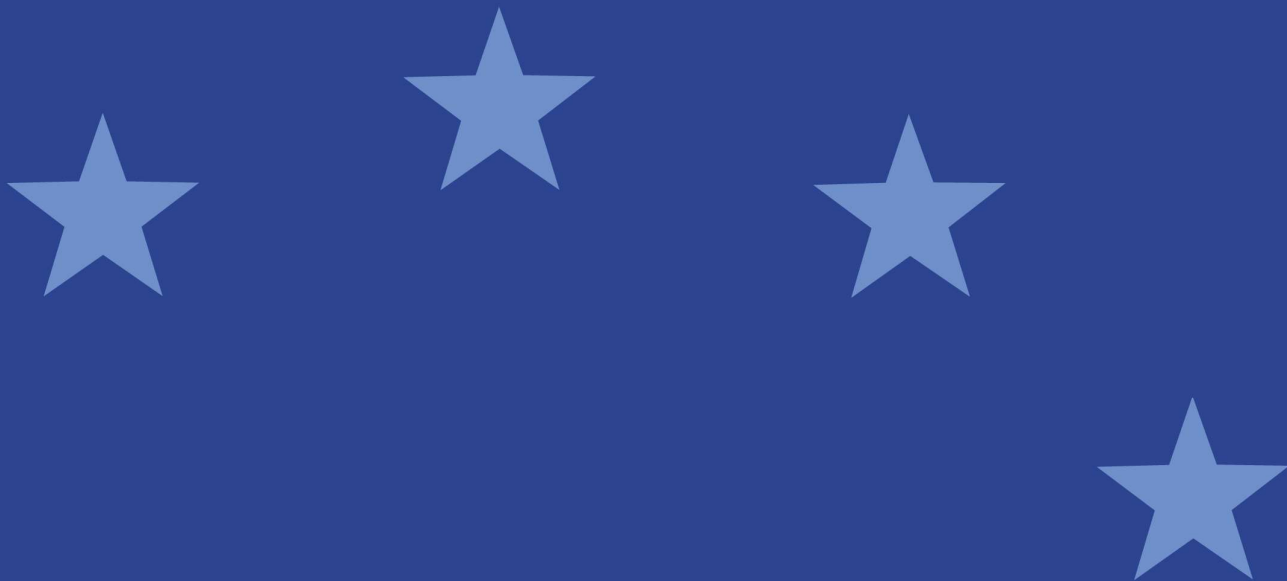


## **Response form for the Consultation Paper on the EU Money Market Fund Regulation – legislative re- view**



## Responding to this paper

ESMA invites responses to the questions set out throughout this Consultation Paper and summarised in Annex 3. Responses are most helpful if they:

- respond to the question stated and indicate the specific question to which they relate;
- contain a clear rationale; and
- describe any alternatives ESMA should consider.

ESMA will consider all comments received by **Wednesday 30<sup>th</sup> June 2021**.

All contributions should be submitted online at [www.esma.europa.eu](http://www.esma.europa.eu) under the heading 'Your input - Consultations'.

### Instructions

In order to facilitate analysis of responses to the Consultation Paper, respondents are requested to follow the steps below when preparing and submitting their response:

- Insert your responses to the consultation questions in this form.
- Please do not remove tags of the type <ESMA\_QUESTION\_MMFR\_1>. Your response to each question has to be framed by the two tags corresponding to the question.
- If you do not wish to respond to a given question, please do not delete it but simply leave the text "TYPE YOUR TEXT HERE" between the tags.
- When you have drafted your response, name your response form according to the following convention: ESMA\_MMFR\_nameofrespondent\_RESPONSEFORM. For example, for a respondent named ABCD, the response form would be entitled ESMA\_MMFR\_ABCD\_RESPONSEFORM.
- Upload the form containing your responses, in Word format, to ESMA's website ([www.esma.europa.eu](http://www.esma.europa.eu) under the heading 'Your input – Open consultations' → 'Consultation on EU Money Market Fund Regulation – legislative review').

### **Publication of responses**

All contributions received will be published following the close of the consultation, unless you request otherwise. If you do not wish for your response to be publicly disclosed, please clearly indicate this by ticking the appropriate box on the website submission page. A standard confidentiality statement in an email message will not be treated as a request for non-disclosure. A confidential response may be requested from us in accordance with ESMA's rules on access to documents. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by ESMA's Board of Appeal and the European Ombudsman.

### **Data protection**

Information on data protection can be found at [www.esma.europa.eu](http://www.esma.europa.eu) under the heading '[Data protection](#)'.

### **Who should read this paper?**

This document will be of interest to (i) MMF managers and their trade associations, as well as (ii) institutional and retail investors (and associations of such investors) investing in MMF.



## General information about respondent

Name of the company / organisation	U.S. Chamber of Commerce, Center for Capital Markets Competitiveness
Activity	Non-governmental Organisation and Other Associations
Are you representing an association?	<input checked="" type="checkbox"/>
Country/Region	North-America

## Introduction

**Please make your introductory comments below, if any:**

<ESMA\_COMMENT\_MMFR\_1>

The U.S. Chamber of Commerce's Center for Capital Markets Competitiveness ("CCMC") appreciates the opportunity to comment on the consultation paper ("Consultation") on EU Money Market Funds Regulation (MMFR) released by the European Securities and Markets Authority ("ESMA").

The U.S. Chamber of Commerce's ("the Chamber") members, many of whom are heavily invested in Europe and maintain global operations, represent a key stakeholder base as the EU considers potential reforms to money market funds (MMFs). MMFs are an integral part of the global financial system, as they provide maturity and liquidity transformation.

MMFs exist for the ease of short-term cash management and investment, and provide economic benefits to issuers and investors, including individuals, governmental entities, and businesses. As the Consultation notes, the "market footprint of MMFs is very high globally," with Euro area MMFs of approximately EUR 1.44 trillion in total assts as of Q4 2020, with funds denominated in Euros, U.S. dollars, and British pounds.

For many businesses, including those that make up the membership of the Chamber, MMFs are the preferred way to manage fluctuations in cash and to ensure adequate cash flow when needed. Businesses benefit from MMFs in two ways—as an investment tool for working capital and as a market for the instruments they issue to finance short-term funding needs. Cash inflows and outflows don't always line up, and MMFs act as a financial intermediary in helping businesses offset these discrepancies.

When companies have a temporary cash shortfall, they often turn to short-term financing instruments, such as commercial paper to bridge the gap. MMFs are significant purchasers of commercial paper, making them a reliable and accessible source of short-term funding for companies. Commercial paper is typically used by companies for financing things like payroll, inventory, and meeting other short-term liabilities. Many businesses prefer commercial paper to bank loans for short-term financing because of the ease and efficiency in issuing commercial paper as well as the lower interest rate.

ESMA's review of MMFs is occurring at the same time that the U.S. Securities and Exchange Commission (SEC) and the Financial Stability Board (FSB) are also reviewing the market turmoil in March 2020 and are considering potential reforms to MMFs. The SEC is currently reviewing comments received in April 2021 in response to recommendations made by the President's Working Group (PWG) on Financial Markets in a December 2020 report "Overview of Recent Events and Potential Reform Options for Money Market Funds."<sup>1</sup> The FSB, on 17 November 2020, issued a report entitled "Holistic Review of the March Market Turmoil"<sup>2</sup> and we expect the FSB, in coordination with IOSCO, to also release a consultation paper by the end of June 2021.

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<sup>1</sup> Report of the President's Working Group on Financial Markets, *Overview of Recent Events and Potential Reform Options for Money Market Funds*, December 2020. <https://home.treasury.gov/system/files/136/PWG-MMF-report-final-Dec-2020.pdf>

<sup>2</sup> Financial Stability Board, *Holistic Review of the March Market Turmoil*, November 17, 2020. <https://www.fsb.org/wp-content/uploads/P171120-2.pdf>



With so many entities evaluating the market for MMFs and offering recommendations for improvements to the markets, the Chamber urges a measured approach to any changes that holistically considers all aspects of short-term funding markets and that preserves the unique benefits provided by MMFs to investors and issuers.<ESMA\_COMMENT\_MMFR\_1>

**Q1 i) Do you agree with the above assessment of the difficulties faced by MMFs during the COVID-19 March crisis? Do you agree with the identification of vulnerabilities? ii) What are your views in particular on the use of MMF ratings by investors? Are you of the view that the use of such ratings has affected the behaviors of investors during the March crisis?**

<ESMA\_QUESTION\_MMFR\_1>

The EU adopted the Money Market Fund Regulation (MMFR) in 2017 with the objectives of providing common standards to (i) ensure stability in the structure of MMFs, (ii) guarantee they invest in well-diversified assets of good credit quality, and (iii) increase liquidity of MMFs.<sup>3</sup>

The market volatility experienced in March 2020 was the first significant test of the effectiveness of the MMFR. Per point 19 of the ESMA Consultation, segments of both the U.S. and EU MMF industry experienced stress and liquidity challenges; however, no EU or U.S. MMF had to implement liquidity fees on redemptions or redemption gates or suspend redemptions.

In particular, there is evidence that LVNAVs and VNAVs in the EU experienced the greatest outflows in March 2020. However, public debt CNAV MMFs performed well during the market volatility and experienced significant inflows as investors sought the liquidity and stability that public debt MMFs provide. Given the greater stress to the performance of LVNAVs and VNAVs, we believe any reforms under consideration should be targeted towards these funds.

The Chamber does not believe inadequate regulation of MMFs was central to the liquidity crisis experienced in short-term funding markets. The FSB expressed similar views in its report on the market challenges for MMFs during the March 2020 market turmoil. The FSB found that, in contrast to the Global Financial Crisis, “the shock originated outside of the financial system,” suggesting that MMFs and their regulatory structure, were in no way a cause of financial instability in March 2020. The report further mentions “some investors in open-ended investment funds may have faced incentives to redeem ahead of others,” but, in general, the FSB takes a holistic review of short-term funding markets, including the role of the banking system and central counterparties.

In line with this, it is important to look at the deteriorating state of liquidity in the underlying markets, as the March 2020 shock occurred due to factors linked to the announcement of lockdowns and not to potential deficiencies of the MMF regulatory framework. The fact that many investors redeemed their shares from MMFs is not connected to the regulatory framework of MMFs but to a variety of reasons, including the management of the cash that they received or paid in relation to margins on their derivative contracts and the need to pay taxes.<sup>4</sup>

<ESMA\_QUESTION\_MMFR\_1>

**Q2 i) Do you agree with the above assessment on the potential MMF reforms related to the review of the MMF Regulation? ii) What are your views on the abovementioned assessment of the interaction between potential MMF reforms and the behaviour of investors during the MMF March 2020 crisis?**

<ESMA\_QUESTION\_MMFR\_2>

As we stated in Question 1, the Chamber does not believe inadequate regulation of MMFs was central to the liquidity crisis experienced in short-term funding markets. However, reforms to MMF regulation

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<sup>3</sup> Council of the EU Press Release, *Money market funds rules adopted*, 16 May 2017. <https://www.consilium.europa.eu/en/press/press-releases/2017/05/16/money-market-fund-rules-adopted/>

<sup>4</sup> European Central Bank, *How effective is the EU Money Market Fund Regulation? Lessons from the COVID-19 turmoil*. [https://www.ecb.europa.eu/pub/financial-stability/macprudential-bulletin/html/ecb.mpbu202104\\_2-a205b46756.en.html#toc6](https://www.ecb.europa.eu/pub/financial-stability/macprudential-bulletin/html/ecb.mpbu202104_2-a205b46756.en.html#toc6)

may be necessary to improve market functioning and improve investor confidence in financial markets, but these reforms should be carefully considered as part of the broader regulatory structure for financial markets. The Chamber supports reforms to financial regulation that will promote liquidity in financial markets. We believe some modest reforms to MMF rules, which would not decrease their utility for issuers or investors, merit discussion. Importantly, the potential reforms would have to consider the importance of the cash equivalent status of MMFs, which makes them attractive to corporate investors.

Additionally, we believe reforms to certain regulations governing capital and liquidity requirements in the banking system are essential to holistically support liquidity in short-term funding markets. Changes to banking regulation, including more flexibility under the Liquidity Coverage Ratio (LCR), merit serious discussion as part of a holistic review, particularly since banks play a central role as intermediaries and liquidity providers for commercial paper. In March 2020, banks understandably withdrew from short-term markets when faced with uncertainty and requirements to maintain their own capital and liquidity. In particular, expanding the definition of high-quality liquid assets (HQLA) to include the highest rated commercial paper would improve bank intermediation in short-term funding markets so that banks can provide greater liquidity.

If ESMA should determine that updates to the MMFR are warranted, the Chamber strongly recommends that they be narrowly applied to address funds that experienced demonstrable liquidity challenges in March 2020. As part of ESMA's thorough review of March 2020 and existing MMF regulations, we urge you to consider the effects and potential unintended consequences of any regulatory modifications under consideration. It is also important to consider that, in the EU, MMF shares are almost exclusively held by institutional investors, who tend to redeem their shares more quickly than retail investors. Depending on the reform, issuers and investors could move their activity to other types of MMFs, bank products, or possibly outside of the regulated financial markets. An increase in demand for liquidity from banks, for example, could simply mean a shift in market activity from MMFs to credit products like term loans and lines of credit. <ESMA\_QUESTION\_MMFR\_2>

**Q3 Do you agree with the above assessment of the i) potential need to decouple regulatory thresholds from suspensions/gates and the corresponding proposals of amendment of the MMF Regulation ii) potential reforms of the conditions for the use of redemption gates? When you answer this question, please also take into account the grid of criteria listed in paragraphs 76 to 80.**

<ESMA\_QUESTION\_MMFR\_3>

The Chamber encourages ESMA to focus any review of MMF regulation on the removal of the tie between liquidity and liquidity fees on redemptions and redemption gates. We agree with the assessment made in the PWG report that "Definitive thresholds for permissible imposition of liquidity fees and redemption gates may have the unintended effect of triggering preemptive investor redemptions as funds approach the relevant thresholds."

The MMFR requires public debt CNAVAs and LVNAVAs to institute liquidity fees and redemption gates on investors to disincentivize runs. MMF boards have discretion to impose fees (equal to the cost of liquidity) or gates when weekly liquid assets (WLA) fall below 30 percent of total assets. These reforms were well-intentioned, but the regulatory linkage between the MMF's requirement to maintain 30 percent WLA and the imposition of redemption gates may have been a contributing factor to unnecessary outflows on LVNAVAs in March 2020.

Despite the absence of actual liquidity risk, the tie between gates and fee thresholds created a first-mover advantage among some investors. Staff at the Federal Reserve Bank of New York foresaw this possibility when it published research in 2014 entitled, "*Gates, Fees, and Preemptive Runs*," finding that redemption gates could have the opposite effect as intended – they may actually encourage runs

in some cases.<sup>5</sup> The report found that, “Rules that provide intermediaries, such as MMFs, the ability to restrict redemptions when liquidity falls short may threaten financial stability by setting up the possibility of preemptive runs.” The report also pointed out the possibility of behavior that may be economically irrational, noting, “...given the similarity of MMF portfolios, is that a preemptive run on one fund might cause investors in other funds to reassess whether risks in their funds are indeed vanishingly small.” Requiring the fund’s board to meet when the 30 percent WLA threshold is breached caused investors confronting market uncertainty in March 2020 to be concerned about draconian redemption measures being imposed by the board despite the fund’s relatively high liquidity and no requirements to impose gates and fees.

Reforms should improve the signaling about the board’s intentions to investors. The Chamber believes that greater research is required to better understand investor behavior regarding the possibility of fund boards imposing gates and fees. Such research should inform potential changes to the MMFR that delink gates and fees.<ESMA\_QUESTION\_MMFR\_3>

**Q4 i) Do you agree with the above assessment of the potential need to require MMFs to use swing pricing and / or ADL / liquidity fees and the corresponding proposal of amendment of the MMF Regulation (including the above list of corresponding potential benefits and drawbacks)? ii) If you are of the view that swing pricing might not be workable for certain types of MMFs, which instruments would you suggest as an alternative for these types of MMFs going forward? When you answer this question, please also take into account the grid of criteria listed in paragraphs 76 to 80.**

<ESMA\_QUESTION\_MMFR\_4>

The Chamber is concerned about the growing discussion of instituting “swing pricing” for MMFs. Swing pricing has recently been opined on in public speeches by policymakers; however, a complete discussion and review of the technical and operational complexities of swing pricing has yet to occur.

Swing pricing is intended to impose the fund’s *trading costs* associated with an investor’s redemption from a fund directly on that redeeming investor. The more overall shares that are redeemed from the fund, the costlier the redemptions. This is accomplished by reducing (“swinging” down) the fund’s NAV when a certain percentage of shares are redeemed.

Although some may offer that swing pricing could reduce the first-mover advantage by imposing a cost when redemptions are high, we do not believe swing pricing would be effective for curtailing runs. We highlight below several drawbacks to swing pricing for MMFs.

It is important to note that swing pricing may cause volatility in the short term, as it can deter advance notice of large trades. In fact, a fund using swing pricing might thus be more prone to experience greater price volatility when the NAV swings than when it does not.<sup>6</sup>

Trading costs are minimal for securities held by MMFs. If there were a large wave of redemptions, the trading costs do not create any meaningful dilution in the funds. As a result, swinging the NAV by an amount based on trading costs would be relatively small. This “swing” in price would then need to be compared against an investor’s desire to redeem shares. There would be relatively low disincentive given the increased desire to redeem shares in the face of relatively low increase in trading costs.

An additional drawback of swing pricing is the likelihood that MMFs would have no choice but to eliminate intra-day and same-day settlements, since MMFs would face significant difficulties in being able

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<sup>5</sup> Federal Reserve Bank of New York Staff Reports, Gates, Fees, and Preemptive Runs (Staff Report No. 670), April 2014. [https://www.newyorkfed.org/medialibrary/media/research/staff\\_reports/sr670.pdf](https://www.newyorkfed.org/medialibrary/media/research/staff_reports/sr670.pdf)

<sup>6</sup> Columbia Business Law Review, *Will Swing Pricing Save Sedentary Shareholders?*, March 21, 2018. <https://core.ac.uk/download/pdf/267804852.pdf>



to collect and evaluate all inflows and outflows of the fund so that an accurate swing price could be determined. Such changes would leave investors worse off.

Importantly, and as pointed out in the PWG report, the increased costs and operational complexity from swing pricing “could lead to increased concentration and a reduction in the overall size of the MMF industry,”<sup>7</sup> which could increase the cost of capital in short-term markets and have serious unintended consequences for financial stability.

Furthermore, we have to underline that in the EU context, the different mutual fund market timing adds a further layer of complexity in swing pricing. This happens given the different timeframe between EU and U.S. markets closing of the trading day and the time funds have to process orders while striking the NAV.

Importantly, even in Europe, where many jurisdictions use swing pricing, neither the AIFMD nor the UCITS legal framework includes swing pricing as a mandatory tool. In the same vein, a report from the Association of the Luxembourg Fund Industry (“ALFI”) underlines that the main drivers behind the non-adoption of swing pricing “range from the effort and operational complexity it would take to implement to concerns about client understanding in certain markets and the acceptance of the practice.”<sup>8</sup> <ESMA\_QUESTION\_MMFR\_4>

**Q5 i) Do you agree with the above assessment of the potential need to increase liquidity buffers and/or make them usable/countercyclical and the corresponding potential proposal of amendment of the MMF Regulation? ii) With respect to option 1 above, views are sought in particular on the relevant threshold (on the size of redemptions) from which WLA would need to be automatically adjusted. When you answer this question, please also take into account the grid of criteria listed in paragraphs 76 to 80.**

<ESMA\_QUESTION\_MMFR\_5>  
TYPE YOUR TEXT HERE  
<ESMA\_QUESTION\_MMFR\_5>

**Q6 What are your views on the potential need to eliminate CNAV and LVNAV funds, in light of the recent market developments, and the corresponding potential proposal of amendment of the MMF Regulation? When you answer this question, please also take into account the grid of criteria listed in paragraphs 76 to 80.**

<ESMA\_QUESTION\_MMFR\_6>

As in Question 2, we urge ESMA to fully consider the effects and potential unintended consequences of any proposed recommendation such as eliminating certain funds. Such reforms could see issuers and investors move their activity to other types of MMFs, but also to bank products or possibly outside of regulated financial markets.<ESMA\_QUESTION\_MMFR\_6>

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<sup>7</sup> Report of the President’s Working Group on Financial Markets, *Overview of Recent Events and Potential Reform Options for Money Market Funds*, December 2020. <https://home.treasury.gov/system/files/136/PWG-MMF-report-final-Dec-2020.pdf>

<sup>8</sup> Association of the Luxembourg Fund Industry, *Swing pricing survey, reports & guidelines*. (2011). [https://www.alfi.lu/getattachment/13c3dc27-2efc-450f-95ab-156e73c4946c/app\\_data-import-alfi-swing-pricing-survey.pdf](https://www.alfi.lu/getattachment/13c3dc27-2efc-450f-95ab-156e73c4946c/app_data-import-alfi-swing-pricing-survey.pdf)

**Q7 What are your views on the extent to which Article 35 of the MMF Regulation should be i) clarified ii) amended? When you answer this question, please also take into account the grid of criteria listed in paragraphs 76 to 80.**

<ESMA\_QUESTION\_MMFR\_7>  
TYPE YOUR TEXT HERE  
<ESMA\_QUESTION\_MMFR\_7>

**Q8 i) Do you agree with the above assessment of the potential need to assess the role of MMF ratings in light of the difficulties faced by MMFs during the March crisis, and the potential need to introduce regulatory requirements for MMF ratings? ii) In your view, based on your experience, what are the benefits of MMF rating from investors' perspective, having in mind that rules applying to MMFs are already very stringent? What would be the likely consequence on investors from the downgrade of one or several MMFs? When you answer this question, please also take into account the grid of criteria listed in paragraphs 76 to 80.**

<ESMA\_QUESTION\_MMFR\_8>  
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<ESMA\_QUESTION\_MMFR\_8>

**Q9 Do you agree with the above assessment of the potential need to amend the requirements on stress tests included in the article 28 of the MMF Regulation? When you answer this question, please also take into account the grid of criteria listed in paragraphs 76 to 80.**

<ESMA\_QUESTION\_MMFR\_9>  
TYPE YOUR TEXT HERE  
<ESMA\_QUESTION\_MMFR\_9>

**Q10 Do you agree with the above assessment on the potential need to review the reporting requirements under the MMF Regulation? When you answer this question, please also take into account the grid of criteria listed in paragraphs 76 to 80.**

<ESMA\_QUESTION\_MMFR\_10>  
TYPE YOUR TEXT HERE  
<ESMA\_QUESTION\_MMFR\_10>

**Q11 Do you agree with the above assessment of the potential need to include additional requirements in the MMF Regulation, and/or potentially in other types of EU piece of legislation on the disclosure of money market instruments (MMIs) and main categories of investors to regulatory authorities (e.g. detailed information on liabilities)? When you answer this question, please also take into account the grid of criteria listed in paragraphs 76 to 80.**

<ESMA\_QUESTION\_MMFR\_11>  
TYPE YOUR TEXT HERE  
<ESMA\_QUESTION\_MMFR\_11>

**Q12 i) Do you agree with the above assessment on the potential creation of a LEF? When you answer this question, please also take into account the grid of criteria listed in paragraphs 76 to**

**80. ii) Several open questions related to the creation of the LEF, on which ESMA would specifically welcome feedback from stakeholders, include:**

- **What should be the appropriate size of such a pooling vehicle as the LEF?**
- **In terms of funding, how much MMF would have to pay each year to participate in the pool? How much of the funding would/should be provided by other sources?**
- **How long would it take to establish such a LEF?**
- **Under which conditions would the LEF be activated?**
- **Who would be responsible for activating the LEF.**

<ESMA\_QUESTION\_MMFR\_12>  
TYPE YOUR TEXT HERE  
<ESMA\_QUESTION\_MMFR\_12>

**Q13 Do you agree with the above assessment on the potential need of further clarification of the requirements of articles 1 and 6 of the MMF Regulation? When you answer this question, please also take into account the grid of criteria listed in paragraphs 76 to 80.**

<ESMA\_QUESTION\_MMFR\_13>  
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<ESMA\_QUESTION\_MMFR\_13>