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May 28, 2012

Mr. David Wright
Secretary General
International Organization of Securities Commissions
Calle Oquendo 12
28006 Madrid
Spain

Dear Mr. Wright:

Re: Money Market Fund Systemic Risk Analysis and Reform Options (Consultation Report)

I. Preface

The Investment Trusts Association, Japan (hereafter, "JITA") appreciates the opportunity to provide these comments in response to the proposed Consultation report, "Money Market Fund Systemic Risk Analysis and Reform Options " which was made public on April 27, 2012 by Technical Committee of the International Organization of Securities Commissions.

JITA was established in July 1957 under a license of the Minister of Finance, which was the governing authority at that time, for the purposes of protecting investors and promoting sound development of investment trusts in Japan. JITA is positioned as "Authorized Financial Instruments Firms Association" under the Financial Instruments and Exchange Act of Japan, and the purposes and the scope of business of JITA are defined by the ACT. JITA comprises of 125 full members including investment trust management companies, and 20 supporting members including securities companies and custodian banks.

JITA would like to express our comments regarding the report.

II. Proposal for the Consultation Report, "Money Market Fund Systemic Risk Analysis and Reform Options"

First of all, please note that this discussion paper does not extensively cover all the propositions due to the short amount of time in making an extensive research on potential reform options.

In the first section, we would like to express our opinions about the appropriate regulations in broad perspective.

Regarding the Question 32, *"Do differences between jurisdictions require different policy approaches or would a global solution be preferable, notably to ensure a global level playing field?,"* it seems to be inappropriate to impose universal restrictions on every MMF in the world, because some policy options may not be suitable to MMFs in some countries even though those options may be found to be feasible.
Therefore, in principle, MMF regulations should be established for each country considering the fact that each country has different legal structures and market practices. And restrictions included in common regulations should be limited to such options as could be effective and feasible to every MMF.
Meanwhile, as a result of different policy approaches, some of these potential options (e.g., Move to VNAV, Funding NAV Buffers) can be imposed only on MMFs in specific countries. It is assumed that a detailed analysis will be required on how the introduction of such options could affect MMFs in regulated countries, and eventually, international short-term money market or MMFs in unregulated countries.

In addition, there might be a room for reconsideration about Definitions of MMF.
In the consultation report, MMF is referred as "*investment funds marketed as "money market funds" as well as collective investment schemes (CIS) which uses close terminologies for their marketing (e.g. "cash" or "liquid" funds) or which are presented to investors and potential investors as having similar investment objectives even though they are labelled differently*".[1]
In the world, not only in Japan, there are many funds marketed as "money fund" or "cash fund" that invest in short maturity securities. And according to the reference above, all of those funds appear to be subject to the potential regulations. However, some of those funds do not offer transaction account services and payment system unlike so-called "MMF". Given the recent discussions about the regulations of MMF in the context of building stricter regulations on shadow banking activities, funds subject to regulations should specifically be limited only to funds with transactional functions.
In Japan, "money reserve funds (MRFs)" offer transaction account services and payment system, but it is thought that the systemic risk raised by MRFs is very limited for the following reasons.
a) In principle, MRFs are not used for the purpose of settlement other than securities settlement.

[1] See OICV-IOSCO, MMF Systemic Risk Analysis and Reform Options, 27th April 2012

b) Unit-holders of MRFs are confined almost exclusively to retail investors.
c) The role of MRFs in short-term funding market is not very significant.

In the following part, we would like to continue our proposal about individual policy options.

4.1.1: Move to variable NAV

One of the alternatives to counter the systemic risk of CNAV has been that of prohibiting the use of amortized cost valuation for any securities held by a MMF and converting to VNAV. In Japan, implementing VNAV is highly challenging due to high implementing costs and the risk of losing transactional functions in payment system.
Fundamental feature of MRF is that investors purchase and redeem at 1 currency unit per share. If VNAV is introduced, it is inevitable to modify the entire payment system at all the retailers based on this feature. The questions are whether it is possible or not as well as how much it would cost to alter the whole system.
If such problems were not solved, the payment system itself would be lost.

4.2: MMF valuation and pricing framework

Another suggestion has been discussed that certain securities with short maturities or high credit rating could be subject to amortized cost accounting. This option poses the difficulties in calculating CNAV because CNAV can be maintained with the premise that all the assets held by MMF are valued at amortized cost accounting method. Hence it seems highly unfeasible.

4.1.2.1: With NAV Buffers

(a) Market-funded NAV buffers--- Subordinated shares

In some countries including Japan, almost all of the funds are established as contractual type investment trusts. It appears to be highly difficult for such contractual type of fund to issue subordinated shares.

(b) Shareholder-funded NAV buffer --- Version 1

This alternative is to retain a portion of MMF income to fund an internal NAV buffer that absorbs initial losses. Considering the current environment in Japan where the level of interest rates has been low over the long term, it appears sceptical that the MMF income could be enough to serve as NAV buffer. Hence, it may not be an effective option to set a certain portion of MMF income aside as NAV buffer.

(d) Sponsor-funded NAV buffer

Although this option appears to be feasible, it might not be necessary if we could construct a framework in which affiliated companies (including sponsors) could purchase the securities held under MMFs to preserve investors' capital.

4.3 Options regarding liquidity management

4.3.2.1.1: Liquidity fees

This proposition argues that investors have to pay redemption fees when a certain market event or the volume of redemptions require. In this case, the most important point is that the conditions under which MMFs charge redemption fees should be fully disclosed from the perspective of accountability. But setting those conditions would make it impossible to make a flexible response according to market environment and cash flows. Also, as indicated in the consultation paper, it is highly likely that this alternative would encourage shareholders to engage in a pre-emptive run if they fear that the situation may require the fee to be imposed.

Moreover, imposing the liquidity fee implies that there is a possibility for MMFs to "break the buck," which leads to the conclusion that it also threatens the transaction account services and the payment system.

4.3.2.1.2: Minimum balance requirement

There is also a discussion that money market funds could be required to have minimum balance requirements which would be held back for a specified period of time and might book loss if the MMF loses value during the holdback period.
This option seems to be far-fetched from the view point of its feasibility, because its methodology or practice has not been discussed clearly and thoroughly.
If the whole expenditure including transaction cost in redeeming the portion other than minimum balance requirement is finally born by the fund overall, the expected role of this option which should contribute to the equality among beneficiaries is extremely limited, even if minimum balance is retained during the specified holdback period.
Furthermore, it is highly unrealistic to manage each shareholder's minimum balance at retailers because it would significantly increase the complexity of managing each account.
The same problem is true of discussions about "Know your shareholder" or "Require/permit MMFs to impose gate".

Sincerely yours.

Kazutoshi Inano
Chairman
The Investment Trusts Association, Japan