variety of differing circumstances for money market funds around the world must inform IOSCO’s efforts to develop recommendations for money market funds on a global basis. A global one-size-fits-all approach is neither advisable nor appropriate.
  
  o Money market funds, globally, differ by size of industry, type of investor, and regulatory framework. National tax laws and other laws as well as market conventions also impact the business and management of these funds. National money markets also markedly differ around the world. These features also are all dynamic and changeable over time.

  o Financial turmoil in the period during 2007 and 2008 impacted national markets and money market funds in those markets differently.

• Money market funds are collective investment funds and it is not appropriate to subject them to bank-like regulation. If IOSCO and the FSB are considering regulatory options at the fund level, only measures consistent with the structure of collective investment funds and tailored for local circumstances e.g., measures to strengthen fund liquidity, disclosure, portfolio composition, should be considered. Further, given the role of the money markets for funds, investors, issuers and local economies, measures to strengthen the functioning of the money markets also should be examined.

• We believe the intense focus on the use of amortized cost valuation by money market funds is not an effective or constructive response to addressing the risks identified by regulators. We do not support a mandatory move to variable NAV or a prohibition on using amortized cost valuation.

• We encourage policymakers to engage in further study of national initiatives and reforms of money market funds. There is significant benefit in helping policymakers analyze both the costs and benefits of existing money market fund regulation around the world. We also urge policymakers to consider and assess the degree to which money markets have been strengthened by broader reforms impacting the strength and functioning of the global financial system, including (but not limited to) banking and mortgage lending reforms as well as initiatives related to asset back securities, derivatives and rating agencies.

I. The Absence of a Single Definition of Money Market Funds

IOSCO is seeking to develop recommendations for the global reform of money market funds for the FSB. IOSCO acknowledges, however, that there is no globally accepted definition. As a result, IOSCO, for purposes of the Report, describes a money market fund as “an investment fund that has the objective to provide investors with preservation of capital and daily liquidity, and that seeks to achieve
that objective by investing in a diversified portfolio of high-quality, low duration fixed-income instruments.\(^5\)

A wide range of very different funds in different markets could be brought under this definition. This is apparent from the descriptions of money market funds in the Report. IOSCO's broad description of money market funds raises a primary question as to what features of such a fund makes it "risky" and therefore could be the focus of recommendations to minimize the identified risk.

While not within the Report's definition of a money market fund, the Report identifies the pricing methodology used by money market funds, i.e., stable NAV funds, as presenting a risk when used in this type of fund. We believe that it is difficult to distinguish between stable NAV money market funds and variable NAV money market funds when the portfolios of such funds are composed of the same types of securities (and, especially, when income is distributed). For example, in the United States (and likely in certain other jurisdictions), the stability of money market fund NAVs is primarily due to the composition of their portfolios, rather than amortized cost valuation; as money market fund portfolios are designed, and are essentially required by U.S. regulation, to minimize risk and price fluctuations.

Many money market funds (not all, as depends on a jurisdiction's rules) invest in very short-term securities, and many of the securities have interest rates that reset frequently. These features mean the value of these securities—and hence the money market funds' per-share portfolio value—is extremely stable, regardless of whether the fund would be classified as either a stable or variable NAV money market fund.\(^6\)

We encourage IOSCO to continue to work on a common definition of money market funds through further examination of the regulation of money market funds globally, including as such regulation has been amended or changed, as well as based on the public comments received on this Report. IOSCO should consider common regulatory provisions (e.g., portfolio quality and duration, disclosure,

\(^5\) Report at 1.

\(^6\) In the context of U.S. money market funds, interest rates would have to rise by 1 percentage point in a single day to reduce the portfolio value of the average $1.00 fund with a 45-day weighted average maturity by $0.0012 (about 0.1 cent). Interest rate changes of such dimension are rare. In the past 30 years, there has only been one day (February 1, 1982, to be specific) when three-month U.S. Treasury bill rates changed by more than 1 percentage point.

The stability of money market fund portfolios in the United States is demonstrated in historical data with mark-to-market prices from a sample of these money market funds from 2000 to 2010. For prime funds (those that invest in commercial paper as well as government securities), the average "shadow price" (a money market fund's mark-to-market value) never fell more than 0.1 cent (or .999) below $1.00 until September 2008, when interest rates rose over several days. Even then—at the worst point in the worst financial crisis in 70 years—the average shadow price was only 0.2 cents (or .998) below $1.00. See Investment Company Institute Research Report, Pricing of U.S. Money Market Funds, January 2011 ("ICI MMF Pricing Paper"), available at http://www.ici.org/pdf/ppr_11_mmf_pricing.pdf.
liquidity) as well as best practices along with due regard for how local circumstances may impact the appropriate parameters of provisions.

Given the diversity of circumstances around the world and the challenges of developing a single definition on such a short timetable, we believe IOSCO and the FSB need to carefully reconsider their goals as they examine global reform options for money market funds. Rather than seeking global regulatory reforms, we believe an exercise to identify and examine features that have improved the operation of these types of funds would provide meaningful benefits to investors and markets around the world and contribute to the development of a common definition.

II. The Variety of Circumstances Around the World Impacting Money Market Funds Must Inform IOSCO’s Work

Given the variety of circumstances as well as the risks of unintended consequences, IOSCO must proceed cautiously in considering money market funds on a global basis. We do not believe a global one-size-fits-all approach is advisable.

A. Differences in Regulation, Markets and Investors

The diversity in circumstances around the world for money market funds is obvious from the Report. There is no global definition of a money market fund and this is reflected in a range of approaches. Local conditions clearly impact the functioning and texture of money market funds in each country and region. In some jurisdictions, money market funds are relatively new. Some countries have fairly detailed rules while others do not. Some countries may have tax regimes that influence structure, e.g., accumulating or distributing share classes. Many offer only funds denominated in their local currency; others have money market funds in multiple currencies.

The valuation approaches as described in the Report appear to be from national regulation, including accounting rules in some cases. Nevertheless, more detail would be helpful as there are descriptions of valuations based on “current valuations of assets” or the “fair value of assets and liabilities.” Some jurisdictions appeared to have more precise rules than other jurisdictions regarding the use of amortized cost valuation for the valuation of fund assets. The impact of using so called “mark to market” valuation versus “amortized cost” valuation also does not seem to be well studied on a global basis. In some countries, pricing services provide valuation information; however, the valuation approaches of pricing services or the number of vendors in a market is not examined in the Report. For example, in Mexico, we understand that Mexican law requires investment funds to use independent service providers that are authorized by the Mexican Securities Commission to price and value fund shares.

The Report also describes the approach in China whereby the Securities Association of China publishes monthly valuation information for individual assets held in money market funds.\(^7\) We appreciate that valuation is a complex area and IOSCO’s consultation report, Principles for the Valuation of Collective...
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Schemes, acknowledges there can be challenges in valuing certain securities, particularly if market prices are not readily available. Accordingly, more detail would be helpful for better understanding the valuation methods used in money market funds globally. In particular, a complete understanding of national valuation rules or practices is a necessary prerequisite to any discussion regarding stable and variable NAV money market funds on a global basis.

The investor base of money market funds varies globally. Retail investors dominate in some markets while in others it is a mix of retail and institutional and still others may have primarily an institutional investor base. Many markets have only domestic investors but others have a geographically diverse group of investors. The size of the money market fund sector also is highly variable with some countries having only a small sector and others a larger industry. The markets to which investors gain exposure through a money market fund also are very different, with some countries having smaller and less diverse markets than others. This plethora of circumstances must inform IOSCO’s goals when examining money market funds on a global basis.

The Report did not analyze the range or type of portfolio assets held by money market funds in different jurisdictions, including how portfolio composition may have changed since 2007. We believe that this type of information would be extremely helpful in better understanding what instruments these funds actually hold in different jurisdictions rather than what are permitted investments or are disclosed investment objectives or strategies which can be quite general. This information and analysis would greatly help regulators and the market better understand and assess these funds globally.

B. Financial Turmoil and Money Market Funds

As described in the Report, financial turmoil in 2007 and 2008 impacted money market funds differently in different countries. In the United States, there also were differences in the impact on

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8 See Technical Committee of IOSCO, Principles for the Valuation of Collective Investment Schemes, CR01/12 (February 2012).


10 FitchRatings, Sector Update, European Money Market Funds, September 2011.

11 New requirements in the United States for more frequent disclosure of the portfolio holdings of money market funds has lead to more scrutiny by regulators, analysts and investors. See Investment Company Institute, Submission to IOSCO on Money Market Fund Reform (February 7, 2012) (“ICI February 2012 Submission”) available at http://www.ici.org/pdf/25877.pdf.

12 The Report describes the freezing of the Canadian non-bank sponsored asset-backed commercial paper market but not the reasons for problems in this market. Similarly, issues with liquidity in 2008 and 2009 in India are not detailed. Report at 60.
prime money market funds versus government-only money market funds. The Report also describes issues associated with enhanced or dynamic cash funds in Europe in 2007 and other effects on money market funds in 2008 due to the decision of the U.S. government to allow Lehman Brothers to fail, resulting in a world-wide banking crisis and lack of confidence in financial institutions, as well as the enactment of deposit guarantees by certain European governments. While money market funds in some countries did face challenges during the financial turmoil, the experiences in other countries appear to differ. For example, the Report describes challenges for Canadian money market funds in 2007 due to problems in the Canadian non-bank sponsored asset backed commercial paper market; however the Report states that in September 2008 regulators examined Canadian money market funds and “all funds reviewed were able to meet redemption requests and no investments held in the funds were written down.”

While China, Korea and Japan are the next largest money market fund domiciles in Asia after Australia, the Report does not describe any challenges during this period in money market funds in those jurisdictions. Similarly the Report does not describe any challenges during this period for money market funds in Mexico and Brazil, the two largest domiciles in the Americas after the United States. Actions by national authorities also affected money market funds. In some cases, these national actions helped restore confidence in the money markets and money market funds, yet in other cases there were negative impacts.

We believe differences such as these, and those described above, support our position that policymakers must proceed with caution and not issue global regulatory recommendations. The structure of funds, their investors and markets differ and, further, the action or inaction of sovereigns is of substantial importance to what can occur in different markets and during periods of turmoil.

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13 ICI Viewpoints, Brian Reid, ICI Chief Economist, Money Market Funds Let's Stick to the Facts (March 6, 2012) available at http://www.ici.org/viewpoints/view_12_mmf_bair (For every dollar that came out of prime money market funds, 63 cents went into Treasury and government money market funds. In the week of the Lehman collapse, the assets of taxable money market funds (prime, Treasury, and government funds combined) declined by only 4 percent).

14 There are also past examples of markets experiencing financial turmoil differently. For example, in 2001, we understand that the collapse of Enron caused problems in some Japanese money management funds, leading several funds to have their NAV fall below their principal value. In January 2002, money market fund reforms were enacted in Japan to strengthen these funds. Investment Trusts Association, Japan, Investment Trusts in Japan 2011, at pages 22-23; and Investment Trusts Association, Japan, Investment Trusts in Japan 2008, at pages 48-49.

15 Report at 60.


17 Id.
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III. Bank-Like Regulation for Money Market Funds

We strongly oppose options seeking to impose bank-like regulation or structures on money market funds. We believe such an approach seriously undermines the fundamental nature of a money market fund as a collective investment fund and will confuse investors and market participants.

Banks are highly leveraged, relying on debt in the form of checking and savings deposits, time deposits, long-term bonds and other borrowings to finance their assets. Banks provide financing and other services for a range of persons and entities. As a result of their structure, banks are required to hold capital to protect depositors, other creditors, central banks, and ultimately taxpayers from losses that may arise from a bank’s portfolio of illiquid, opaque assets. Deposit guarantee schemes also exist.

Unlike depositors of a bank, interests of investors in a fund are equity interests, representing a pro-rata share of a fund’s current net assets. In contrast to banks, the principal activities of investment funds are more narrowly focused: investing, reinvesting and trading in securities for the benefit of the fund and its investors. Fund regulation established by national authorities imposes many conditions and limits on these activities, including on leverage, and particularly in the case of rules applicable to money market funds, the types of investments. Transparency and disclosure are also important requirements imposed on regulated funds. For fund investors, collective investment vehicles provide a convenient means to seek economically the market “exposure” that they would obtain through direct market investment in the underlying assets.18 The differences between funds and banks are reflected in the very different laws that govern banking and funds. The regulatory framework of funds, and securities regulation more broadly, reflects policy objectives that promote the protection of investors as well as efficient and well-functioning capital markets.

We believe an approach to make an investment fund bank-like blurs important distinctions and is not helpful to solving the problems identified by regulators. We also do not think options, such as capital, have been considered in a wide range of jurisdictions. Consequently, their possible implementation is far from well understood from many standpoints including specific legal, accounting, or tax issues as well as the national market or economic features that would affect if, and how, such options could operate or be implemented.19 This basic and essential step must first be taken before developing a recommendation for global application.

18 In the case of money market funds, like other funds that primarily invest in fixed income securities, a collective investment vehicle is especially important given the nature of the money market and fixed income markets generally (e.g., high minimum denominations) and, for money market funds, the short term nature of the instruments.

19 While there has been consideration of different ways in which capital-like features could be implemented in the context of U.S. money market funds, we are unaware of similar evaluations in other jurisdictions. See Investment Company Institute, The Implications of Capital Buffer Proposals on Money Market Funds (May 16, 2012) available at http://www.ici.org/pdf/ppr_12_mmfs_capital_buffer.pdf (Study finding that requiring U.S. money market fund advisers to hold capital would fundamentally change the nature of these funds and depending on the size of the capital buffer and the assets covered, a capital buffer could result in advisers shifting
Rather than bank-like regulation, we recommend examining the strengths of approaches drawn from investment fund laws, a framework familiar to investors and the market. We support the analysis of approaches such as those related to disclosure, liquidity, and portfolio assets (e.g., credit quality, instrument duration). The details of such measures, however, must be informed by local regulations, customs and market conditions. We also believe there has been limited attention given to the functioning of the money markets and what measures may strengthen these markets.

IV. Amortized Cost Valuation

We believe that the intense focus on amortized cost valuation, particularly as used by stable or constant NAV funds, is not ultimately helpful to addressing the risks identified by regulators. This valuation method is used by other funds, including both variable and stable NAV money market funds, as well as under international accounting standards. As described in the lengthy submissions of other public commenters on this Report and this topic, amortized cost valuation was not a cause of heavy redemptions in money market funds and its elimination would not have prevented the impacts on money market funds on either side of the Atlantic that occurred during the financial turmoil in 2007 and 2008. As described above, the stability of the NAV of money market funds with high quality, short duration instruments is not simply due to valuation conventions.

We do not support a mandatory move to variable NAV money market funds that cannot use amortized cost valuation.

V. Evaluating National Reforms To Inform Policymaking

We believe it is crucial that IOSCO and the FSB spend more time evaluating those money market fund reforms that have already been implemented, including both the costs and the benefits of such reforms. We note that costs and benefits will vary by jurisdiction and therefore national regulators need time to consider the reforms of other jurisdictions and the advisability of implementing similar or new measures in their own jurisdictions. This type of information is vital, as IOSCO must be aware of the parameters that may practically or legally limit the ability of regulators or markets to implement or support options.

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Many reforms to money market funds are relatively new. Their costs and benefits are only now being assessed, e.g., the United States and Europe. The pan-European definition for money market funds, creating two definitions, was a significant change, and is contributing to improved market transparency and consistency.\(^{21}\) In the United States, the extensive reforms of 2010 are now being analyzed\(^{22}\) and discussion continues on the possibility of more changes. Canadian reforms, such as liquidity requirements and enhanced disclosure, are very new (in 2012).\(^{23}\) Other countries are apparently actively considering money market fund reforms. Some have adopted other changes that impact money market funds. In India, investments by banks in money market funds were limited.\(^{24}\) Although not detailed in the Report, other important and far-reaching regulatory reforms have also been enacted, or are underway, to strengthen and improve the functioning of the financial system more broadly, including banking and mortgage lending reforms, reforms related to asset backed securities and an extensive new regime for derivatives. Important changes to the regulation of rating agencies and the use of ratings also have been areas of change.\(^{25}\) Important analysis remains to be done.

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In summary, we do not think one-size-fits-all recommendations for money market funds on a global basis are workable or advisable and could result in serious adverse consequences. There is substantial work to be completed regarding the impact of existing and recent reforms. Further, the costs and benefits of any additional reforms must be considered. Consequently, we are highly concerned that policymakers are rushing in their deliberations with incomplete information and perspective. We urge IOSCO and the FSB to follow a timetable that will allow full and accurate information to inform a measured analysis of the issues.

\(^{21}\) FitchRatings, Sector Update, European Money Market Funds, September 2011.

\(^{22}\) See ICI February 2012 Submission.


\(^{24}\) Report at 67.

\(^{25}\) Since the onset of the global financial crisis, the G20 has established core elements of a new global financial regulatory framework that are intended to make the financial system more resilient and better able to serve the needs of the global economy. Through the efforts of the FSB, the national authorities and international bodies have further advanced this financial reform program. These include reforms designed to, among other things, improve the soundness of the banking system, address the risks posed by systemically important financial institutions, strengthen the regulation and oversight of non-bank financial intermediation, improve the over-the-counter and commodity derivatives markets, develop “macroprudential” frameworks and tools to identify and monitor systemic risk, strengthen and converge global accounting standards, strengthen adherence to international financial standards, and reduce reliance on credit rating agency ratings. See generally Report of the FSB to G20 Leaders, Overview of Progress in the Implementation of the G20 Recommendations for Strengthening Financial Stability (November 4, 2011), available at http://www.financialstabilityboard.org/publications/r__111104.pdf.
We appreciate your consideration of our views. If you have any questions or need additional information, please contact me at +44 203 009 3101, or Susan Olson, Senior Counsel – International Affairs (+1 202 326 5813).

Sincerely,

/s/

Dan Waters
Managing Director