A Guide to Money Market Funds under the MMFR

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1. INTRODUCTION

A money market fund (**"MMF"**) is a type of mutual fund that invests in short term assets such as money market instruments (**"MMIs"**) issued by credit institutions, governments or corporations (e.g. treasury bills, commercial paper and certificates of deposit).

Historically there were two main types of MMFs in Europe:-

- A constant net asset value (**"CNAV"**) MMF
  CNAV MMFs aim to preserve a stable value (such as €1) per share at which investors either subscribe or redeem. The net asset value of the assets held by a CNAV MMF can be subject to fluctuation resulting in a situation in which the market value of a share may not always equal the stable value per share (i.e. €1). To address this, a CNAV MMF employs amortised costs to value its assets.

- A variable net asset value (**"VNAV"**) MMF
  VNAV MMFs offer subscriptions or redemptions at a price equal to the MMF's net asset value per share. The value is calculated by subtracting the liabilities of the MMF from the market value of its assets, and is stated on a per share basis.

Investors tend to prefer CNAV MMFs to VNAV MMFs mainly because of their stable net asset value, avoidance of capital gains tax implications and expedited settlement.

MMFs are a considerable source of short-term financing for credit institutions, governments and corporations. For investors, MMFs are mainly used to invest excess cash within short timeframes and offer diversification of their investment portfolio while maintaining a high level of liquidity.

MMFs in issue in the EU manage assets of approximately €1 trillion representing approximately 15% of the EU's fund industry. As of 31 May 2017, Irish domiciled MMFs had assets under management of approximately €486.5 billion reflecting Ireland's status as the leading European domicile for MMFs.

The financial crisis of 2007 – 2008 shed light on several features of MMFs that make them vulnerable when there are difficulties in financial markets, in which circumstances a risk of contagion across the EU could ensue. In particular, when the prices of assets in which an MMF has invested start to decrease, especially during stressed market situations, the MMF cannot always facilitate redemptions immediately and preserve the principal value of shares issued by the MMF to investors. That situation could trigger sudden redemption requests on a massive scale, so called "runs", potentially triggering broader macroeconomic consequences (e.g. impacting credit institutions that significantly rely on MMFs as a source of short term funding).

Although Guidelines on a common definition of European money market funds were adopted by the Committee of European Securities Regulations on 19 May 2010 to address some of the vulnerabilities of MMFs highlighted during the financial crisis and to create a level playing field for MMFs in the EU, the Guidelines were not applied by all EU member states and therefore different national approaches prevailed.

Pursuant to the G20 commitments to establish direct regulation of MMFs, the European Commission proposed in 2013 an EU regulation on MMFs providing for the harmonisation of prudential requirements aimed at inter alia enhancing the liquidity and stability of MMFs in Europe.

After protracted negotiations, the Council and the European Parliament reached political agreement on the final text of the Regulation on MMFs (the **"MMFR"**) in November 2016. The Council formally adopted the MMFR on 16 May 2017 following the Parliament's approval of the agreed text on 5 April 2017. The MMFR entered into on 20 July 2017 (having been published in the Official Journal of the European Union on 30 June 2017) and will become effective from 21 July 2018 with the exception of certain provisions imposing obligations on the European Commission to adopt delegated acts and implementing technical standards, which provisions came into effect on 20 July 2017.

Consequently the provisions of the MMFR will not impact new MMFs until 21 July 2018 and existing UCITS and AIFs that meet the definition of an MMF under the MMFR will have 18 months (i.e. by 21 January 2019) to comply with the requirements of the MMFR and submit an application to their national competent authority for authorisation under the MMFR.

The purpose of this briefing is to summarise and clarify the:-

- Key elements of the MMFR i.e.
  - scope;
  - types of MMFs;
  - investment policy requirements regarding eligible assets, diversification, concentration and credit quality;
  - risk management requirements regarding portfolio rules (such as WAM, WAL and liquidity buckets), MMF credit ratings, know your customer and stress testing;
  - valuation and dealing requirements;
  - specific requirements for Public Debt CNAV MMFs and LVNAV MMFs;

  - external support; and
  - transparency / reporting requirements;
- Next steps in the implementation of the MMFR;
- Implications for existing MMFs; and
- How Dillon Eustace can assist.

2. KEY ELEMENTS OF THE MMFR

2.1 Scope

The MMFR lays down rules for MMFs established, managed or marketed in the EU and applies to collective investment schemes that:-

- require authorisation as UCITS or are authorised as UCITS under Directive 2009/65/EC as amended (the **"UCITS Directive"**) or are AIFs under Directive 2011/61/EU as amended (the **"AIFM Directive"**);
- invest in financial assets with a residual maturity not exceeding two years; and
- have distinct or cumulative objectives offering returns in line with money market rates or preserving the value of the investment.

An MMF may not undertake any of the following activities:

- short selling of MMIs, securitisations, asset-backed commercial paper ("**ABCPs**") and other MMFs;
- take direct or indirect exposure to equity or commodities;
- enter into securities lending agreements or securities borrowing agreements, or any other agreement that would encumber the assets of the MMF; and
- borrow and lend cash.

2.2 Types of MMFs

MMFs may be set up as one of the following types under the MMFR:-

- a VNAV MMF;
- a Public Debt CNAV MMF; or
- a LVNAV MMF.

The "LVNAV MMF" or low volatility net asset value MMF is a new category of MMF and has been made available as a viable alternative to existing CNAV MMFs given:-

- LVNAV MMFs may apply the amortised cost method of valuation to their assets that have a residual maturity of up to 75 days. However, where the difference between the market value of any asset and the amortised cost method of valuation of that asset does deviate by more than 0.10%, the price of that asset must be calculated using its market value; and

- LVNAV MMF may only offer shares for subscription or redemption at a constant net asset value per share where such price does not deviate by more than 0.20% from the net asset value per share of the MMF calculated in accordance with market prices.

In the context of CNAV MMFs, the MMFR introduces a change in that they are required to invest at least 99.5% of their assets in public debt instruments, reverse repos subject to certain conditions and in cash and accordingly are named "public debt constant net asset value money market funds" or "Public Debt CNAV MMFs".

MMFs must be classified as either:

- Short-Term MMFs; or
- Standard MMFs.

Although Short-term MMFs may be structured as Public Debt CNAV, LVNAV or VNAV MMFs, Standard MMFs may only be structured as VNAV MMFs i.e.

	Short-Term MMF ("ST MMF")	**Standard MMF ("STD MMF")**
Public Debt CNAV	✓	X
LVNAV	✓	X
VNAV	✓	✓

Compared to Short-Term MMFs, Standard MMFs are subject to less onerous requirements under the MMFR relating to:

- weighted average maturity (**"WAM"**) and weighted average life (**"WAL"**);

  The MMFR imposes portfolio maturity limitations such as the maximum allowable weighted average maturity (WAM) and weighted average life (WAL). WAM is used to measure the sensitivity of an MMF to changing money market interest rates and WAL is used to measure the credit risk, and limit the liquidity risk, of an MMF's portfolio.

Short-Term MMFs have the objective of offering money market rate returns while ensuring the highest possible level of safety for investors. Consequently in order to ensure that duration risk and credit risk of Short-Term MMFs are kept at low levels, both the WAM and WAL must be kept at low levels. However Standard MMFs are permitted to avail of extended portfolio maturity limits and therefore both the WAM and WAL may be kept at higher levels.

- the financial instruments eligible for investment by the MMF as detailed below under "Eligible Assets"; and

- the liquidity requirements for assets in the portfolio of the MMF (as detailed below under "Portfolio Rules").

2.3 Investment Policy Requirements

2.3.1 Eligible Assets

An MMF may invest only in one or more of the following categories of financial assets:-

- MMIs

  MMIs are eligible subject to the following conditions:-

  (a) they must fall within one of the categories of eligible MMIs provided for in the UCITS Directive (excluding MMIs which fall within the 10% unlisted bucket provided for in the UCITS Directive);
  (b) they must have a legal maturity at issuance of 397 days or less; or have a residual maturity of 397 days or less. However Standard MMFs are allowed to invest in MMIs with a residual maturity until the legal redemption date of less than or equal to two years, provided that the time remaining until the next interest rate reset date is 397 days or less; and
  (c) the issuer of the MMI and the quality of the MMI must have received a favourable assessment pursuant to the internal credit quality assessment to be carried out by the manager of the MMF in accordance with the provisions of the MMFR.

- Eligible securitisations and ABCPs

  Both a securitisation and an ABCP are eligible for investment by an MMF provided that the securitisation or ABCP is sufficiently liquid, has received a favourable assessment pursuant to the internal credit quality assessment to be carried out by the manager of the MMF in accordance with the provisions of the MMFR, and is any of the following:

(a) a securitisation that constitutes a "Level 2B Securitisation" under the Liquidity Coverage Ratio Commission Delegated Regulation (EU) 2015/611 made under the EU Capital Requirements Regulation (575/2013) ("**CRR**");
(b) an ABCP issued by an ABCP programme which (i) is fully supported by a regulated credit institution; (ii) is not a re-securitisation and the exposures underlying the securitisation at the level of each ABCP transaction do not include any securitisation position; and (iii) does not include a synthetic securitisation; or
(c) a simple, transparent and standardised (STS) securitisation or ABCP.

A Short-Term MMF may invest in the securitisations or ABCPs referred to above provided any of the following conditions is met, as applicable:-

(i) the legal maturity at issuance of the securitisation referred to in point (a) above is two years or less and the time remaining until the next interest rate reset date is 397 days or less;
(ii) the legal maturity at issuance or residual maturity of the securitisations or ABCPs referred to in points (b) and (c) above is 397 days or less; or
(iii) the securitisations referred to in points (a) and (c) above are amortising instruments and have a WAL of two years or less.

A Standard MMF may invest in the securitisations or ABCPs referred to above provided any of the following conditions is met, as applicable:

(i) the legal maturity at issuance or residual maturity of the securitisations and ABCPs referred to in points (a), (b) and (c) above is two years or less and the time remaining until the next interest rate reset date is 397 days or less; or
(ii) the securitisations referred to in points (a) and (c) above are amortising instruments and have a WAL of two years or less.

- Deposits with credit institutions

A deposit is an eligible investment for an MMF provided:-

(a) it is repayable on demand or is able to be withdrawn at any time;
(b) it matures in no more than 12 months; and
(c) it is made with an EU credit institution or a non-EU credit institution subject to prudential rules considered equivalent to those laid down in the CRR.

- Financial derivative instruments ("**FDI**")

  An FDI may be entered into provided:-

  (a) the underlying of the FDI consists of interest rates, foreign exchange rates, currencies or indices representing one of those categories;
  (b) it serves only the purpose of hedging the interest rate or exchange rate risks inherent in other investments of the MMF;
  (c) the counterparties to OTC FDI are institutions subject to prudential regulation and supervision and belonging to the categories approved by the competent authority of the MMF; and
  (d) an OTC FDI is subject to reliable and verifiable valuation on a daily basis and can be sold, liquidated or closed by an offsetting transaction at any time at their fair value at the MMF's initiative.

- Repurchase agreements

  Repurchase agreements (or repo agreements) may be entered into provided:-

  (a) they are used on a temporary basis only (for no more than seven working days) for liquidity management purposes and not for investment purposes other than as detailed in (c) below;
  (b) the counterparty is prohibited from selling, investing, pledging or otherwise transferring those assets without the MMF's prior consent;
  (c) the cash received is only (i) placed on deposit with eligible credit institutions pursuant to the UCITS Directive, or (ii) invested in liquid transferable securities or MMIs (other than eligible MMIs) where they are issued or guaranteed by certain public bodies provided a favourable assessment has been received pursuant to the internal credit quality assessment to be carried out by the manager of the MMF in accordance with the provisions of the MMFR;
  (d) the cash received by the MMF does not exceed 10% of its assets; and
  (e) the MMF has the right to terminate the agreement at any time upon giving prior notice of no more than two working days.

- Reverse repurchase agreements

  A reverse repurchase agreement may be entered into provided:-

  (a) the MMF has the right to terminate the agreement at any time upon giving prior notice of no more than two working days;

(b) the market value of the assets received is at all times at least equal to the value of the cash paid out;
(c) the assets received by an MMF are eligible MMIs except that an MMF may receive liquid transferable securities or MMIs (other than eligible MMIs) where they are issued or guaranteed by certain public bodies provided a favourable assessment has been received pursuant to the internal credit quality assessment to be carried out by the manager of the MMF in accordance with the provisions of the MMFR;
(d) the assets received are not sold, reinvested, pledged or otherwise transferred;
(e) the assets received are issued by an entity that is independent from the counterparty and expected not to display a high correlation with the performance of the counterparty;
(f) the assets received are sufficiently diversified with a maximum exposure to a given issuer of 15%, except where those assets take the form of MMIs issued or guaranteed by certain public bodies;
(g) the aggregate amount of cash provided to the counterparty does not exceed 15% of the MMF's assets: and
(h) the MMF is able to recall the full amount of cash at any time on either an accrued basis or a mark-to-market basis.

- Other MMFs

An MMF may invest in another MMF provided certain conditions are met, such as:-

(a) the other MMF (the "**targeted MMF**") is authorised under the MMFR;
(b) no more than 10% in aggregate of the assets of the targeted MMF may under its fund rules be able to be invested in other MMFs;
(c) the targeted MMF does not hold shares in the acquiring MMF;
(d) the diversification limits set out below in relation to investment in other MMFs are complied with;
(e) where the targeted MMF is managed, whether directly or under delegation, by the same manager as that of the acquiring MMF or by any other company to which the manager of the acquiring MMF is linked by common management or control, or by a substantial direct or indirect holding, the manager of the targeted MMF, or that other company, is prohibited from charging subscription or redemption fees on account of the investment by the acquiring MMF in the targeted MMF;
(f) where an MMF invests 10% or more of its assets in targeted MMFs, (i) the prospectus of the acquiring MMF must disclose the maximum level of the management fees that may be charged to the MMF itself and to the other MMFs in which it invests; and (ii) the annual report must indicate the maximum

proportion of management fees charged to the MMF itself and to the other MMFs in which it invests; and

(g) a Short-Term MMF may only invest in other Short-Term MMFs whereas a Standard MMF may invest in Short-Term MMFs and/or other Standard MMFs.

2.3.2 Diversification & Concentration

The following is a summary of the diversification and concentration requirements applicable to an MMF (and specifically to each type of Short-Term MMF (i.e. Public Debt CNAV MMF, LVNAV MMF and VNAV MMF) and to the Standard VNAV MMF:-

	PUBLIC DEBT CNAV SHORT TERM MMF	LVNAV SHORT TERM MMF	VNAV SHORT TERM MMF	STANDARD VNAV MMF
DIVERSIFICATION REQUIREMENTS[1]				
Money Market Instruments ("MMIs"), Securitisations and ABCP[2]	Max 5% in MMIs, securitisations & ABCPs issued by the same body; Aggregate 15% /20%[3] max in securitisations & ABCPs	Max 5% in MMIs, securitisations & ABCPs issued by the same body; Aggregate 15% /20%[3] max in securitisations & ABCPs	Max 10% in MMIs, securitisations & ABCPs issued by the same body (subject to 5/10/40 rule); Aggregate 15% /20%[3] max in securitisations & ABCPs	Max 10% in MMIs, securitisations & ABCPs issued by the same body (subject to 5/10/40 rule); Aggregate 15% /20%[3] max in securitisations & ABCPs

[1] Group companies for the purposes of consolidated accounts under Directive 2013/34/EU or in accordance with recognised international accounting rules are regarded as a single body for the purpose of these diversification limits.

[2] Subject to an MMF being authorised to invest up to 100% in MMI issued or guaranteed by a single public administration, institution or organisation provided investment is diversified across a minimum of six different issues with a maximum investment of 30% per issue. Note latter most likely to be availed of by Public Debt CNAV MMFs given 99.5% must be invested in (i) MMIs issued / guaranteed by public bodies, (ii) reverse repos secured by government debt and (iii) cash.

[3] Max 15% until date of application of Commission Delegated Act referred to in Art 11(4) of MMFR relating to the proposed Regulation on STS securitisations and 20% thereafter whereby up to 15% may be invested in securitisations and ABCPs that do not comply with the criteria for the identification of STS securitisations and ABCPs.

OTC Derivative Counterparty Exposure	Max 5%	Max 5%	Max 5%	Max 5%
MMIs issued / guaranteed by public bodies	Max 100% per public administration, institution or organisation, diversified across a min 6 issues with max 30% per issue	Max 100% per public administration, institution or organisation, diversified across a min 6 issues with max 30% per issue	Max 100% per public administration, institution or organisation, diversified across a min 6 issues with max 30% per issue	Max 100% per public administration, institution or organisation, diversified across a min 6 issues with max 30% per issue
Deposits	Max 10% in deposits with the same institution	Max 10% in deposits with the same institution	Max 10% in deposits with the same institution	Max 10% in deposits with the same institution
Reverse Repos	Cash provided subject to max 15% per counterparty (Must be fully collateralised)	Cash provided subject to max 15% per counterparty (Must be fully collateralised)	Cash provided subject to max 15% per counterparty (Must be fully collateralised)	Cash provided subject to max 15% per counterparty (Must be fully collateralised)
Repos	Cash received cannot exceed 10%	Cash received cannot exceed 10%	Cash received cannot exceed 10%	Cash received cannot exceed 10%
Other Money Market Funds[4]	Max 5% per MMF; Aggregate max 17.5% (Investment in ST MMFs only)	Max 5% per MMF Aggregate max 17.5% (Investment in ST MMFs only)	Max 5% per MMF Aggregate max 17.5% (Investment in ST MMFs only)	Max 5% per MMF Aggregate max 17.5% (Investment in ST and STD MMFs)
Aggregate Exposure per Counterparty[5]	Max 15% in MMIs, securitisations,	Max 15% in MMIs, securitisations,	Max 15% in MMIs, securitisations,	Max 15% in MMIs, securitisations,

[4] MMFs operating solely as employee savings schemes may diverge from these limits where the participants in such schemes, who are natural persons, are subject to restrictive redemption conditions that are not linked to market developments but instead relate to particular and predefined life events.

	ABCPs issued by, deposits made with and OTC FDI giving exposure to, a single body	ABCPs issued by, deposits made with and OTC FDI giving exposure to, a single body	ABCPs issued by, deposits made with and OTC FDI giving exposure to, a single body	ABCPs issued by, deposits made with and OTC FDI giving exposure to, a single body
CONCENTRATION REQUIREMENTS				
MMIs, Securitisations and ABCPs	Max 10% may be held in such instruments issued by a single body (excluding holdings in MMIs issued / guaranteed by public bodies)	Max 10% may be held in such instruments issued by a single body (excluding holdings in MMIs issued / guaranteed by public bodies)	Max 10% may be held in such instruments issued by a single body (excluding holdings in MMIs issued / guaranteed by public bodies)	Max 10% may be held in such instruments issued by a single body (excluding holdings in MMIs issued / guaranteed by public bodies)

2.3.3 Credit Quality

Under the MMFR, the manager of an MMF must have a prudent internal credit quality assessment procedure for determining the credit quality of the MMIs, securitisations and ABCPs in which the MMF may invest, taking into account the issuer of the instrument and the characteristics of the instrument itself.

In accordance with the EU Credit Rating Agencies Regulation, there can be no over-reliance on external ratings. A new credit quality assessment must be undertaken whenever there is a material change that could have an impact on an existing assessment.

The internal assessment procedure must be based on prudent, systematic and continuous assessment methodologies which must be subject to validation by the manager of the MMF based on historical experience and empirical evidence, including back testing. The credit quality assessment methodologies must be reviewed at least annually by the manager to determine whether they remain appropriate and the review must be transmitted to the competent authority of the manager.

[5] Subject to an MMF being authorised to invest up to 100% in MMI issued or guaranteed by a single public administration, institution or organisation provided investment is diversified across a minimum of six different issues with a maximum investment of 30% per issue.

The credit quality assessment must take into account certain prescriptive factors including inter alia quantitative and qualitative measures on the issuer of the instrument, which will be the subject of Level 2 measures to be adopted by the European Commission in order to ensure greater harmonisation.

Finally the manager of an MMF must ensure that its internal credit quality assessment procedure and credit quality assessments are documented and must retain such documentation for at least three complete annual accounting periods.

2.4 Risk Management Requirements

2.4.1 Portfolio Rules

As stated previously, in order to reduce the portfolio risk of MMFs, the MMFR imposes maturity limitations such as the maximum allowable weighted average maturity (WAM) and weighted average life (WAL).

Furthermore in order to strengthen MMFs' ability to face redemptions and prevent their assets from being liquidated at heavily discounted prices, MMFs must hold on an ongoing basis a minimum amount of liquid assets that mature daily and weekly. Daily maturing assets must comprise assets such as cash which is able to be withdrawn by giving one working day's prior notice, eligible securities that mature within one working day and reverse repurchase agreements which are able to be terminated by giving one working day's prior notice. Weekly maturing assets must comprise similar assets but have greater flexibility in terms of maturity, withdrawal and termination which must be able to be effected within five working days. To calculate the proportion of daily and weekly maturing assets, the legal redemption date of the asset must be used.

The following is a summary of the portfolio rules applicable to an MMF (and specifically to each type of Short-Term MMF (i.e. Public Debt CNAV MMF, LVNAV MMF and VNAV MMF) and to the Standard VNAV MMF:-

	PUBLIC DEBT CNAV SHORT TERM MMF	LVNAV SHORT TERM MMF	VNAV SHORT TERM MMF	STANDARD VNAV MMF
PORTFOLIO RULES				
WAM (max)	60 days	60 days	60 days	6 months
WAL (max)[6]	120 days	120 days	120 days	12 months
Maturity (max)	397 days	397 days	397 days	2 years provided next interest rate reset date is 397 days or less
Daily liquid assets (min)	10%	10%	7.5%	7.5%
Weekly liquid assets (min)	30%[7]	30%[7]	15%[8]	15%[8]

2.4.2 MMF Credit Rating

An MMF that solicits or finances an external credit rating must do so in accordance with the EU Credit Rating Agencies Regulation.

2.4.3 Know Your Customer

In order to ensure appropriate liquidity management, the manager of an MMF must establish sound policies and procedures to get to know the investors of the MMF and in particular with

[6] When calculating the WAL for securities, including structured financial instruments, an MMF must base the maturity calculation on the residual maturity until the legal redemption of the instruments. However, in the event that a financial instrument embeds a put option, an MMF may base the maturity calculation on the exercise date of the put option instead of the residual maturity, but only if certain conditions are met. When calculating the WAL for securitisations and ABCPs, an MMF may instead, in the case of amortising instruments, base the maturity calculation on (i) the contractual amortisation profile of such instruments; or (ii) the amortisation profile of the underlying assets from which the cash-flows for the redemption of such instruments result.

[7] MMIs issued / guaranteed by public bodies which are highly liquid and can be redeemed and settled within one working day and have a residual maturity of up to 190 days may also be included within the weekly maturing assets up to a limit of 17.5 %.

[8] MMIs or other MMFs may be included within the weekly maturing assets up to a limit of 7.5 % provided they are able to be redeemed and settled within five working days.

a view to anticipating the effect of concurrent redemptions by several investors, taking into account at least the type of investor, the number of shares in the MMF owned by a single investor and the evolution of inflows and outflows.

So that an MMF does not face sudden massive redemptions, particular attention must be paid to large investors representing a substantial portion of the MMF's assets, such as with one investor representing more than the proportion of daily maturing assets. The manager of an MMF must whenever possible look at the identity of the MMF's investors, even if they are represented by nominee accounts, portals or any other indirect buyer.

2.4.4 Stress Testing

As part of prudent risk management, MMFs must, at least bi-annually, conduct stress testing that identify possible events or future changes in economic conditions which could have unfavourable effects on the MMF. The MMF or the manager of an MMF must assess the possible impact that those events or changes could have on the MMF and is expected to act in order to strengthen the MMF's robustness whenever the results of stress testing point to vulnerabilities. For Public Debt CNAV MMFs and LCNAV MMFs, the stress tests must also estimate, for different scenarios, the difference between the constant net asset value per share and the net asset value per share.

An extensive report with the results of the stress testing and proposed action plan must be submitted for examination to the board of directors of the MMF, where applicable, or the board of directors of the manager of an MMF. The board of directors must amend the proposed action plan if necessary and approve the final action plan. The extensive report and the action plan must be kept for a period of at least five years. The extensive report and the action plan must be submitted for review to the competent authority of the MMF who in turn must send the extensive report to the European Securities and Markets Authority ("**ESMA**").

2.5 Valuation & Dealing Requirements

The assets of an MMF must be valued on at least a daily basis by using mark to market whenever possible. However where an asset is inherently difficult to value based on market prices (e.g. certain OTC derivatives), the manager of an MMF may assign a fair value to the asset by using mark-to-model.

Notwithstanding the above, Public Debt CNAV MMFs and LVNAV MMFs may use the internationally recognised amortised cost method as set out under international accounting standards adopted by the European Union for the valuation of certain assets. However, for the purpose of ensuring that the difference between the constant net asset value per share and the net asset value per share is monitored at all times, Public Debt CNAV MMFs and LVNAV MMFs must also calculate the value of their assets on the basis of mark-to-market or mark-to-model.

	PUBLIC DEBT CNAV SHORT TERM MMF	LVNAV SHORT TERM MMF	VNAV SHORT TERM MMF	STANDARD VNAV MMF
VALUATION & DEALING				
Valuation Methodology	Amortised cost	Amortised cost for instruments with residual maturity $\leq$ 75 days[9]; Mark-to-market/ Mark-to-model for instruments >75 days	Mark-to-market / Mark-to-model	Mark-to-market / Mark-to-model
Dealing NAV per Share	CNAV per share rounded to nearest percentage point (e.g. nearest cent for CNAV per share of €1)	CNAV per share rounded to nearest percentage point (e.g. nearest cent for CNAV per share of €1), provided CNAV per share does not deviate from NAV per share by >20 basis points	NAV per share rounded to nearest basis point or equivalent in a currency unit (e.g. every €0.0001 in the case of NAV per share of €1 and every €0.01 in the case of NAV per share of €100)	NAV per share rounded to nearest basis point or equivalent in a currency unit (e.g. every €0.0001 in the case of NAV per share of €1 and every €0.01 in the case of NAV per share of €100)

[9] Provided the mark-to-market / mark-to-model value of the instrument does not deviate from the amortised cost value of the instrument by >10 basis points as in such circumstance the mark-to-market / mark-to-model value of the instrument must be used.

2.6 Specific Requirements for Public Debt CNAV and LVNAV MMFs

In order to be able to mitigate potential investor redemptions in times of severe market stress, Public Debt CNAV MMFs and LVNAV MMFs must have in place provisions for liquidity fees and redemption gates to ensure investor protection and prevent a 'first mover advantage. The liquidity fee must adequately reflect the cost to the MMF of achieving liquidity and must not amount to a penalty charge that would offset losses incurred by other investors as a result of the redemption.

In particular whenever the proportion of weekly maturing assets of a Public Debt CNAV MMF or LVNAV MMF falls bellows 30% and net daily redemptions on a single business day exceed 10%, such measures in addition to the suspension of redemptions must be available to the board of the MMF. Similarly whenever the proportion of weekly maturing assets of a Public Debt CNAV MMF or LVNAV MMF falls bellows 10%, measures such as the provision of liquidity fees and the suspension of redemptions must be available to the board of the MMF.

2.7 External Support

External support provided to an MMF with a view to maintaining either liquidity or stability is prohibited under the MMFR.

2.8 Transparency / Reporting Requirements

2.8.1 Transparency

The manager of an MMF must, at least weekly, make all of the following information available to the investors of the MMF:-

- the maturity breakdown of the portfolio of the MMF;
- the credit profile of the MMF;
- the WAM and WAL of the MMF;
- details of the 10 largest holdings in the MMF;
- the total value of the assets of the MMF; and
- the net yield of the MMF.

2.8.2 Reporting

In addition to reporting already required under the UCITS Directive and the AIFM Directive, the manager of an MMF must report to the competent authority of the MMF on at least a quarterly basis (or at least annually where the AUM of the MMF does not exceed €100 million) a detailed list of information on the MMF, including the type and characteristics of the MMF, portfolio indicators, results of stress tests and information on the assets and liabilities held in the portfolio. Competent authorities must collect and transmit that data to ESMA which is tasked with creating a central database of MMFs.

The manager of a LVNAV MMF must also report the following additional information:-

- every event in which the price of an asset valued by using the amortised cost method deviates from the price of that asset calculated in accordance with the mark-to-market / mark-to-model by more than 10 basis points;
- every event in which the constant net asset value per share deviates from the net asset value per share by more than 20 basis points; and
- every event in which (i) the proportion of weekly maturing assets falls bellows 30% and net daily redemptions on a single business day exceed 10%; or (ii) the proportion of weekly maturing assets falls bellows 10%, and the measures taken by the board of the MMF.

3. FURTHER STEPS IN THE IMPLEMENTATION OF THE MMFR

3.1 Level 2 & Level 3 Measures

The MMFR entered into force on 20 July 2017 and will become effective from 21 July 2018.

In the interim however, the European Commission is obliged pursuant to the MMFR to adopt the following Level 2 measures:-

- implementing technical standards ("**ITS**") to establish a reporting template containing all necessary information required to be reported by the manager of an MMF to the competent authority of the MMF; and
- delegated acts specifying:-
  - (a) liquidity and credit quality requirements applicable to assets received as part of a reverse repurchase agreement;
  - (b) the criteria for the validation of the credit quality assessment methodologies, in relation to which the internal credit quality assessment procedures of an MMF's manager must be based;

(c) the meaning of "material change" that could have an impact on an existing credit quality assessment of an MMI, securitisation or ABCP and that would trigger a new credit quality assessment for that instrument;

(d) the criteria for quantification of the credit risk and the relative risk of default of an issuer and of the instrument in which the MMF invests, which factors must be taken into account by the manager of an MMF when carrying out a credit quality assessment of that instrument; and

(e) the criteria to establish qualitative indicators on the issuer of the instrument, which indicators must also be taken into account by the manager of an MMF when carrying out a credit quality assessment of an instrument.

In addition pursuant to the MMFR, ESMA is obliged to issue Level 3 guidelines with a view to establishing common reference parameters of the stress test scenarios to be included in the stress tests which managers of MMFs are required to conduct.

In order to provide technical advice to the Commission in relation to the above required delegated acts, to develop draft ITS to be adopted by the Commission and to develop the above referenced Level 3 guidelines, ESMA issued a consultation paper on 24 May 2017 seeking the views of external stakeholders.

Given the deadline for responses to the consultation paper is 7 August 2017 and given the MMFR is not prescriptive on the timeframe for the adoption of the above referenced Level 2 measures (except the delegated act referred to in (a) above which must be adopted by 21 January 2018, subject to no objection being expressed by the European Parliament and the Council), it is anticipated that the ITS and remaining delegated acts will be adopted by the Commission in the first half of 2018 in advance of the effective date of the MMFR, being 21 July 2018.

3.2 Further Review of the MMFR

The European Commission must review by 21 July 2022 the adequacy of the MMFR from a prudential and economic point of view including whether changes are to be made to the regime for Public Debt CNAV MMFs and LVNAV MMFs. Such review must take into account certain prescribed criteria as detailed in the MMFR following consultations with ESMA and, where appropriate, the European Systemic Risk Board.

The European Commission must also present a report by 21 July 2022 on the feasibility of establishing an 80% EU public debt quota. That report must have regard to the availability of short-term EU public debt instruments and assess whether LVNAV MMFs might be an appropriate alternative to non-EU Public Debt CNAV MMFs.

4. IMPLICATIONS FOR EXISTING MMFS

By 21 January 2019, an existing UCITS or AIF regulated by the Central Bank of Ireland (the "**Central Bank**") that invests in short-term assets and has as a distinct or cumulative objective the offering of returns in line with money market rates or preserving the value of the investment must submit an application to the Central Bank together with all documents and evidence necessary to demonstrate compliance with the MMFR.

Within two months of receiving a complete application, the Central Bank must assess whether the UCITS or AIF is compliant with the MMFR and issue a decision.

In order to ensure compliance with the MMFR, it will be necessary for an existing MMF to, inter alia:-

- determine, where necessary, what type of MMF under the MMFR it will re-categorise itself as e.g. if currently a CNAV MMF, will it categorise itself as a Public Debt CNAV MMF or a LVNAV MMF and consequently will it restructure the existing MMF or strive to transfer assets / investors to a new MMF under the MMFR;
- ensure required policies and procedures are in place;
- amend its constitutional document e.g. to provide for the MMFR valuation and dealing requirements, the specific requirements for Public Debt CNAV MMFs and LVNAV MMFs (where applicable), the MMF's internal credit quality assessment procedures and liquidity management procedures, etc.;
- amend its prospectus e.g. to reflect where necessary the chosen type of MMF under the MMFR, changes in objective/ policies, portfolio rules, liquidity management procedures to ensure compliance with the portfolio liquidity thresholds, diversification and concentration limits, investment and borrowing restrictions, etc.;
- amend documentation used for marketing purposes (including KIIDs); and
- ensure communication with investors includes certain prescribed disclosures.

5. HOW DILLON EUSTACE CAN ASSIST

Dillon Eustace has one of the largest financial services legal practices in Ireland serving clients across a whole range of activities, including Asset Management and Investment

Funds, Investment Services, Insurance and Pensions, Debt and Funds Listing, Regulatory and Compliance and Regulatory Investigations.

Dillon Eustace represents the largest number of Irish domiciled funds (Monterey Insight – Ireland Fund Survey 2016) reflecting the fact that the Asset Management and Investment Funds practice has been, and remains, one of the firm's core activities with partners having been to the forefront of the Irish funds industry from its beginning.

Dillon Eustace has significant experience in establishing and obtaining authorisation of MMFs, both CNAV and VNAV MMFs, and having advised such MMFs pre and post the credit crisis of 2007 – 2008 has significant experience on the issues faced by MMFs not just in market stress scenarios but also in low / negative interest rate periods.

Consequently Dillon Eustace is ideally placed to assist managers / promoters seeking:-

- to establish and obtain authorisation of a new UCITS or AIF MMF (and in the latter case as either a retail or qualifying investor MMF); or

- authorisation of an existing UCITS or AIF MMF under the MMFR.

In this regard, Dillon Eustace can advise on the structural and other decisions referred to above under “Implications for Existing MMFs” which the MMF and its manager will need to make and draft applicable documentation accordingly.

In addition, as an authorised AIFM is required as part of the authorisation process of an AIF MMF established, managed or marketed in the EU, Dillon Eustace can assist in the establishment and authorisation of an Irish AIFM if required.

For more details on how we can help you, to request copies of our most recent newsletters, briefings or articles, or simply to be included on our mailing list going forward, please contact us.

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