

Regulatory News Alert

ESMA provides guidance on stress testing and reporting standards for MMFs

24 July 2019

Context and objectives

Regulation (EU) 2017/1131 of 14 June 2017 on money market funds (MMFs) (the “MMF Regulation”) requires guidance on selected requirements. Therefore, ESMA (the European Securities and Markets Authority) has now issued **two sets of guidelines** that will help MMFs interpret the existing regulatory requirements.

The issued guidelines are:

- Guidelines on stress test scenarios under the MMF Regulation
- Guidelines on the reporting to competent authorities under Article 37 of the MMF Regulation

The first set of guidelines aim to establish **common reference parameters for the stress test scenarios** to be applied by MMFs.

The second set of guidelines clarifies how MMFs should apply ESMA’s implementing technical standards (ITS), which provide the **reporting template** to be used by MMFs when sending their quarterly reports to national competent authorities (NCAs).

Prescriptive approach chosen over a principles-based one

Both sets of guidelines provide **practical details** on how to implement the scenarios and to complete the respective reporting template. This should facilitate the implementation, improve the consistency, and reduce the costs of conducting stress tests and reporting. The view of some market participants that the existence of granular parameters might increase complexity is rejected by the ESMA – instead, a comprehensive set of parameters would reduce the need to extrapolate or interpret scenarios when a data point is missing. Having **prescriptive and consistent guidelines** is thus deemed necessary to achieve the objective of comparing MMFs exposed to the same risk.

Calibration for the MMF stress tests

The ESMA's guidelines contain among others a section on the **2019 calibration for the stress tests that MMFs need to conduct** and the results of which need to be reported to NCAs. This calibration has been based on the adverse scenario calibrated by the European

Central Bank (ECB) and approved by the European Systemic Risk Board (ESRB) in March 2019.

According to the set out calibration, the following specificities will apply:

1. **Only relevant parameters are included in the guidance**, i.e. shocks applying to instruments with a maturity higher than two years were removed
2. Should managers of MMFs **need a parameter not included in the guidance**, they should **consult the adverse scenario provided by the ESRB** on its website
3. ESMA has defined **shocks to credit spreads** as the difference between bond yields and the swap yield curve but adjusted certain values to avoid negative shocks
4. **Additional calibration is provided where necessary**, i.e. ESMA produced liquidity discount factors for sovereign and corporate bonds by ratings and defined the interest rate yield shocks for countries not included in the ESRB scenario
5. Should inconsistency between the calibration in ESMA's guidelines and the calibration provided by the ESRB exist, **ESMA's guidance will prevail**

To ensure that the calibration of the stress test scenarios remains adequate over time, the guidelines will be updated at least every year and will take into account the latest market developments.

Reporting template for MMFs

Following the publication of the ESMA guidelines on MMF Reporting, the next step for establishing the MMF reporting process at MMFs will include the finalization of the corresponding IT requirements. In particular, ESMA has clarified that the format of the MMF report will comply with the ISO 20022 Standard, which is currently used in both MiFIR and EMIR reporting.

ESMA has confirmed that managers of MMFs will be allowed to report quarterly, even if they are subject to yearly reporting. Furthermore, ESMA has specified that the first reporting should cover the period starting at the authorization date of the MMF and lasting until the end of the reporting period.

The guidelines on the reporting under Article 37 of the MMF Regulation are supplemented by related technical reporting instructions, which were also published by ESMA. These technical documents provide the reporting validation rules specifying the criteria of acceptance of MMF reports by the NCAs and conditions under which fields are not applicable and should not be populated. In addition, the instructions include the XML schemas of the candidate ISO 20022 messages.

Next steps

MMFs and managers of MMFs are expected to **measure the impact** of the common reference stress test scenarios specified in the first set of guidelines. Using these measurements as input, they are then required to **fill in the reporting template** referred to in Article 37 of the MMF Regulation and further explained by the second set of guidelines. This template forms part of the MMF's quarterly reports and must be sent to the NCAs for the first time in **Q1 2020**.

How can Deloitte help?

Deloitte's advisory specialists and dedicated services will help you design and implement your business strategy in light of the future evolution of the regulatory framework and market trends.

Additionally, within its Reporting Factory service, Deloitte can help with a range of solutions for the forthcoming MMF reporting tailored to your business needs.

With our Regulatory Watch Kaleidoscope service, Deloitte can also help you stay ahead of the regulatory curve to better manage and plan upcoming regulations.

Your contacts

Xavier Zaegel

Partner – Capital Markets/Financial Risk Leader
Tel : +352 45145 2748
xzaegel@deloitte.lu

Lou Kiesch

Partner – Regulatory Consulting Leader
Tel : +352 45145 2456
lkiesch@deloitte.lu

Fabian De Keyn

Director – Capital Markets Expert
Tel: +352 45145 3413
fdekeyn@deloitte.lu

Marijana Vuksic

Manager – Regulatory & Consulting
Tel : +352 45145 2311
mvuksic@deloitte.lu

Sylvain Crépin

Partner – Capital Markets/Financial Risk
Tel: +352 45145 4054
screpin@deloitte.lu

Simon Ramos

Partner – IM Advisory & Consulting Leader
Tel : +352 45145 2702
siramos@deloitte.lu

Benoit Sauvage

Director – RegWatch, Strategy
& Consulting
Tel : +352 45145 4220
bsauvage@deloitte.lu

Deloitte Luxembourg
20 Boulevard de Kockelscheuer
L-1821 Luxembourg

Tel: +352 451 451
Fax: +352 451 452 401
www.deloitte.lu

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