Updated as at 9 December 2016

MONEY MARKET FUNDS

Text of reference: Draft proposal of the European Commission - 4 September 2013

Link: http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52013PC0615&from=FR

Description

The Financial Stability Board (FSB), created in April 2009 by the G20, has defined ***SHADOW BANKING*** as a system in parallel of credit intermediation, activity traditionally the preserve of banks. It involves entities and activities outside the traditional banking system. For further details on ***SHADOW BANKING*** please refer to **Fact sheet on *SHADOW BANKING*.** Among activities linked to the banking system in parallel so-called ***Shadow Banking*** are included **Money Market Funds**.

Key dates

- 2009 – The Financial Stability Board (FSB), mandated by G20 to issue recommendations to strengthen oversight and regulation of the Shadow Banking.
- 29 August 2013 – The FSB publishes 3 new reports including recommendations to address *Shadow Banking* risks in securities lending & repo activities.
- 4 September 2013 – The European Commission (EC) publishes a draft regulation for money market funds out of the scope of the UCITS 4 Directive.

This Regulation aims at imposing stricter diversification rules and the obligation to put in place a *buffer* for **Money Market Funds** (MMFs) with constant NAV (C-NAV) **(*)**. It forces a buffer of 3% for money market funds with CNAV, despite facing opposition from the industry.

The last version of the Regulation includes diversification rules more stringent (max. 15%/30% in assets with daily/weekly maturity and max 5% in assets issued by a same entity).

Ireland and Luxembourg have C-NAV **(*)** MMFs whereas France has only V-NAV **(*)** for MMFs.

Money Market figures

- European MMFs have assets **around € 1 trillion** (50% C-NAV and 50% V-NAV and **65%** since the **last IOSCO Report**).
- France, Ireland and Luxembourg hold, all 3, **85%** of assets of European MMFs.
- MMFs represent 15% of investment fund assets in Europe.

Critical points

These new investment and diversification rules seem particularly stringent for fund managers and banks to implement and control like maximum 10% of assets with a maximum maturity of one day or additional 20% whose maximum maturity is one week.

The Capital BUFFER cost had been estimated at € 18 billion. Fund managers had to immobilize a reserve of asset in cash. For these managers, if the BUFFER was maintained as such, this would have been the end of the CNAV MMFs. These managers located in Anglo-Saxons countries could have left Europe partly due to tax advantage for their clients. They did not want to convert their C-NAV MMFs into V-NAV MMFs.

The last compromise of the Italian Presidency of the European Council does not make any reference to the Capital Buffer, removed and replaced by liquidity fees and redemption gates, largely inspired from the American Regulation of Money Funds, published by the SEC on 23 July 2014.

Under this last and new version of this draft regulation, CNAV MMF would be allowed to retail investors and to certain categories of investors like pension funds. Valuation rules will remain unchanged.

Chronology

- ✓ **26 February 2015**: Vote in ECON Commission (Economic and Monetary Affairs)
- ✓ **29 April 2015**: Vote in plenary session at the European Parliament

Since April 30th 2015, ECON could have started *trilogue* discussion upon Council approval. However during Latvian Council Presidency and Luxembourg Council Presidency, the trilogues between the Parliament, the Commission and the Council have not been organized for this MMF reform.

*In the meantime **IOSCO** published **end of September 2015** its last report on reforms in respect of money market funds: This report highlights that most of the jurisdictions have a specific and dedicated regulation for money market funds and that some of them have reinforced their regulation regarding CNAV MMF. In 2016 IOSCO will be carrying out a second review of the progress made in the adoption of all MMF reforms. This review could be followed by an assessment of the compliance of those reforms implemented with to IOSCO recommendations.*

- ✓ **5 April 2016**: The Dutch Presidency of the EU Council decided to reactivate this MMF reform by publishing a **4th compromise**. This new text should be the new set up for the MMF.

  We can legitimately wonder why MMF reform has been suddenly put to the agenda of the Dutch Presidency knowing that MMFs are currently facing very low and/or negative performance.

  Capital buffer of 3% has been definitively removed. Like US Money Funds regulation, redemption gates & liquidity fees have been introduced to deal with runs (massive redemption orders). 3 new categories of MMF have been created: **Public Debt CNAV** (assets invested in sovereign debts – 99.5%), **Retail CNAV** for retail investors and public authorities and the **Low Volatility NAV**.

  Two key elements to be considered in this **4th compromise** issued by the Dutch Presidency:

  - External Sponsor Support in order to maintain a stable NAV is prohibited.
  - The **sunset clause** has been deleted for the low volatility category. This clause had been included to convert C-NAV into V-NAV after a five years' period.

  Timeline for EU Money Market Fund Reform in 2016

  - ✓ **10 May 2016:** the Council of the EU published a **new** and **5th compromise** with changes about the holding of ancillary liquid assets and the use of asset-backed securities/ commercial papers.
  - ✓ **15 June 2016:** Agreement on the final text of the MMF reform (version of the 5th Compromise) reached the same day at the Permanent Representatives Committee (COREPER) of the Council.
  - ✓ **Next and likely last step:** The EC waits for the conciliation procedure (TRILOGUE) with a first step, the preparatory meeting between the delegations in order to adopt the final text.
  - ✓ **16 November 2016: The TRILOGUE process is over. A final agreement has been reached. The regulation should come into force by the end of the second quarter 2017, giving normally until beginning of 2019 to be compliant with.**

Contact list at the EU Commission / EU Parliament

RAPPORTEUR: Neena Gill (S&D, UK),

Shadows: Brian Hayes (EPP, IE),

Syed Kamall (ECR, UK),

Philippe Lamberts (Greens, BE)

Petr Jezek (ALDE, CZ)

Eva Joly (greens:EFA, FR)

Steven Woolfe (EFDD, UK)

Alain Lamassoure (EPP, FR)

Contact SGSS/SMI: Jean-Pierre Gomez (Jean-Pierre.Gomez@sgss.socgen.com)

***(*)** A MMF with CNAV is a fund using amortized cost method for asset valuation contrary to MMF with VNAV using mark-to-market method for asset valuation*