

Table of risks covered by measures implemented by UCITS regulations & European Money Market Funds

Shadow banking issues	UCITS (including ETFs) & Money Market Funds ¹ regulations coverage	with the following measures					
Specific risks identified for Money Market Funds (MMF)	In addition to general UCITS provisions described below Money Market Funds (MMF) are also subject to the following provisions which reduce specific risks identified:						
UCITS MMF - Liquidity/credit risk (addressed) - Valuation: (risks of discrepancy with amortisation cost basis/stable NAV funds) (addressed) - Risk Management Process (RMP)	<ul style="list-style-type: none"> • Art. 1(o) & Art. 50 of Dir. 2009/65/EC² • Art. 3, Art. 4 & Art. 5 of Dir. 2007/16/EC³ • CESR/07-⁰⁴⁴ b4, items 18 & 19 • CESR/10-049⁵ item 20 	<ul style="list-style-type: none"> • restriction on eligible money market instruments (MMI) (e.g. maturity 397 days) & assessment of liquidity of MMI (at the instrument & fund levels). This ensures that MMF <i>have sufficient planning in the structuring of the portfolio and in foreseeing cash flows [...]</i> (CESR/07-434). • value must be accurately determined at any time & <i>if UCITS consider that an amortisation method can be used [...they] must ensure that this will not result in a material discrepancy</i> at MMI or UCITS level • RMP should include for MMF a prudent approach to the management of currency, credit, interest & liquidity risk & a proactive stress-testing regime. 					
UCITS & non UCITS MMF⁶ (liquidity risk, credit risk : addressed)	CESR/ 10-049	NAV	<table border="1"> <thead> <tr> <th>Short-term MMF</th> <th>MMF</th> </tr> </thead> <tbody> <tr> <td>Floating NAV or stable NAV (only if strict requirements apply to credit quality, sensitivity to market parameters, diversification & maturity of these holdings, and portfolio be marked to market on a regular basis according to the law of the jurisdiction in which the MMF is</td> <td>Floating NAV only</td> </tr> </tbody> </table>	Short-term MMF	MMF	Floating NAV or stable NAV (only if strict requirements apply to credit quality, sensitivity to market parameters, diversification & maturity of these holdings, and portfolio be marked to market on a regular basis according to the law of the jurisdiction in which the MMF is	Floating NAV only
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¹ The managers of non-UCITS ETFs and non-UCITS MMF in addition, fall under AIFMD coverage

² Directive of 13 July 2009 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS)

³ Directive of 19 March 2007 "Eligible Assets Directive"

⁴ CESR Guidelines concerning eligible assets for investment by UCITS – March 2007

⁵ CESR Guidelines on a common definition of European money market funds – 19 May 2010 and Q&A ESMA/2011/273

⁶ Scope of CESR Guidelines relating to a common definition on money market funds (box 1 of the Guidelines):

a) The regime is applicable to both UCITS and non UCITS :

b) Any fund labelling or marketing itself (it goes beyond the mere naming convention or labelling of a fund) as a money market fund must be compliant with the Guidelines.

		authorised or supervised (items 21 and 22))	
		Required security maturity	Max. 397 days Max. two years if interest rate reset date is less than 397 days
		WAM	Max. 60 days Max. 6 months
		WAL	Max. 120 days Max. 12 months
		Credit ratings	one of the two highest short-term credit ratings or equivalent one of the two highest short-term credit ratings or equivalent (exception for sovereign issue).
General risks identified for funds (incl. ETFs & MMFs) & use of securities lending & repos			
Risk of run off (addressed)	Art. 84 (2) a) & b) of Dir 2009/65/EC	NAV temporary suspension at UCITS' or supervisory authority initiative (if in the best interest of unitholder or required by public interest)	
Liquidity risk (limited & adequately monitored)	<ul style="list-style-type: none"> • Art. 84 & Art. 51 <i>et seq.</i> of Dir. 2009/65/EC • Recital 5 of Dir. 2009/65/EC • Dir. 2007/16/EC • CESR/07-434 • Dir. 2010/43/EU⁷ (section 2/Art. 40.3) • Art. 1.2 of Dir. 2009/65/EC 	<ul style="list-style-type: none"> • UCITS must redeem their units at shareholders' request & are subject to strict diversification rules • invest only in liquid assets. • adequate management of liquidity risk • appropriateness of liquidity profile with redemption policy • stress tests enabling assessment of liquidity risk under exceptional circumstances • ETFs: liquidity for investors ensured through secondary market makers & authorised participants. Are assimilated to redemptions, actions taken by a UCITS to ensure that stock value does not significantly vary from UCITS' NAV 	
Transfer of credit risks (addressed)	• Art. 50 <i>et seq.</i> of Dir. 2009/65/EC	• UCITS have to comply with credit & counterparty risks limits, especially with the overall 20% limit & 5/10% limit for OTC derivatives like "TRS"	

⁷ Commission Directive 2010/43/EU of 1 July 2010 implementing Directive 2009/65/EC of the European Parliament and of the Council as regards organisational requirements, conflicts of interest, conduct of business, risk management and content of the agreement between a depositary and a management company

	<ul style="list-style-type: none"> • Art. 43 of Dir. 2010/43/EU • CESR/10-788⁸ (box 26/27) 	<ul style="list-style-type: none"> • adequate monitoring of counterparty risk in OTC derivatives & use of collateral allowed to reduce counterparty risk which must meet strict criteria regarding liquidity, diversification, reinvestment (see third bullet point in securities lending & repurchase agreement section below) • The counterparty risk net exposure in securities lending & repos, has to be aggregated within the 20% limit above. • cf securities lending & repos section below
<p>Financial leverage risk (limited risk & adequate monitoring)</p>	<ul style="list-style-type: none"> • Art. 83 of Dir. 2009/65/EC • Art. 51.3 of Dir. 2009/65/EC • CESR/10-788 (Boxes 24 & 25) 	<ul style="list-style-type: none"> • UCITS cannot use borrowing other than on a temporary basis & up to a maximum of 10% of their NAV. • UCITS shall employ a RMP & must ensure that their global exposure resulting from the use of derivatives (& securities lending & repos) may not exceed their NAV • UCITS using VaR to calculate their global exposure must disclose in their prospectus, the expected level of leverage & in their annual reports, the actual level of leverage
<p>Securities lending & repurchase transactions (“repos”) & related risks of such activities (strict limitation of their use & additional forthcoming regulations regulating strictly collateral)</p>	<ul style="list-style-type: none"> • Art. 51.2 of Dir. 2009/65/EC • Art. 41.4 Dir. 2010/43/EU • CESR/10-788 • ESMA Consultation ESMA/2012/44⁹ (Box 6 item 6) 	<ul style="list-style-type: none"> • UCITS may only use these techniques for efficient portfolio management (EPM) • these techniques must be taken into account in calculation of global exposure when they increase leverage or exposure to market risk • ESMA suggests applying (to all UCITS) the same rules to collateral received within the context of securities lending & repos as those currently applicable to collateral received within the context of OTC derivatives. Those rules are essentially related to liquidity, valuation, issuer credit quality, non-correlation between the counterparty & the collateral received, diversification, operational & legal risks, holding of collateral by a 3rd party custodian which is subject to prudential supervision, prohibition to sell, re-use or pledge the collateral received & only authorise reinvestment of cash collateral in risk free assets. = limits any systemic risk that may be implied (i) by the use/re-use of the same securities in several transactions (ii) leverage effect generated by reinvestment of cash collateral in non-risk free assets

⁸ CESR Guidelines on Risk Measurement and the Calculation of Global Exposure and Counterparty Risk for UCITS – 28 July 2010

⁹ Consultation paper ESMA Guidelines on ETFs and other UCITS issues



association of the
luxembourg fund industry

Systemic risk contribution (efficient supervision & monitoring)	Art. 51 <i>et seq.</i> of Dir. 2009/65/EC	<ul style="list-style-type: none">• UCITS or management companies shall notify on an ongoing basis to supervisory authority for each UCITS the type of derivatives used, underlying risks, quantitative limits & methodologies used to manage the risk• restrictions on use of borrowings, on use of derivatives, on global exposure & disclosure of leverage (see above)
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