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AmCham EU's position on Money Market Funds

Money market funds ("MMFs") perform a vital role as intermediaries between borrowers in search of short-term funding and investors seeking low risk cash management solutions. We believe that the key features of money market funds offer the greatest protections to investors while enabling MMFs to play an important role in the capital markets. These features include constraints on a fund's liquidity and maturity of holdings, diversification and credit quality requirements, portfolio transparency and clear governance requirements. All of these practices have proven effective in increasing the resilience of MMFs in the United States.

The American Chamber of Commerce to the EU (AmCham EU) appreciates the European Commission's policy initiatives aimed at addressing money market fund regulation as well as financial intermediation risks outside the banking sector. However, we would also underline the need to strengthen alternative liquidity in the financial markets to deal with Europe's current funding needs.

It is our concern that if EU and US governments fail to develop a framework that will allow MMFs to invest in a wide range of money market instruments, there is a real risk that liquidity issues for sovereigns will become exacerbated.

In addition, companies worldwide are in need of efficient cash management solutions. Preservation of these solutions is especially important at a time where current market outlooks make it difficult for companies to adequately plan their treasury inventory.

It is crucial that EU and US authorities act to coordinate their approach, to create a level playing field and consistent risk approach for investors, market participants and fund sponsors. Any new reforms to MMFs should be based upon sound economic analysis.

A number of policy measures have been suggested in both the EU and the US, such as enhanced portfolio restrictions, enhanced client disclosure, floating net asset value (NAV), gates, and we provide comments on some of these measures here.

Enhanced portfolio restrictions

AmCham EU would encourage that consideration be given to the amendments made in the US to SEC Rule 2a-7 in 2010. Various provisions in the 2010 amendment were useful in strengthening the resiliency of MMFs, including the imposition of daily and weekly liquidity requirements, tightening of credit and diversification limitations and improvements in portfolio holdings disclosure.

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POSITION STATEMENT

The SEC's current ideas out for consultation do not propose investment limitations for repo collateral. On the other hand, the European Commission's intention to impose limits on the amount of collateral types may result in MMFs ceasing to engage in repo transactions. The vast majority of repo collateral consists of long dated sovereign paper. Due to the fact that financial market participants will continue to need financing for their securities collateral, entities less regulated than MMFs may fill the void if MMFs no longer are engaged in these repo transactions.

Furthermore, we have concerns over restrictions on MMF investments in asset backed commercial paper, and believe the exclusion of asset-backed commercial paper (ABCP) will have broader and negative economic effects. We estimate that over 80% of underlying ABCP assets represent loans to businesses and consumers. A ban would result in higher costs for end users and fewer loans to businesses.

Enhanced disclosure

To ensure that investors clearly understand the underlying volatility in MMF investments, many fund sponsors in the industry have begun voluntarily disclosing the market-based NAV of the underlying investments. This information is very valuable in allowing investors to compare the relative risks of various MMFs, and should be required of all MMFs as part of any regulatory reform.

Credit ratings

We understand that the European Commission may be considering suggesting restrictions on the solicitation of credit ratings by managers of MMFs. In our view, this would actually increase systemic risk to the industry. Harmful consequences would include reduced transparency and uncertainty about the creditworthiness of a MMF's investments. Furthermore, a ban on the solicitation of credit ratings could set a dangerous precedent. No other piece of EU legislation has gone as far as to remove the right of market participants to ask for ratings, moreover, such a prohibition would contradict the approach of CRA3 (Regulation 462/2013), amending the EU CRA Regulation (Regulation 1060/2009). Rather than restricting the use of solicited ratings, we feel a more appropriate policy approach would be to encourage a higher number of assessments on MMFs. AmCham EU considers it more appropriate to gradually remove regulatory mandates that require the use of credit ratings as set out in the Financial Stability Board's "Principles for reducing reliance on CRA ratings" of October 2010. These FSB principles also set out a balanced approach regarding the use of credit ratings in investment mandates and funds' investment rules.

Floating NAV

A central concern that has been articulated is that MMFs that operate a stable or constant net asset value (CNAV MMFs) are particularly susceptible to runs.

CNAV MMFs serve a broad range of investors all with similar objectives, and have a range of characteristics that make them useful investment vehicles, including daily liquidity, administrative efficiency in respect of tax and financial bookkeeping, professional credit risk management, competitive returns and sound governance.

The objective of both CNAV and variable net asset value (VNAV) MMFs is to provide investors with security of capital and high levels of liquidity. They achieve that objective by investing in a portfolio of high quality, low duration money market instruments. The likelihood of investors redeeming is determined by the quality of the assets held by the fund and the levels of liquidity held, and not by the accounting procedure used. There is no material difference between the underlying assets and therefore no greater susceptibility to runs in one type of fund or the other. Therefore we do not believe a conversion from CNAV to VNAV MMF will prevent client redemptions in times of market stress. There is evidence that some VNAV MMF in Europe had issues in 2007 and 2008 and faced substantial decreases in value over very short time periods.

Further, a requirement for CNAV MMFs to float NAVs would fundamentally reshape the product and its ability to deliver these core benefits to investors. Floating the NAV has the benefits of providing transparency of market values to investors and reducing the possibilities for transaction activity that result in non- equitable treatment across all shareholders; however, it will likely give rise to a number of consequences for investors and market participants that should be examined rigorously and addressed in order to arrive at a constructive solution.

Gates

Many funds in Europe provide for a gate, whereby redemptions in excess of 10% of the NAV of the fund may be deferred. This is a very useful tool in slowing a run on a fund.

Conclusion

It is evident that there is no single "solution" to address regulatory concerns around MMFs. A combination of several thoughtful initiatives, selectively applied and rigorously implemented, could have a significant impact in improving the resiliency of these funds to ensure their continued value for investors and short-term market participants.

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AmCham EU speaks for American companies committed to Europe on trade, investment and competitiveness issues. It aims to ensure a growth-orientated business and investment climate in Europe. AmCham EU facilitates the resolution of transatlantic issues that impact business and plays a role in creating better understanding of EU and US positions on business matters. Aggregate US investment in Europe totalled €1.9 trillion in 2012 and directly supports more than 4.2 million jobs in Europe.

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