MEMO# 35640

March 8, 2024

ICI Global Responds to UK FCA Consultation on MMF Reforms

[35640]

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TO: ICI Members
ICI Global Members
Europe Regulatory and Policy Committee
Global Operations Advisory Committee
Money Market Funds Advisory Committee SUBJECTS: Financial Stability
International/Global
Money Market Funds RE: ICI Global Responds to UK FCA Consultation on MMF Reforms

On 8 March, ICI Global filed a response to the UK Financial Conduct Authority's (FCA) consultation on updating the regime for money market funds (MMFs) (the Consultation).[1] The Consultation proposed revisions to the retained Money Market Fund Regulation (MMFR), with an intent to tailor the MMF regulatory framework for the UK market. ICI Global's response is summarized below.

ICI Global highlighted the importance of MMFs to the financial system. We encouraged evaluating any reform options by comparing their impact on the ability of MMFs to fulfil this role (i.e., preservation of their key characteristics) against the likely practical impact any MMF reforms will have on making the overall financial system more resilient. Any new reforms for MMFs must be measured and appropriately calibrated, taking into account the costs and benefits these funds provide to investors, the economy, and the short-term funding markets.

We also provided observations on the potential interaction between changes to UK MMF liquidity requirements and the forthcoming HM Treasury determination of whether the EU and UK MMF frameworks are equivalent. We urged UK authorities to consider ways to proceed that would avoid outcomes such as confusion in the markets and constrained the availability of MMFs in the UK.

On the FCA's proposed changes to the retained MMFR, ICI Global provided the following comments.

- Liquidity management tools (LMTs). We supported the FCA's determination to not propose to mandate the use of macro-prudential swing pricing. While the Consultation proposed to require MMF managers to have access to specific LMTs (i.e., suspensions and an anti-dilution levy or adjustment), we welcomed the proposed flexibility fund managers would have to implement these tools, including how to respond when there is a breach of liquid asset limits and how to calibrate LMTs and activation thresholds. We supported the FCA's position that fund managers should exercise this discretion in a manner that prioritises the best interest of investors.

- Removal of regulatory link. We strongly supported the removal of the regulatory link between liquidity levels in MMFs and the need for a manager to consider or impose tools such as liquidity fees or redemption gates, because such a regulatory link makes MMFs more susceptible to financial stress.
- Minimum weekly liquid assets (WLA). We recommended no increase to the WLA requirements because an increase is:
  - Unnecessary. Removing the regulatory link will enhance the existing, well-functioning requirements. Fund managers will be able to access their WLA, removing the unintended hard liquidity floor.
  - Based on flawed modelling. The Bank of England's modelling contains two assumptions that are, in our view, overly restrictive and may materially overstate the results. With these assumptions removed, we believe the model will show MMFs can sustain higher redemption rates with WLA at a level lower than the proposed 50 percent.
  - Lacks appropriate calibration. If increased the FCA nevertheless determines to increase the liquid asset requirements, we recommended a WLA increase to 40 percent, rather than the 50 percent that has been proposed.
  - Disproportionately impacts variable NAV (VNAV) funds. We recommended that the FCA consider the performance of UK-domiciled VNAV funds prior to determining that there is a need to adjust WLA for VNAV funds and the appropriate extent of any such adjustment.
- "Know your customer" (KYC). We supported the retained KYC provisions, but we did not support the proposed revisions, which would fail to achieve the intended outcomes of enhancing MMF resilience and mitigating risks associated with correlated investor behaviour.

In response to a question posed in the Consultation, ICI Global also provided some insights on the challenges that would make a commercial borrowing facility for MMF liquidity in a stress event unviable.

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Notes

[1] For a summary of the Consultation, see ICI Memo #35554.