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The Tokenisation of Money Market Funds Part 2: 'What has been achieved so far?'

Recent strides in the technology of tokenisation and its application to funds have created opportunities to enhance the attractiveness of Money Market Funds (MMFs) for investors. As noted in our previous white paper 'The Tokenisation of MMFs'¹, tokenisation brings a number of potentially transformative benefits including increased portability and reduced operational friction, making it much easier to transfer ownership of MMFs and facilitate new usages, such as their use as margin collateral, and thereby attract a wider investor base.

The speed of innovation has attracted a high level of press coverage. This, along with the prospect of significant benefits, has generated momentum as market participants seek to capitalise on technological advances. The speed of change has, however, led to a disparate range of information on the topic and a plethora of terms which can be confusing. This short paper seeks to build on our earlier one in clarifying some of the concepts being used and how they are currently being applied.

We start by looking at where tokenised MMFs fit within the current regulatory framework and then define some of the terms.

MMF Regulation

There is an *a priori* distinction between regulated and non-regulated MMFs which is also a primary consideration when looking at tokenised MMFs. IMMFA MMFs are regulated under EU Regulation 2017/1131 (MMFR'). EU MMFR was retained in UK regulation after the UK's departure from the EU.² All IMMFA MMFs are domiciled in either the EU (primarily Ireland or Luxembourg) or the UK and therefore come under MMFR. Additionally, all IMMFA MMFs have at least one AAA money market fund rating from an authorised credit rating agency. You can see more detail on fund types on the IMMFA website <https://www.immfa.org>.

In the case of tokenised MMFs (for the purposes of this paper we will adopt the acronym 'TMMFs'), it is essential that an investor consider whether the fund falls under existing regulation and in addition, the form of the unit which they hold.

In the following sections we consider the differences between two commonly used terms which describe the form in which TMMFs may be created, namely 'native' and 'non-native'. These processes are in varying stages of implementation. We have taken 'non-native' first as

¹ See IMMFA White Paper 'The Tokenisation of Money Market Funds', February 2025, www.immfa.org

² UK MMFR is still the subject of proposed targeted reforms resulting from the FCA's 2023 Consultation' CP 23/28 'Updating the regime for Money Market Funds', the final outcome of which is as yet undecided. It is also anticipated that the EU may propose reforms.



it is an extension of the existing mode of creation and recording as opposed to the more radical change towards something which exists only in the digital space.

Non-Native Tokenisation

The term 'non-native' tokenisation *refers to a model in which an existing MMF share is tokenised*, a process often noted as the creation of a '*digital twin*' or '*mirror recorded tokenisation*'.³

This process has seen significant activity, predominantly driven by Third Party as opposed to Issuer Driven Tokenisation (defined below). In both instances the shareholder interest in a pre-existing MMF unit remains the same but is recorded via Distributed Ledger Technology (DLT) in addition to the traditional centralised shareholder register held by a transfer agent.

In this instance, the underlying MMF remains the same in all other respects, so in the case of a pre-existing IMMFA MMF unit being tokenised, that MMF unit would continue to be governed by the constraints of the regulation.

Tokenisation of the fund allows for a much more efficient transfer (portability) of the units.

Third Party Tokenisation

Third party tokenisation refers to the role of tokenising agents. The manager of an MMF may open an account with a tokenising agent and put in place a distribution agreement which allows that agent to tokenise MMF units. This process is essentially the same as that currently taking place between managers and custodians under an omnibus agreement.

There is also significant activity in this sphere and there are a number of tokenisation agents operating in the field.

Any third party tokenisation agent which has entered into a distribution arrangement with the MMF manager is allowed to tokenise units in the MMF whilst retaining the integrity of the registration constraints of the traditional MMF.

The end investor holds the physical shares in the MMF in the traditional way, i.e. on an off-chain shareholder register, albeit within the intermediary account of the tokenising agent. That share unit can then be immobilised and tokenised by this third party agent. ***This means that each share unit remains in the investor's account, but that interest is also represented in parallel on the DLT.*** In this instance, assuming the MMF is regulated in the first place, nothing changes in that respect i.e. the MMF continues to be governed by existing regulation.

³ Other terms for 'non-native' include hybrid register, off chain register and, as stated, digital twin and mirror recorded.



Issuer Driven Tokenisation

Issuer driven tokenisation refers to a process **where the fund manager themselves**, in concert with their existing transfer agent or, alternatively, a dedicated tokenisation agent, **tokenises units or share classes of an existing fund**.

The benefit of issuer-led tokenisation, as it stands today, is that the product scale and liquidity remain intact (versus potential fragmentation through third party tokenisation).

IMMFA members are keen to support the move of the TradFi (traditional finance) market to one which is on-chain. Such a move has the ability to unlock greater opportunities including the use of TMMFs as collateral, something which we have strongly advocated. **The ability to leverage existing franchises, whilst retaining the regulatory framework that traditional investors seek, is key.**

Native Tokenisation

A 'native' tokenised MMF is **one where ownership of the shareholder units has been represented digitally ab ovo**, i.e. from the initial point when the fund came into existence. This is distinct from non-native fund where a pre-existing fund created in traditional format has some⁴ share classes subsequently tokenised.

A number of digitally native funds have been established, and some have attracted significant inflows. To date, these have mostly been private⁵ funds that have cash-style investment guidelines and are initially intended for a DeFi (decentralised finance) investor base. This means they will settle on-chain using digital money.

Whilst some of these native tokenised funds are domiciled in EU jurisdictions where regulated MMFs are equally present, **this does not mean that they are necessarily subject to the same MMF regulation**, nor that they are IMMFA MMFs (since all IMMFA MMFs fall under MMFR). In the case of Luxembourg, specific legislation to support tokenised assets has been introduced and at least one native TMMF domiciled in Luxembourg has been approved as a regulated TMMF. Other jurisdictions have, as yet, not gone that far.

Other native tokenised funds have, for example, used the British Virgin Islands⁶.

⁴ Or all, since that is theoretically possible.

⁵ I.e., the blockchain is restricted to a group of participants who have been granted access to that network.

⁶ In this case the fund would not be regulated under MMFR as that only covers EU jurisdictions.



Conclusion

To conclude, in time we are likely to see IMMFA members evolving in one of the following directions:

- i. Tokenisation of existing share classes
- ii. Tokenisation of a new, digitally focused set of share classes.
- iii. Native tokenisation as outlined above.

The readiness and approach of the relevant EU jurisdictions where most MMFs are domiciled currently varies but we expect to see national competent authorities and regulators gradually enhance the frameworks to support tokenisation. We would certainly welcome such developments.

This paper has aimed to provide a snapshot of where the development of tokenised MMFs currently stands. We close by noting that the product cycle is evolving very rapidly and we can certainly expect further changes to come.

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