THE INVESTMENT FUNDS INSTITUTE OF CANADA
L'INSTITUT DES FONDS D'INVESTISSEMENT DU CANADA
IFIC

Via Electronic Mail (moneymarket@iosco.org)

June 28, 2012

Mr. Mohamed Ben Salem
International Organization of Securities Commissions (IOSCO)
Calle Oquendo 12
28006 Madrid
Spain

Dear Mr. Ben Salem:

Re: Money Market Fund Systemic Risk Analysis and Reform Options

We are writing to express our Members' comment on the consultation report on Money Market Fund Systemic Risk Analysis and Reform Options (the "Report") issued by the Technical Committee of the International Organization of Securities Commissions ("IOSCO").

The Investment Funds Institute of Canada ("IFIC") is the national association of the Canadian mutual funds industry. Our Members include fund managers, distributors and industry service organizations (including accounting, legal and other service providers). The Canadian mutual fund industry is comprised of investment fund managers that sponsor, manage and administer funds, and dealer and broker firms that distribute funds' securities. As of March 2012 the mutual fund industry in Canada represented about CAD $813 billion in total assets under management in highly-regulated, publicly offered mutual funds.

IFIC is also a long-standing member of The International Investment Funds Association ("IIFA"), and serves as Secretariat to that Association. We are aware that IIFA is also submitting a comment letter on the Report (the "IIFA Letter"). Our letter is largely based on the IIFA letter, and repeats its main arguments, but provides additional local information about the Canadian money market fund industry in order to substantively illustrate the advantages of local and regional regulation from the Canadian experience.

11 KING ST. WEST, 4TH FLOOR, TORONTO, ONTARIO, M5H 4C7 TEL 416 363-2158 FAX 416 861-9937 WEBSITE www.ific.ca

Investment Funds Should Not be Regulated as Banking Products

We reiterate the fact noted in the IIFA letter that there are substantial differences between investment funds and the banking industry, and that it is critical for IOSCO and the Financial Stability Board ("FSB"), in any consideration of potential policy options for money market funds, to fully consider, and recognize the unique and substantively different roles investment funds and banks play in the global financial system. IOSCO's member regulators are most familiar with these differences and hence, IOSCO has a role to ensure they are equally understood by the FSB.

Investment funds are vehicles that provide collective investment and ownership of assets through the issuance of equity shares ("units"), with such units representing a *pro rata* interest in a fund. In Canada, in similar fashion to other major jurisdictions, authorized publicly-available investment funds, and the intermediaries that offer their units for sale, are subject to nationally harmonized securities regulations that impose strict requirements on the management of the funds (including regulation of their investment activities), the authorization of the management firms and their employees to perform fund management, compliance and portfolio management activity, and the authorization and operating practices of intermediary distribution firms and their representatives to offer the units of such funds for sale to investors.

Investment funds invest in portfolio securities, providing a convenient and affordable conduit for investors to economically seek the market exposure that they would obtain through direct investment in the underlying assets. In contrast, banks transform private short-term securities or claims into private credit. The managers of investment funds typically operate on the basis of an agency relationship, and not on the basis of trading of the manager's own assets.

Because investment funds differ significantly in their business and operation models, we believe it is imperative that bank-like regulation not be imposed upon investment funds.

Money Market Funds are Critical to the Short-Term Debt Markets

We completely endorse the IIFA's presentation on the importance of money market funds in the short-term debt markets, how they offer a valuable intermediation service between lenders and borrowers in the short-term debt markets and how they offer investors low-cost access to credit expertise, diversification, liquidity management and secure and efficient operational processes that would be prohibitively expensive to the majority of cash investors outside of pooled investment vehicles.

In considering appropriate money market fund regulatory changes, noted further below, the securities regulators in Canada well understood this role in the unique context of

the Canadian short-term debt market, and the different composition of unitholders in Canadian money market funds, in contrast to the experience of U.S. and European money market funds.

No "One Size Fits All" Approach

As noted in the IIFA Letter, IOSCO wisely questions whether the differences between jurisdictions require different policy approaches, or whether a global solution would be preferable. It must be borne in mind that money market fund oversight globally has evolved to different levels of regulation appropriate to the local environment and characteristics in each jurisdiction. IFIC agrees with IIFA that the differences that already exist in the local/national regulations applicable to money market funds – including the differing degrees of investment restrictions imposed on funds – and the local market conditions – including the types of investors, tax treatment, banking and securities laws – are so significant and fundamental as to make the crafting of detailed world-wide regulatory approaches inappropriate.

Along with IIFA, we believe that implementation on a national level of a regulatory approach promoted by IOSCO that does not take into account the unique characteristics of a particular jurisdiction's money market fund industry could create unintended adverse consequences, rather than help mitigate risks. As a consequence, each jurisdiction's regulator is in the best position to understand the local market, and therefore is best able, and should be allowed, to define which rules funds must follow to be permitted to be a "money market fund" in its own national/regional market.

To emphasize this point, we note that strong and conservative Canadian regulation permitted the Canadian banking sector to remain one of the strongest in the world throughout and after the market crisis in 2008. More broadly, the Canadian economy as a whole performed better and did not suffer the depth of recession experienced by other nations. We submit that this was a result of prudent, made-in-Canada regulation that ensured the economic sectors were appropriately understood and regulated.

More specifically, the Canadian money market fund industry did not experience similar problems to those encountered by such funds in some jurisdictions. Canadian money market funds functioned as designed and withstood the liquidity crisis of 2008-2009 without a single fund "breaking the buck" or otherwise collapsing. This fact was confirmed in a report released by the Ontario Securities Commission[1] which noted that during the review period all Canadian money market funds were able to meet

[1] Ontario Securities Commission Staff Notice 33-733 *Report on Focused Reviews of Investment Funds, September 2008 – September 2009* available at http://www.osc.gov.on.ca/documents/en/Securities-Category3/sn_20100119_33-733_rpt-rev-inv-funds.pdf.

redemption requests, no investments held by the funds defaulted or were written down, and that virtually all funds were in compliance with the securities laws regulating money market funds.

As regards liquidity redemption risk, the Report concluded (at page 16):

> "Fund managers did not have issues in meeting redemption requests by fund investors. In addition, they did not foresee issues in meeting future redemption requests given the high level of liquidity of their portfolios."

As we noted earlier, Canadian regulators have implemented liquidity buffers appropriate to the unique Canadian capital marketplace. These measures recognized several unique aspects about the Canadian money market fund industry, including (a) that the significant majority of investors in Canadian money market funds are individual retail investors, which creates a much lower risk of massive immediate large–dollar redemptions by a single unitholder, and (b) that the Canadian short-term debt market is much smaller and less diverse than in other jurisdictions that have elected to implement a broader set of measures. The significant uniqueness of each local market makes it imperative that IOSCO not propose a "one size fits all" approach.

Many of the policy options under consideration by IOSCO would represent fundamental structural changes to the money market fund industry. While the benefits that the proposed policy options would bring are unclear, we believe that a fundamental change to the regulation of money market funds would create substantial uncertainty and potentially systemic risk. We therefore urge IOSCO and other regulatory authorities to exercise extreme caution as they proceed in the consideration of money market fund reforms.

<u>No Capital Buffers and Mandatory Floating NAV</u>

Finally, along with IIFA, we strongly disagree with the policy options in the Report that would require funds to establish a capital buffer and would impose a mandatory move from constant net asset value ("CNAV") to variable net asset value ("VNAV").

As has been argued, money market funds are investment products, whose risks and reward are borne by their investors. Requiring money market fund managers to back-stop losses, and to provide for those losses through a capital requirement, would fundamentally undermine the economic viability of money market funds, and would convert them from an investment product into a *de facto* banking product.

We also do not support a global ban of CNAVs (which would amount to prohibiting the use of amortized cost valuation for any securities held by a money market fund). We share the view that there is appropriate space in the global money market fund industry

for both CNAV and VNAV funds, provided of course that each category is subject to an appropriate regulation. Again we would refer you to the reforms already implemented by regulators in the US, Europe and Canada to strengthen the resilience of money market funds.

We would also refer IOSCO to the comment letters that have been, and that will be filed by various national and regional associations that are members of the IIFA for more detail on the concerns raised by the policy options described in the Report, including capital buffers and mandatory VNAV.

Given the very short consultation period on the Report we also request that IOSCO consider providing a comment/consultation period on its final recommendations, before they are submitted to the FSB. If this is not possible, we request that IOSCO provide assurances that any recommendations it proposes to make to the FSB be public so that the public and the industry can make comments to the FSB. Further, the work of the FSB should also be subject to public consultation.

* * * * *

We appreciate the opportunity to express our views. Please contact Ralf Hensel at rhensel@ific.ca or at 1-416-309-2314 if you have any questions about our comments, or if you would like to discuss them in more detail.

Very truly yours,

Joanne De Laurentiis
President and CEO