Opinion on the review of the CESR guidelines on a common definition of European Money Market Funds. November 2014.

ESMA has published, on the 22nd August, a review of the CESR (ESMA´s predecessor) on a common definition of European Money Market Funds. ESMA´s competence to deliver opinions to competent authorities is based on article 29.1.a) of the Regulation nº 1095/2010 (the ESMA Regulation).

CESR adopted, in May 2010, the Guidelines on a common definition of European Money Market Funds with the purpose that a harmonised definition of "Money Market Fund" would improve investor protection. The Guidelines set out a two-tiered approach for a definition of European Money Market Funds: 1) Short Term Money Market Funds (STMMFs), which operate a very short weighted average maturity and weighted average life, and 2) Money Market Funds (MMFs), which operate with a longer weighted average maturity and weighted average life. CESR Guidelines set out criteria that money market instruments should respect in order to be considered as eligible investments for both types of money market funds: a money market instrument should not be considered to be of high quality by STMMFs and MMFs managers unless it has been awarded one of the two highest available short-term credit ratings by each Credit Rating Agency (hereinafter CRA) that has rated the instrument.

Otherwise, article 5b of Regulation nº 462/2013 amending Regulation 1060/2009 on Credit Rating Agencies (CRAIII Regulation) established that ESMA, EBA (European Banking Authority) and EIOPA (European Insurance and Occupational Pensions authority) shall not refer to credit ratings in their guidelines, recommendations and draft technical standards where such references have the potential to trigger sole or mechanistic reliance on credit ratings by the competent authorities, the sectoral competent authorities, financial institutions and other financial market participants. Also the CRA III Regulation entrusted ESMA, EBA and EIOPA to review and remove, where appropriate, all such references to credit ratings in their existing guidelines and recommendations.

ESMA, EBA and EIOPA published, on the 6th February 2014, a joint final report on mechanistic references to credit ratings in their guidelines and recommendations according to which **the management company should undertake a new assessment of the credit quality of the instrument to ensure it continues to be of high quality when the creditworthiness rating of a money market instrument downgrades below the two highest short-term credit ratings in the case of STMMF or below the investment grade in the case of sovereign issuance for MMF**.

ESMA opinion sets out the manner in which the that CESR Guidelines were to be amended according to the proposal of the joint final report of ESMA, EBA and EIOPA, and that competent national authorities should take into account the amendments when they monitor the application of the CESR guidelines.

ESMA will not reissue the CESR guidelines under article 16 of the ESMA Regulation, which means that national competent authorities will not have to notify ESMA whether or not they comply or intend to comply with the amended version of the CESR guidelines. However, ESMA will monitor the implementation of this opinion by the competent national authorities.

ESMA believes, in section 7 of the opinion, that paragraph 4 of the Box 2 –related to STMMFs- of the original CESR guidelines should be replaced by the following paragraph:

"4. For the purposes of point 3a), ensure that the management company performs its own documented assessment of the credit quality of money market instruments that allows it to consider a money market instrument as high quality. Where one or more credit rating agencies registered and supervised by ESMA have provided a rating of the instrument, the management company's internal assessment should have regard to, inter alia, those credit ratings. While there should be no mechanistic reliance on such external ratings, a downgrade below the two highest short-term credit ratings by any agency registered and supervised by ESMA that has rated the instrument

should lead the manager to undertake a new assessment of the credit quality of the money market instrument to ensure it continues to be of high quality."

ESMA believes, in section 8 of the opinion, that paragraph 3 of the Box 3 –related to MMFs- of the original CESR guidelines should be replaced by the following paragraph:

"2. May, as an exception to the requirement of point 4 of Box 2, hold sovereign issuance of a lower internally-assigned credit quality based on the MMF *manager's own documented assessment of credit quality. Where one or more credit rating agencies registered and supervised by ESMA have provided a rating of the instrument, the management company's internal assessment should have regard to, inter alia, those credit ratings. While there should not be mechanistic reliance on such external ratings, a downgrade below investment grade or any other equivalent rating grade by any agency registered and supervised by ESMA that has rated the instrument should lead the manager to undertake a new assessment of the credit quality of the money market instrument to ensure it continues to be of appropriate quality. 'Sovereign issuance' should be understood as money market instruments issued or guaranteed by a central, regional or local authority or central bank of a Member State, the European Central Bank, the European Union or the European Investment Bank*."

Furthermore, to ensure consistency with the new version of paragraph 4 of Box 2 of the CESR guide-lines, national competent authorities should not take into account the last sentence of paragraph 10 of the explanatory text under Box 2 and paragraph 25 of the explanatory text under Box 3 of the original CESR guidelines.

For ease of reference, an informal consolidated version of the CESR guidelines that reflects the modifications of the provisions on the assessment of the credit quality of money market instruments is annexed to the opinion.

If you want to read the ESMA opinion on the review of the CESR Guidelines on a common definition of European money market funds, please click on: http://www.esma.europa.eu/system/files__/2014-esma-1103_esma_opinion_on_cesr_guidelines_on_mmfs.pdf

If you want to read ESMA, EBA and EIOPA final report on mechanistic references to credit ratings in the ESA´s guidelines and recommendations, please click: http://www.esma.europa.eu/system/files/jc_2014_004_final_report_mechanistic_references_to_credit_ratings_rect.pdf

If you want to read CESR´s Guidelines on a common definition of European money market funds, please click here: http://www.esma.europa.eu/system/files/10-049_cesr_guidelines_mmfs_with_disclaimer.pdf