

MEMO# 35927

November 19, 2024

IOSCO Publishes Consultations on Liquidity Risk Management in OEFs

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TO: ICI Members

ICI Global Members

Asia Regulatory and Policy Committee

Europe Regulatory and Policy Committee

Operations Committee

SEC Rules Committee SUBJECTS: Financial Stability

International/Global RE: IOSCO Publishes Consultations on Liquidity Risk Management in OEFs

On 11 November 2024, the International Organization of Securities Commissions (IOSCO) published two related consultations on liquidity risk management in open-end funds (OEFs): (i) [Revised Recommendations for Liquidity Risk Management for Collective Investment Schemes](#) (Revised Recommendations); and (ii) [Guidance for Open-ended Funds for Effective Implementation of the Recommendations for Liquidity Risk Management](#) (Proposed Guidance) (collectively, the Consultations).^[1] Comments on both Consultations are due on 11 February 2025 and must be submitted by electronic form.

The Consultations are intended to be read together and update IOSCO's 2018 recommendations and guidance on liquidity risk management (LRM) for OEFs.^[2] They are intended to:

- 1) operationalise the Financial Stability Board's (FSB) 2023 Revised Policy Recommendations to Address Structural Vulnerabilities from Liquidity Mismatch in Open-ended Funds (FSB Revised Recommendations),^[3]
- 2) reflect market and policy developments since 2018, including IOSCO's 2023 Anti-dilution Liquidity Management Tools - Guidance for Effective Implementation of the Recommendations for Liquidity Risk Management for Collective Investment Schemes (ADT Guidance),^[4] and
- 3) improve readability.

The questions in both Consultations are limited and specific. IOSCO instructs commenters

to limit their responses to short, targeted answers to these questions, providing examples and supporting details where requested or relevant. Commenters are instructed explicitly not to comment on aspects of the documents that were part of the 2023 consultation on anti-dilution tools (ADTs). However, the Consultations each have a "catch all" question which asks whether there are comments that do not fall within the scope of the targeted questions.

Scope

Consistent with IOSCO's earlier work, the Revised Recommendations address open-ended Collective Investment Schemes (CIS), with a focus on OEFs. IOSCO indicates in the text that certain recommendations also may be applicable to closed-end CIS. The Proposed Guidance focuses on OEFs.

IOSCO explicitly excludes money market funds and exchange-traded funds from the scope of the Revised Recommendations and the Proposed Guidance because of their unique characteristics and specialized guidance for these types of funds.

The Consultations are addressed primarily to "responsible entities," such as fund managers or fund boards, who are responsible for the overall operation of the fund, particularly including compliance with the applicable legal and regulatory framework. The Revised Recommendations also address the role of securities regulators.

Overview of the Consultations

The Revised Recommendations and Proposed Guidance cover a broad scope of liquidity management tools (LMTs), although the covered tools are not intended to exhaustively describe all LRM tools and measures. The Consultations incorporate recent policy work on anti-dilution LMTs (ADTs) and include new and updated consideration of quantity-based LMTs (QBTs) and other liquidity management measures (LMMs). Consistent with the ADT Guidance and the FSB Recommendations, the Consultations seek to ensure jurisdictions make LMTs broadly available, so that OEFs are able to select and implement LMTs as appropriate for the fund in normal and stressed market conditions. The LMTs discussed in the Consultations include:

ADTs

QBTs

Other LMMs

Swing pricing

Suspension of redemptions and subscriptions

Side pockets

Valuation at bid/ask prices

Redemption gates

Redemptions In-kind/in-specie

Dual pricing

Extension of notice periods

Credit facilities

Anti-dilution levy

Extension of settlement periods

Interfund lending

Subscription/redemption fee

Despite the broader scope, the approach IOSCO takes in revising the recommendations and proposing new guidance is largely consistent with its earlier policy work on OEF LRM. IOSCO acknowledges the diversity of funds, and that there is no one-size-fits-all approach to LRM. In addition, IOSCO explicitly affirms that responsible entities are best placed to and have responsibility for LRM, which they execute through the exercise of "sound professional judgment in the best interests of investors."[\[5\]](#) The Consultations generally are outcomes-focused, promoting flexible approaches to LRM. IOSCO does indicate that certain LMTs are suitable to all types of funds and highlights complexities of implementing certain tools, such as redemptions-in-kind, in certain funds. However, the Consultations do not recommend that certain types of funds select and implement particular LMTs.

The Consultations observe that some regulators have authority to direct the use of LMTs and cautions that this power "has rarely deemed to be necessary for the purpose of orderly market function and financial stability reasons and should be kept for extreme cases."[\[6\]](#)

The Consultations highlight a few general concerns that are each addressed at several points in the Revised Recommendations and Proposed Guidance. While the earlier policy work focused on redemptions, the Consultations add text regarding OEFs' other liabilities, with an aim to ensure that OEFs can meet liquidity demands from margin and collateral calls and other liabilities.[\[7\]](#)

Citing concerns of fairness and investor protection, the Consultations generally state that LMTs should apply to all redeeming investors in the same way with no differentiation by type of investor or share class.

IOSCO encourages responsible entities to exercise professional judgment to achieve a balance between ADTs, QBTs, and other LMMs. IOSCO also cautions against "exclusive reliance" on QBTs because of the potential for unintended consequences, such as triggering redemptions. Rather, QBTs are generally permitted and used in "exceptional circumstances," which "could be understood as unforeseen events and/or operational/regulatory environments that have a material impact on the OEF's ability to carry out normal business functions and activities and which would temporarily prevent the manager to meet the funding obligations arising from the liabilities side of the balance sheet [\[8\]](#)

The Consultations also include an increased emphasis on the importance of appropriate valuation procedures.[\[9\]](#)

Revised Recommendations

The Revised Recommendations update IOSCO's 2018 Recommendations and are designed to support the effective exercise of responsible entities' professional judgment in normal and stressed market conditions, throughout the fund's lifecycle.

There are seventeen recommendations with a revised structure that cover six areas:

- 1) design process,
- 2) LMTs and other LMMs,
- 3) day to day liquidity management practices,
- 4) stress testing,
- 5) governance, and
- 6) disclosures to investors and authorities.[\[10\]](#)

The questions regarding the Revised Recommendations are directed to recommendations that are new or have substantial changes, including the following:

- Recommendation 3 addresses the consistency of OEF asset liquidity and redemption terms.[\[11\]](#)
- Recommendation 6 refers to the consideration and implementation of a broad set of ADTs, QBTs, and other LMMs.[\[12\]](#)
- Recommendation 7 address the uses of ADTs. This recommendation is new, drawing from the ADT Guidance and FSB Revised Recommendations.[\[13\]](#) There are no questions addressed to this recommendation because it was the subject of the 2023 consultation on the ADT Guidance.
- Recommendation 13 addresses effectively maintaining the liquidity risk management process with adequate and appropriate governance.[\[14\]](#)
- Recommendation 17 focuses on disclosures to investors regarding the use of ADTs, QBTs, and other LMMs. This recommendation is new but the explanatory text combines elements of the ADT Guidance and Good Practices.[\[15\]](#)

Proposed Guidance

The Proposed Guidance incorporates and supersedes the Good Practices and the ADT Guidance. Focusing on OEFs, the Proposed Guidance has nine elements intended to facilitate the effective implementation of the Revised Recommendations with illustrative effective examples. Each of the elements provides a reference to the relevant revised recommendations.

Proposed Guidance 1 and 2 discuss approaches to minimise structural liquidity mismatch, addressing how to determine asset and portfolio liquidity (Proposed Guidance 1) and consistency between portfolio liquidity and redemption terms (Proposed Guidance 2). This section offers technical details to facilitate implementation of the FSB's Revised Recommendation on fund categorisation according to the liquidity of the fund's assets. The

U.S. Securities and Exchange Commission's rule 22e-4 is used to illustrate an approach to determining asset liquidity.^[16] IOSCO includes a discussion of the role of liquidity buffers in LRM but cautions that such requirements can have unintended consequences and does not recommend a minimum liquidity buffer across the OEF sector.^[17] IOSCO also reviews regulatory limits on illiquid assets, such as in the U.S., as a means of contributing to consistency between the liquidity of the fund's assets and the redemption terms.^[18]

In Proposed Guidance 3-8, IOSCO sets forth a framework for the design and use of LMTs and other LMMs, extending the structure from the ADT Guidance to also cover QBTs and LMTs. Proposed Guidance 3 provides general considerations for the framework, including governance and disclosure to investors. As an illustration, the Proposed Guidance outlines the best governance practices identified in the UK Financial Conduct Authority's multi-firm review of OEF LRM in 2023.^[19]

Proposed Guidance 4-6 are not open to consultation because they pertain to ADTs.^[20]

Proposed Guidance 7 and 8 are new and address types of QBTs and other LMMs (Proposed Guidance 7) and appropriate activation and deactivation of QBTs and other LMMs (Proposed Guidance 8).

Proposed Guidance 9 covers the design of stress testing scenarios.

The Proposed Guidance also incorporates the discussion of barriers and disincentives to implementation of LMTs from the ADT Guidance.

Next Steps

The Consultations express strong expectations that securities regulators will implement the Revised Recommendations in their jurisdictions. IOSCO will monitor implementation. As described in the FSB Revised Recommendations and ADT Guidance, this review will start with a stocktake to be completed by the end of 2026. The findings from the stocktake will inform an assessment of whether Revised Recommendations, the Proposed Guidance, and the FSB Revised Recommendations "have sufficiently addressed risks to financial stability."^[21] This assessment will consider whether existing tools need refinement or additional tools should be developed.

Kirsten Robbins
Associate Chief Counsel, ICI Global

Notes

^[1] IOSCO, [Revised Recommendations for Liquidity Risk Management for Collective Investment Schemes](#) (11 November 2024) (Revised Recommendations); IOSCO, [Guidance for Open-ended Funds for Effective Implementation of the Recommendations for Liquidity Risk Management](#) (11 November 2024) (Proposed Guidance) (collectively, the Consultations).

^[2] IOSCO, [Recommendations for Liquidity Risk Management for Collective Investment Schemes](#) (1 February 2018) (2018 Recommendations); IOSCO, [Open-ended Fund Liquidity and Risk Management - Good Practices and Issues for Consideration](#) (1 February 2018) (Good Practices).

[3] FSB, [Revised Policy Recommendations to Address Structural Vulnerabilities from Liquidity Mismatch in Open-ended Funds](#) (20 December 2023) (FSB Revised Recommendations). See Memo [35575](#) for a summary of this report.

[4] This includes IOSCO's recent guidance on anti-dilution liquidity risk management tools. IOSCO, [Anti-dilution Liquidity Management Tools - Guidance for Effective Implementation of the Recommendations for Liquidity Risk Management for Collective Investment Schemes](#) (20 December 2023) (ADT Guidance). See Memo [35575](#) for a summary of this report.

[5] Revised Recommendations at 10; Proposed Guidance at 8.

[6] Revised Recommendations at 12. See also Proposed Guidance at 40.

[7] See, e.g., Revised Recommendations at 10, 20, 24, 34-36; Proposed Guidance at 18, 39, 53, 57.

[8] Proposed Guidance at 38-39. See also Revised Recommendations at 27-28. While the term "exceptional circumstances" is used in the Revised Recommendations, it is only defined in the Proposed Guidance.

[9] See, e.g., Revised Recommendations at 24. As noted in IOSCO's workplan, IOSCO is undertaking a review of its [Principles for the Valuation of Collective Investment Schemes](#), which were published in 2013, to determine whether updates are necessary that take into account the outcomes of the OEF LRM work as well as work on emerging risks in private finance. IOSCO, [Update to IOSCO 2023-24 Work programme: March 2024-2025 Workplan](#) (12 April 2024) at 5.

[10] While the 2018 Recommendations covered the same topics, the recommendations were structured around a fund's lifecycle- design phase, day-to-day LRM, and contingency planning. The new structure puts greater emphasis on the LMTs, which may be used in normal or stressed conditions, and highlights the importance of governance, stress testing, and disclosures.

[11] Revised Recommendation 3 combines and updates Recommendations 3 and 4 from the 2018 Recommendations. The substantial revisions incorporate Recommendation 3 of the FSB Revised Recommendations, which IOSCO finds provides a baseline framework for categorising assets. IOSCO also identifies relevant features of redemption terms beyond notice periods, including lock-up periods, settlement periods, and redemption caps.

[12] Revised Recommendation 6 includes substantial changes from Recommendation 17 of the 2018 Recommendations. While the text on ADTs draws from the ADT Guidance and the FSB's Revised Recommendations, the discussions of QBTs and other LMMs are new. See ADT Guidance 1-3; FSB Revised Recommendation 4.

[13] See ADT Guidance 1-3; FSB Revised Recommendation 5.

[14] Revised Recommendation 13 combines and updates Recommendations 8 and 9 from 2018 and incorporated the ADT Guidance (see ADT Guidance 4-5).

[15] See ADT Guidance 6; Good Practices at 11.

[16] Proposed Guidance at 12-13.

[\[17\]](#) Proposed Guidance at 18.

[\[18\]](#) Proposed Guidance at 19.

[\[19\]](#) Proposed Guidance at 23-24.

[\[20\]](#) Proposed Guidance 4 focuses on types of ADTs, Proposed Guidance 5 describes calibration of liquidity costs for ADTs, and Proposed Guidance 6 considers appropriate activation thresholds for ADTs.

[\[21\]](#) Revised Recommendations at 6.

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