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International Regulators' Recommendations and Guidance on Liquidity Mismatch Mitigation Measures



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On 20 December 2023, the Financial Stability Board ("FSB") published [revised policy recommendations to address structural vulnerabilities from liquidity mismatch in open-ended funds \("OEF"\)](#), concurrently with the publication by the International Organisation of Securities Commissions ("IOSCO") of its final [Guidance on Anti-Dilution Liquidity Management Tools \("LMTs"\)](#). The aim of these two papers is to support regulatory and supervisory authorities to effect a framework that addresses vulnerabilities arising from liquidity mismatches and strengthens liquidity management in light of perceived deficiencies in current practices. Alongside recent publications by the FCA, the coming year looks to be one of a focus on liquidity management and resilience in the face of stressed market conditions.

FSB Recommendations

These are addressed to regulatory and supervisory authorities and set out key objectives for an effective regulatory and supervisory framework designed to address liquidity mismatches. The revisions build on the FSB's 2017 Policy Recommendations to Address Structural Vulnerabilities from Asset Management Activities, and updates focus on clarity of redemption terms and conditions linked to the liquidity of the OEF's underlying assets through a categorisation approach (liquid, less liquid, illiquid, etc.) Also emphasised is the need for regulators to make sure that a broad set of anti-dilution and quantity-based LMTs are available to OEF managers and used consistently and with greater regularity in both normal and stressed market conditions, and that those anti-dilution LMTs are included in OEF constitutional documents. The Recommendations shift away from characterising LMTs as exceptional tools towards referring to them as quantity-based measures to be used in stressed market conditions. LMTs contemplated include suspensions, gates, in-kind redemptions and side pockets.

IOSCO Final Report

This sets out guidance to entities on the need for appropriate systems and controls to enable compliance with regulatory requirements for the design and use of anti-dilution LMTs as part of an overall liquidity risk management framework that can adapt to both normal and stressed market conditions. The activation of anti-dilution measures should take place in such a way as to avoid material dilution events for funds, and be subject to robust governance and decision-making tools. As with the FSB Recommendations, investor awareness is key to enable investors to factor in the cost of liquidity to their investment decisions.

Next Steps

The FSB and IOSCO plan to review the process, with that process beginning with a stocktake of measures and practices adopted in FSB member jurisdiction scheduled to complete by the end of 2026. IOSCO will also aim to coordinate a stocktake of its recommendations and guidance with the FSB's. As mentioned above, the UK's Financial Conduct Authority has also been in touch with UK managers about improvements they expect to see in liquidity management practices and techniques (see [here](#) for our note on this) and we anticipate significant regulatory scrutiny to be a feature of this year and into the next with a general emphasis on robust governance, investor awareness and risk management to smooth the effects of stressed market conditions.
