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- **Public comment on IOSCO's Consultation Report on Money Market Fund Systemic Risk Analysis and Reform Options**

Dear Mr. Ben Salem.

Thank you for giving us the opportunity to comment on your Consultation Report CR07/12 "Money Market Fund Systemic Risk Analysis and Reform Options".

The report provides a good review and analysis of: the role of MMFs in funding markets; their characteristics and risks including systemic risk; the role of MMFs in the 2007-2008 financial crisis; and relevant current and planned regulatory initiatives. I agree that guidance and action is required in order to mitigate the susceptibility of money market funds (MMFs) to runs, and to address the risks that MMFs pose to financial stability.

Credit quality, maturity and liquidity standards

Constant net asset value money market funds (CNAV funds) refer to funds that use amortized cost accounting to value their assets and / or share price rounding method, enabling them to maintain a constant value of the fund. The most important issue to address here is that investors expect a constant value, and we have to address their reasonable expectations. CNAV funds should only be allowed to use amortized cost accounting or share price rounding if they meet globally coordinated, prudent credit quality, maturity and liquidity standards. This is a reasonable regulatory approach, which should act to alleviate some of the obvious concerns with CNAV funds, and help to meet investors' expectations. I would even go further and recommend that sponsors of CNAV funds should be required to adopt procedures for stress testing their funds' ability to maintain a stable NAV for investors. This is a very useful procedure that will help sponsors to better understand the risk drivers, and their impact on CNAV fund values.

Shadow pricing

I would also recommend that sponsors of CNAV funds should be required to adopt shadow pricing procedures. This is absolutely necessary in order to better manage the risks of CNAV funds and also the reasonable expectations of investors. I would recommend a general principle that, should the difference between the shadow price and the amortized cost price be greater than ½ %, the sponsor would be required to take action to reduce dilution of investors' interests or other inequitable results to investors in the fund. Given the current low interest rate environment, it may even be necessary, in order to balance and protect investors' interests, to apply a lower threshold than ½ %.

Redemptions

Short-term suspensions or restrictions on redemptions in times of market stress are a useful method of protecting investors from the harmful effects of extraordinary levels of withdrawals during a period when the shadow price is materially different from the amortized cost price. This will reduce dilution of investors' interests or other inequitable results to investors in MMFs. I do accept that suspending or restricting redemptions reduces the attractiveness of MMFs to investors, who value the ability to redeem at short notice, and therefore such suspensions or restrictions should only be introduced in times of market stress, and where extraordinary levels of withdrawals would lead to dilution or other inequitable results to investors.

Summary

Money market funds have received a lot of bad press during the recent financial crisis,[1] but my suggested proposals, either alone or together, would help to alleviate some of the obvious concerns with MMFs, whilst maintaining their key features and attractiveness to investors. The proposals are generally accepted, and should therefore be relatively easy to implement. They represent a pragmatic, targeted and balanced approach to improving the regulation of MMFs, mitigating their susceptibility to runs, and therefore addressing the risks that MMFs pose to financial stability.

Yours sincerely

C.R. Barnard

Chris Barnard

[1] See for example Wednesday catastrophe: breaking the buck, The Financial Times, 17/8/2008, available at: http://ftalphaville.ft.com/blog/2008/09/17/15992/wednesday-catastrophe-breaking-the-buck/