

FSC Guidance Note No. 35

Money Market Funds
Naming Convention
September 2017

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Commencement: This Guidance Note commences from 1 January 2018, with a 6 month transition period.

Application of this Guidance Note: FSC Members who are Issuers of Managed Investment Schemes ('Money Market Funds') issued to investors via a Product Disclosure Statement.

Main Purpose of this Guidance Note: This Guidance details the following matters:

- a) the formats Managers may choose to adopt when reporting to investors on dividend imputation credits derived from investments in Australian shares;
- b) the formula for calculating the franking level of distributed Income;
- c) the basis for quoting Franking Credits.

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1 Title

This Guidance Note may be cited as FSC Guidance Note No. 35 *Money Market Funds Naming Convention*.

2 Date of Issue

This Guidance Note is dated as at September 2017.

3 Definitions and interpretation

Unless otherwise stated, defined terms have the meanings given to them in the Corporations Act 2001 (Cth).

ASIC Australian Securities & Investments Commission

IOSCO International Organization of Securities Commissions

Money Market Fund (MMF) is defined by ASIC as an unlisted managed investment scheme, with investment objectives of capital preservation and yield generation that primarily invests in a diversified portfolio of high-quality, low-duration money market instruments. Related terms for this purpose include 'cash', 'liquid', 'ready assets' and similar terms.

Collective Investment Scheme (or Managed Investment Scheme) is a type of investment scheme that involves collecting money from different investors and then combining all the money collected to fund investments. Terminology varies with country but collective investment vehicles are often referred to as 'mutual funds', 'investment funds', 'managed funds' or 'managed investment schemes' in Australia.

Major Australian Banks includes the Commonwealth Bank of Australia (CBA), National Australia Bank (NAB), Westpac and Australia and New Zealand Bank (ANZ) only.

Daily Liquid Assets is defined as cash, securities and securities convertible into cash in one business day.

Weekly Liquid Assets is defined as Daily Liquid Assets plus agency notes with remaining maturities of 60 days or less, and securities convertible into cash whether by maturity, sale or through exercise of a demand feature, within five business days.

NAV refers to Net Asset Value.

Variable NAV A fund has a variable NAV structure when it quotes a variable dollar price for application and redemption purposes.

Product Disclosure Statement is a document that must be given to a retail client in relation to the offer or issue of a financial product in accordance with Div. 2 of Pt 7.9 of the Corporations Act

Weighted Average Life (WAL) A measure of asset liquidity and maturity. It calculates the average amount of time for which each dollar of principal on a loan remains outstanding.

Weighted Average Maturity (WAM) A measure of asset liquidity and maturity. It calculates the average amount of time until all the assets in a portfolio mature. This is calculated by reference to the maturity date for non-floating rate note (FRN) securities. For FRN securities, it is calculated by reference to the next FRN reset date.

4 Statement of Purpose

4.1 The purpose of this Guidance Note is to assist the following organisations with guidance as to naming conventions of retail offer money market funds:

- issuers of money market funds (the **Issuer**); and

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- other relevant industry participants, including superannuation RSEs.

- 4.2 Users must take their own advice and consider their own circumstances. Users of this Guidance Note should not rely solely on this Guidance Note without also assessing the particular factual circumstances applicable to their situation, and also obtaining appropriate advice specific to their circumstances. This document does not constitute any form of advice (including taxation, legal, actuarial, pricing methodology, accounting or other advice) and should not be relied upon as such. Users of this document should take their own advice on legal, taxation, accounting, actuarial, regulatory, and any other relevant matters as appropriate in relation to fees and costs disclosure.
- 4.3 This Guidance Note sets out industry best practice based on feedback from the Australian Securities & Investments Commission (**ASIC**)¹ and principles governing money market funds that were produced by the International Organization of Securities Commissions (**IOSCO**)².

5 Application

This Guidance Note applies to FSC Members who issue 'Money Market' Managed investment schemes offered to retail investors via a Product Disclosure Statement (PDS).

The Guidance Note applies to funds offered to retail clients through a platform or wrap, but is not applicable to funds offered solely to wholesale or institutional clients.

The Guidance Note rules relate specifically to **fund names**.

6 Naming Convention Rules

- 6.1 This Guidance Note sets out criteria for two types of Money Market Funds (**MMFs**):
1. Short term money market fund - hold high quality short term money market instruments that are highly liquid; and
 2. Standard money market fund – hold quality money market instruments that are highly liquid but has a longer portfolio maturity than a short term money market fund. The rules and features of these funds are outlined in Section 8.
- 6.2 Funds that meet either of these criteria are permitted to use the words 'money market', 'cash', 'liquid', 'ready assets' or similar terms in their name. Funds that do not meet either of these criteria should **not** use the words 'money market', 'cash', 'liquid', 'ready assets' or similar terms in their name.
- 6.3 In addition, where a fund meets the criteria for a short term fund, the Issuer may use the phrase 'short term' in fund's name. This will signal to consumers that the fund adheres to the rules and features of this type of money market fund.
- 6.4 Where a fund does not meet the criteria for a short term money market fund but does meet the criteria for a standard money market fund, the fund is permitted to use the term 'standard' in the fund name. The fund however is **not** permitted to use the phrase 'short term' in its name.
- 6.4 The PDS of the fund should make it clear which criteria the fund meets and this Guidance Note may be referred to in the PDS for this purpose.

7 Background

- 7.1 MMFs garnered attention from regulators globally following the run on MMFs during the global financial crisis. Internationally, they have tended to be highly regulated and have very narrow definitions and naming conventions. Australia's MMF industry is very small by global standards and plays a minor role in providing liquidity to the market.
- 7.2 In 2012, IOSCO produced a report on money market funds globally and provided policy

¹ <http://asic.gov.au/regulatory-resources/find-a-document/reports/rep-324-money-market-funds/>

² <http://www.iosco.org/library/pubdocs/pdf/IOSCOPD392.pdf>

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recommendations for all member countries to adhere to, in order to move to consistent market features and regulation. ASIC believes Australia's market practice and regulation is substantially aligned with IOSCO recommendations.

- 7.3 ASIC subsequently produced a report in 2012 (ASIC REP 324) which examined money market funds and their risks to determine whether regulatory intervention is appropriate in Australia. The report concluded that Australia's funds do not share many of the characteristics that are prevalent in overseas money market funds and recommended that regulatory intervention was not required at this time but that ASIC would encourage industry to adopt more standardise product branding to better distinguish 'enhanced' money market funds from the other money market funds.

8 Guidance

MONEY MARKET FUND (MMF) FEATURE	'SHORT TERM' MMF FEATURES	'STANDARD' (FSC) MMF FEATURES
Structure	Managed Investment Scheme offered to retail investors via a Product Disclosure Statement.	Managed Investment Scheme offered to retail investors via a Product Disclosure Statement.
Investment objectives	Funds that seek to preserve capital and provide daily liquidity, while offering returns consistent with money market rates.	Investment objectives of capital preservation, liquidity and yield generation.
Investment assets	Specific limitations should apply to the types of assets in which MMFs may invest and the risks they may take: <ul style="list-style-type: none"> i. Should hold high quality money market instruments and other low- duration money market instruments. 	Specific limitations should apply to the types of assets in which MMFs may invest and the risks they may take: <ul style="list-style-type: none"> i. Should achieve these objectives by investing in a portfolio of high - quality, predominantly low-duration money market instruments.
	ii. Prohibit MMF from taking a direct or indirect exposure to equities or commodities.	ii. Prohibit MMF from taking a direct or indirect exposure to equities or commodities.
	iii. The use of derivatives should be in line with the investment strategy of the fund.	iii. The use of derivatives should be in line with the investment strategy of the fund.
	iv. MMF should prohibit or impose limits on investments in securitised products. Floating Rate Notes, including Asset Backed Floating Rate Notes permitted, up to maximum exposure of 10%.	iv. MMF should prohibit or impose limits on investments in securitised products. Floating Rate Notes with a WAM over 397 days, including Asset Backed Floating Rate Notes permitted, up to maximum exposure of 30%.
	v. MMF should prohibit or impose limits on investments in derivatives. Only exchange traded Inter-Bank and Bank Bill futures (and options on each) are allowed. The gross exposure of all futures and delta adjusted options must be fully cash backed.	v. MMF should prohibit or impose limits on investments in derivatives. Only exchange-traded Australian Bank Bill, Interbank Cash Rate, and 3-year futures contracts (and options on these contracts), as well as AUD interest rate swaps/swaptions with a tenor of 3 years or less, are permitted.

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		The gross exposure of all futures and delta adjusted options must be fully cash backed.
	vi. Short term MMFs must hold direct assets in Australian-dollar denomination.	vi. Standard MMF may invest in non-AUD based currency securities up to a limit of 15% provided the currency exposure is fully hedged.
	vii. MMFs must impose concentration limits and/or diversification ratios to reduce the MMF's exposure to a single entity: <ul style="list-style-type: none"> – Exposure to money market instruments issued by Major Australian Banks be capped at 35% of the MMFs portfolio per entity; AND – Exposure to non-major, non- government money market instruments issued by all other issuers be capped at 15% of the MMFs portfolio. 	vii. MMFs must impose concentration limits and/or diversification ratios to reduce the MMF's exposure to a single entity: <ul style="list-style-type: none"> – Exposure to money market instruments issued by Major Australian Banks be capped at 35% of the MMFs portfolio per entity; AND – Exposure to non-major, non- government money market instruments issued by all other issuers be capped at 15% of the MMFs portfolio.
	viii. Term to Maturity of underlying instrument within portfolio: For short term MMFs, limit investment in securities to those with a residual maturity until the legal redemption date of less than or equal to 397 days.	viii. Term to Maturity of underlying instrument within portfolio: Each instrument within portfolio to have a maximum Term to Maturity of 3 years, except Asset Backed Floating Rate Notes which must have a maximum Weighted Average Life of 3 years at time of purchase.
	ix. Portfolio to have a Weighted Average Maturity of no more than 60 days.	ix. For the standard MMF, Portfolio to have a Weighted Average Maturity of 180 days or less.
	x. Portfolio to have a Weighted Average Life of no more than 120 days.	x. Portfolio to have a Weighted Average Life of 365 days or less.
	xi. Invest a minimum 50% amount of the Scheme in A-1+ rated or Major Bank assets with a maximum maturity of 12 months.	xi. Invest a minimum 25% amount of the Scheme in A-1+ rated or Major Bank assets with a maximum maturity of 12 months.
Leverage limits	Leverage within the Fund is only permitted for short term borrowing to manage redemption requests and limited to 10% of funds under management.	Leverage within the Fund is only permitted for short term borrowing to manage redemption requests and limited to 10% of funds under management.
Reference in product documentation and terminology	Only MMFs that meet the criteria in this table may use the terms "cash," "liquid," "money," "ready assets" or similar terms in their name. Short term MMFs may brand themselves as 'short term' – for	Only MMFs that meet the criteria in this table may use the terms "cash", "liquid", "money", "ready assets" or similar terms in their name. Standard MMFs may brand themselves as 'standard' to differentiate between a

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	example, a 'short term cash fund'.	short term fund – for example, a 'standard cash fund'. They are not permitted to use the words 'short term' in their name.
NAV/Unit price approach & valuation practices (MMFs should comply with the general principle of fair value when valuing the securities held in their portfolio. Amortised cost method should be used in limited circumstances.)	<p>i. MMF should adopt mark-to-market and/or fair value valuation methodology. While the industry has a number of funds that use a fixed unit pricing model for the ease of fund administration, nearly all of them utilise marked to market valuation methodology when valuing their portfolio holdings.</p> <p>When marked to market valuation deviate from the fixed unit pricing, there are no restrictions in varying the fixed unit pricing to reflect the market value at any point in time.</p>	<p>i. MMF should adopt mark-to-market and/or fair value valuation methodology. While the industry has a number of funds that use a fixed unit pricing model for the ease of fund administration, nearly all of them utilise marked to market valuation methodology when valuing their portfolio holdings.</p> <p>When marked to market valuation deviate from the fixed unit pricing, there are no restrictions in varying the fixed unit pricing to reflect the market value at any point in time.</p>
	<p>ii. The use of amortised cost accounting should be subject to conditions and monitoring including:</p> <ul style="list-style-type: none"> – Deemed to allow for an appropriate approximation for the price of the instrument; and/or – Restricted to instruments with residual maturity of 90 days and less; and/or – Materiality thresholds (10bps deemed to be appropriate) and escalation procedures in place. 	<p>ii. The use of amortised cost accounting should be subject to conditions and monitoring including:</p> <ul style="list-style-type: none"> – Deemed to allow for an appropriate approximation for the price of the instrument; and/or – Restricted to instruments with residual maturity of 90 days and less; and/or – Materiality thresholds (10bps deemed to be appropriate) and escalation procedures in place.
	<p>iii. MMF valuation practices should be reviewed by a 3rd party as part of their period reviews of the fund accounts</p>	<p>iii. MMF's fund valuation practices should be reviewed by a 3rd party as part of their periodic review of the fund accounts.</p>
	<p>iv. Units in the scheme may have constant or variable NAV/Unit Price.</p> <p>IOSCO recommends that MMFs that offer a stable NAV should be subject to measures designed to reduce the specific risks associated with the stable NAV feature and to internalise the costs arising from these risks.³</p>	<p>iv. Units in the scheme may have constant or variable NAV/Unit Price.</p> <p>IOSCO recommends that MMFs that offer a stable NAV should be subject to measures designed to reduce the specific risks associated with the stable NAV feature and to internalise the costs arising from these risks.⁴</p>

³ If a conversion to variable NAV is not workable, additional safeguards should be put in place to compensate the day to day variations between the stable NAV and underlying asset value.
While there are a number of MMFs that use a fixed unit pricing model for the ease of fund administration, nearly all of them utilize marked-to-market valuation methodology when valuing their portfolio holdings. They can vary their unit pricing to reflect the underlying valuation when significant deviation occurs. If operating a constant NAV MMF with amortised cost accounting methodology, including possible amendments to fund constitutions to allow for gating/suspensions, appropriate safeguards should be considered with respect to global regulation.

⁴ See footnote as above

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Liquidity management	MMFs should establish sound policies and procedures to know their investors. A redemption profile in the customer profiling process will be implemented.	MMFs should establish sound policies and procedures to know their investors. A redemption profile in the customer profiling process will be implemented.
Unit liquidity	MMFs should hold a minimum amount of liquid assets to strengthen their ability to face redemptions and prevent fire sales. MMF to be subject to requirements that 10% of its assets be invested in Daily Liquid Assets and 30% of its assets be invested in Weekly Liquid Assets.	MMFs should hold a minimum amount of liquid assets to strengthen their ability to face redemptions and prevent fire sales. MMF to be subject to requirements that 10% of its assets be invested in Daily Liquid Assets and 30% of its assets be invested in Weekly Liquid Assets.
Stress Testing	Responsible Entities of standard MMFs should regularly conduct stress testing and/or scenario analysis of the material risks identified for the schemes they operate in accordance with the investment strategy, scale and complexity of the schemes.	Responsible Entities of standard MMFs should regularly conduct stress testing and/or scenario analysis of the material risks identified for the schemes they operate in accordance with the investment strategy, scale and complexity of the schemes.
	MMFs should have tools in place to deal with exceptional market conditions and substantial redemption pressures. These tools are currently in place under the Corporations Act and scheme constitution.	MMFs should have tools in place to deal with exceptional market conditions and substantial redemption pressures. These tools are currently in place under the Corporations Act and scheme constitution.
Credit ratings	The Responsible Entity should be responsible for the assessment of credit risk of investments and external credit ratings are only one element to be taken into consideration by Short Term MMFs when assessing the credit quality of an instrument.	The Responsible Entity should be responsible for the assessment of credit risk of investments and external credit ratings are only one element to be taken into consideration by Standard MMFs when assessing the credit quality of an instrument.
	Invest in instruments awarded minimum A2 short term rating, or A- long term rating by Standard and Poor's, or other Nationally Recognised Statistical Rating Organisation (NRSRO).	Invest in instruments awarded minimum A3 short term rating, or BBB long term rating by Standard and Poor's, or other Nationally Recognised Statistical Rating Organisation (NRSRO).
Credit Rating Agencies	No action. This will be covered under a broader regulatory reform in relation to credit ratings and any applicable industry best practice guidelines.	No action. This will be covered under a broader regulatory reform in relation to credit ratings and any applicable industry best practice guidelines.
Disclosure requirements	<i>MMF documentation should include a specific disclosure drawing investors' attention to the absence of a capital guarantee and the possibility of principal loss.</i> This disclosure is part of existing Product Disclosure Statement (PDS) disclosure requirements. MMFs' disclosure to investors should include all necessary information regarding the funds' practices in relation to valuation and the applicable procedures in times of stress. The PDS may reference this type of	<i>MMF documentation should include a specific disclosure drawing investors' attention to the absence of a capital guarantee and the possibility of principal loss.</i> This disclosure is part of existing PDS disclosure requirements. MMFs' disclosure to investors should include all necessary information regarding the funds' practices in relation to valuation and the applicable procedures in times of stress. The PDS may reference this type of fund as a standard fund and reference

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	fund as a short term fund and reference this guidance note.	this guidance note.
Repurchase agreements	The Standard and Poor's limitations on repurchase agreements apply. These limitations are contained in the Standard and Poor's criteria for principal stability fund ratings: <i>Fixed-Income Funds: Principal Stability Fund Rating Methodology</i> .	The Standard and Poor's limitations on repurchase agreements apply. These limitations are contained in the Standard and Poor's criteria for principal stability fund ratings: <i>Fixed-Income Funds: Principal Stability Fund Rating Methodology</i> .