FSB FINANCIAL STABILITY BOARD

Leverage in Non-Bank Financial Intermediation: Consultation report

Response to Consultation

Bundesverband Investment und Asset Management (BVI)

Recommendation 1

1. **Is the description of the financial stability risks from leverage in NBFI accurate and comprehensive? Are there additional vulnerabilities or risk dimensions related to NBFI leverage that authorities should consider for monitoring purposes?**

In fact, the use of leverage via investment funds is rather low in Germany, but also in the EU as a whole (please see ESMA's TRV Risk Analysis, Financial Stability, Assessing risks posed by leveraged AIFs in the EU). Only the European hedge fund sector has high leverage and this may pose a risk of market impact. However, hedge funds account for only a very small share of the total European market. In 2022, they are only account for 2 percent of the total AIF market, which in turn accounted for around 36 percent of the NAV of the EU fund industry at the end of 2022. Moreover, most hedge funds domiciled in two EU Member States (not in Germany) also dispose of large levels of cash to address potential margin calls, which limits the risk of fire sales.

Irrespective of this, we generally support the FSB's approach of establishing policy recommendations to address financial stability risks arising from leverage in the entire NBFI sector and analysing any need for further action. However, after many years of using the term 'shadow banking' after the 2008 financial crisis, which was introduced at the time without any pejorative meaning, it is important to emphasise that many of the entities covered by the NBFI concept are themselves subject to strict regulations in the European Union. Compared to other legislators in other countries, the EU Commission has already done its homework. This applies in particular to investment funds managed by managers who fall under the AIFM and UCITS Directives and account for a good 21 per cent of the NBFI sector in the EU. The well-functioning European regulatory system should not be overloaded with new and different international recommendations just because jurisdictions outside the EU are maybe not able to establish adequate rules or monitor compliance with these rules and therefore cases may arise that have an impact on the financial market in certain countries (such as the Archegos debacle and the UK gilt crisis in 2022).

The failure of Archegos Capital Management, an unregulated 'family office' outside the EU, as mentioned in the consultation paper, cannot be used as an example to justify the

introduction of additional measures in the already strictly regulated fund sector. In order not to underestimate the possible impact of unregulated market participants in the NBFI sector, we suggest conducting an overall review of the activities of unregulated NBFI and their impact on financial stability. If these firms are found to be capable of posing systemic risks to the financial market, supervisors should carefully consider the effectiveness, feasibility and potential costs when designing policy measures.

2. **What are the most effective risk metrics that should be considered by authorities to identify and monitor financial stability risks arising from NBFI leverage?**

In the context of funds as NBFI, we refer to the toolkit that ESMA has already established in the EU in the context of the AIFM Directive in the guidelines on Article 25 of Directive 2011/61/EU. There is no need for additional metrics that authorities should consider for monitoring purposes. In particular, we observe that in several areas excessive regulation ties up huge amounts of resources that could be used for investments in technology and the development of new markets. Instead of developing a new macroprudential policy framework that would duplicate the existing sector-specific frameworks, the existing instruments should first be utilised to the full and used in a balanced way without compromising the global competitiveness of companies.

Furthermore, we would like to point out that it makes no sense to apply the toolkit metrics at the entitylevel to all NBFI as explained in the last section under the first recommendation. In the case of investment funds, the focus should be exclusively on the use of leverage at the fund level.

3. **What are the most effective metrics for the monitoring of financial stability risks resulting from:**

(i) specific market activities, such as trading and investing in repos and derivatives

With the updated European Market Infrastructure Regulation (EMIR), the European legislator has established strict cross-sectoral rules to curb systemic risks in the European derivatives market. This results in further comprehensive obligations for certain parties, including investment funds, and for authorities to monitor these risks.

Moreover, we refer to the ESMA guidelines on Article 25 of Directive 2011/61/EU which require competent authorities to monitor potential liquidity demands from collateral calls (on funds' derivatives and repo) relative to available liquid assets for each fund in focus of the monitoring.

(ii) specific types of entities, such as hedge funds, other leveraged investment funds, insurance companies and pension funds

In the context of funds as NBFI, we would welcome a two-step approach: Identifying and analysing funds that may pose a risk to financial stability as a first step and further analysis of this sub-set of funds as a second step. This approach appropriately takes into account that not all investment funds could pose financial stability risks. This applies, in particular, for small-sized funds. We would therefore suggest the FSB to limit the scope of application of its Recommendations to cases where the fund rules explicitly permit the use of leverage on a substantial basis.

However, we are aware that rules relating to measure and report market exposure of investment funds vary around the world. There is a wide variety of funds and fund strategies with different jurisdictions and market structures which allow different methods to increase the fund's market exposure beyond its net asset value. Moreover, national legal requirements could limit the use of leverage in certain funds such as retail funds or funds for institutional investors (e. g. limits for borrowing of cash, limits for using derivatives, and special requirements for borrowing of securities). Even if the use of methods by which the fund manager could increase the fund's exposure differs among investment funds on micro level around the world, the metric for the calculation of the market exposure for identifying macro-economic risks should be based, in principle, on the same method. Such an approach would efficiently ensure a sustainable and meaningful understanding and monitoring of leverage for financial stability purposes.

Therefore, it is of utmost importance to clarify a global approach for leverage in funds and its calculation to facilitate more meaningful monitoring of leverage for financial stability purposes. In particular, we see the need for a common understanding among regulators, asset managers and investors. This is also a crucial prerequisite in periods of market stress where timely decisions by national competent authorities (NCAs), supra national authorities and market participants are essential. Leverage in investment funds means methods such as the use of derivatives, borrowing of cash or securities which might, but not necessarily have to increase the ratio of the fund's market exposure over its net asset value. There is a wide variety of funds and fund strategies in different jurisdictions and market structures which allow for different methods to increase leverage. The general understanding of leverage in investment funds is as follows: The ratio of the fund's market exposure over its net asset value. In this respect, the use of leverage is not a risk as such rather than a purely technique that allows to assess whether there could be a risk. However, the main challenge is to define meaningful metrics with supplementary data points for the calculation of the market exposure to monitor funds from a macroeconomic perspective. We propose to keep the metric as simple as possible.

(iii) concentration and crowded trading strategies

Data exchange between the respective authorities is an option in order to gain a better insight into the respective transactions. In particular, the supervisors should continue work on better data collection about NBFIs and data exchange between the authorities and policy makers. Before further macroprudential measures are defined, this data should first be adequately analysed and evaluated. Assertions for possible systemic risks based on model calculations are not sufficiently valid.

For example, competent authorities already facilitate analysis of the risk impact of investment funds in the European Union. In particular, information of the risk profile of alternative investment funds gathered by competent authorities are shared with ESMA and the ESRB so as to facilitate a collective analysis of the impact of the risk profile (including leverage and liquidity) of investment funds on the financial system in the Union as well as a common response to potential risks. This is also planned for UCITS and laid down in the EU legal texts. These measures ensure that competent authorities are able to quickly

intervene on a case-by-case basis in case of identified potential risks to financial stability or to the functioning of financial markets.

Recommendation 3

4. **What types of publicly disclosed information (e.g. transaction volumes, outstanding amounts, aggregated regulatory data) are useful for market participants to enhance their liquidity or counterparty credit risk management? Are there trade-offs in publicly disclosing such information and, if so, what would be the most important elements to consider? What is the appropriate publication frequency and level of aggregation of publicly disclosed information?**

In principle, we believe it makes sense for the results of the analyses carried out by authorities to assess systemic risks to be made available to market participants in a transparent manner. For example, we welcome ESMA's insights about their analyses of investment funds in its Economic Report on stress simulation for investment funds: As a main outcome, the fund industry is resilient and is able to absorb economic shocks. We also welcome that ESMA has already started establishing guidance to operationalising existing tools to address risks and to identify the effect of macro-systemic shocks affecting the economy as a whole. Comparable publication methods could be used by all financial stability bodies.

In any case, public announcements should only summarise anonymised and aggregated data, without disclosing information about the risks of individual companies or funds. Such detailed entity- or fund-related information could have undesirable effects on the market, especially if published in real time. Therefore, potential systemic risks or measures relating to specific NBFI should only be discussed between the supervisors and the respective company, along with any possible actions. If certain identified risks affect the entire market (or parts of it), it may also be useful for the relevant authorities to publish appropriate warnings here, without naming individual market participants. However, there is a need for better transparency of risk analyses on a country basis in the reports published by the supervisors assessing the impact of any potential systemic risks for the European financial market – individual risk factors were only visible in certain markets (such as LDI funds).

Moreover, the lack of standards for financial market data makes reporting and supervision by the authorities more difficult. In addition, the financial sector is dependent on data oligopolies such as stock exchanges, rating agencies, or index providers and has to accept massive price increases due to their market dominance. The regulatory framework for the provision and use of financial market data should therefore be improved under appropriate conditions. We also recommend making data available free of charge and licence-free via a public data collection point for benchmarks, making the European Rating Platform practicable for institutional use, stipulating in EU law that market data is not protected by copyright, and expanding the equity ticker (consolidated tape) to include pre-trade data. We are also calling for the streamlining of supervisory reporting requirements at the EU level.

Recommendation 5

5. **Do Recommendations 4 and 5 sufficiently capture measures that would be used to address the scope of non-bank financial entities under consideration in this report? In what ways may the policy measures proposed in the consultation report need to be adjusted to account for different types of non-bank financial entities?**

   We refer to investment funds as NBFIs. They play a significant role in financing the real economy. They bring together the money provided by millions of savers and institutional investors and match it with the capital demands of companies and governments. They therefore enable growth and innovation. Moreover, we consider investment funds to diminish systemic risks in general as they balance between investors who want to divest and those who want to invest in a financial market. In general, the European fund industry is resilient and able to absorb economic shocks. One of the reasons for this is that the AIFM and UCITS Directives already contain comprehensive measures to address the handling of relevant financial risk on a micro level and any systemic risks on a macro level. In addition, other EU frameworks such as the CRD/CRR and Solvency II Directive impose strict regulatory requirements on investments by institutional investors such as banks and insurance companies in funds, so that the interconnectedness between institutional investors and their investments in funds is already considered. Moreover, with the updated European Market Infrastructure Regulation (EMIR), the European legislator has established strict cross-sectoral rules to curb systemic risks in the European derivatives market. This results in further comprehensive obligations for certain parties, including investment funds.

   In our view, these existing sector-specific requirements in the European NBFI sector already cover the requirements and measures demanded by recommendations 4 and 5. There is no need for additional macro-prudential tools similar to the ones existing in the banking sector. In particular, we are strictly opposed to extending rules or measurements that the banking supervisors have developed solely for banks to the fund industry. There are fundamental differences in the business models and risk assessments, so that the macro tools developed for banks are in no way suitable for transfer to NBFIs. This applies in particular to the margin requirements, minimum haircuts in securities financing transactions and large exposure reporting requirements for individual asset classes and markets established for banks only. The same applies to the calibration of reporting limits on the basis of stress tests or liquidation cost analyses.

   Moreover, narrowing down the range of eligible assets is not a commensurate measure to address any perceived shortcomings identified in individual cases with internal and external governance failures on fulfilling the strict framework for asset managers. The same applies to liquidity buffers in investment funds. Instead, we are in favour of further developing the governance requirements while retaining the flexibility in terms of eligible exposures and liquidity management.

6. **In what circumstances can activity-based measures, such as (i) minimum haircuts in securities financing transactions, including government bond repos, (ii) enhanced margin requirements between non-bank financial entities and their derivatives counterparties, or (iii) central clearing, be effective in addressing financial stability risks related to NBFI leverage in core financial markets, including government bond**

markets? To what extent can these three types of policy measures complement each other?

In general, we welcome a global discussion on activity-based measures, such as liquidity preparedness for margin and collateral calls during times of stress. However, we do not agree with the result of the analysis laid out in the FSB's consultation report that – based on individual cases – the fund sector as part of the NBFI sector is not adequately prepared with respect to spikes in margin and collateral calls and therefore new and strict rules are necessary. The European legislator has already provided a highly regulated framework for investment funds and their liquidity management including margin calls and collateral management. In fact, strict rules and practises on liquidity management of margin and collateral have been in place for many years for European investment funds. In this context, we refer to our position paper on that FSB consultation.

However, regarding interconnectedness, for both banks and non-banks, due to the current dispositions of some regulations on eligible assets for meeting margin calls, the interconnectedness can also have the role of a stress canal, especially when the margin call volumes are unexpected. For instance, being required to only use cash as collateral for meeting variation margin calls implies to sell assets and can have an unintended procyclical effect and amplify stress on the markets. Being able to put as collateral for cleared markets' variation margin calls, along cash, highly liquid assets (in particular investment grade government bonds) would significantly limit contagion during stressed moments on the markets and hence contribute to financial stability.

7. **Are there benefits to dynamic approaches to minimum margin and haircut requirements, e.g. where the requirements change based on changes in concentration or system-wide leverage? If so, what types of indicators capturing concentration or system-wide leverage should the requirements be linked to?**

   We refer to our answers to questions 5 to 6.

8. **Are there any potential unintended consequences from activity-based measures beyond those identified in the consultation report?**

   We refer to our answers to questions 5 to 6.

9. **For non-centrally cleared securities financing transactions, including government bond repos, what are the merits of margin requirements compared to minimum haircuts?**

   We refer to our answers to questions 5 to 6.

10. **In what circumstances can entity-based measures, such as (i) direct and (ii) indirect leverage limits be effective in addressing financial stability risks related to NBFI leverage in core financial markets?**

    We would like to point out that it makes no sense to apply the toolkit metrics at the entity-level to all NBFI. In the case of investment funds, the focus should be exclusively on the use of leverage at the fund level. Here, too, the AIFM and UCITS Directives already provide appropriate measures to assess any systemic leverage risks of funds. This also includes the reporting obligations to the supervisory authorities laid down therein and the exchange of data between the relevant authorities, which is now addressed by the AIFMD review.

According to the AIFMD, managers of AIFs are required to set leverage limits for the funds they manage, to monitor the leverage and to disclose information regarding the overall level of leverage employed vis-à-vis investors and competent authorities. UCITS are legally restricted in using leverage methods such as use of derivatives and borrowing agreements. In addition, national legal requirements might limit the use of leverage in certain funds. Even if the acceptable methods by which the fund manager may increase the fund's exposure differ among investment funds in order to protect investors, the calculation of the market exposure should be based, in principle, on the same method for both UCITS and AIFs. Such an approach would ensure a sustainable and meaningful understanding and monitoring of leverage for financial stability purposes. However, it is important to highlight that the use of leverage by investment funds is limited within the European market, with the notable exception of hedge funds.

11. **Are there ways to design and calibrate entity-based measures to increase their risk sensitivity and/or their effectiveness in addressing financial stability risks from NBFI leverage?**

    We refer to our answers to questions 5, 6 and 10.

12. **Are there any potential unintended consequences from entity-based measures beyond those identified in the consultation report?**

    We refer to our answers to questions 5, 6 and 10.

13. **To what extent can activity-based and entity-based measures complement each other? What are the main considerations around using these two types of measures in combination?**

    We refer to our answers to questions 5, 6 and 10.

Recommendation 6

14. **How could counterparty credit risk management requirements for leverage providers be enhanced to be more effective in addressing financial stability risks from NBFI leverage in core financial markets, such as government bond repo markets? In what circumstances can they be most effective?**

    We request that recommendation 6 be amended to indicate that it only applies to the authorities of banks that fall within the scope of the new BCBS guidelines for managing counterparty credit risk and that leverage the NBFI sector (proposed amendment in recommendation 6: "Authorities of banks should ensure …"). In fact, the BCBS has stated that these guidelines "are intended to apply to [...] banks". Therefore, as the proposed recommendation has a broader scope (i.e. authorities of NBFI and their debt providers), they could be misunderstood to imply that the BCBS guidelines should also apply to authorities of NBFI.

    Moreover, the European requirements (such as the CRD/CRR) already comprehensively cover any significant risks from exposures of banks to NBFIs. It is the interlinked bank's responsibility (here: acting as a lender) to appropriately evaluate their exposure – not only to NBFI – and to integrate it into their internal risk management systems. In particular, banks

are responsible for how they hedge NBFI transactions as part of their own risk processes. If they cannot keep their promises to pay because investment funds are potential ‘risky’, this must not lead to tighter rules for investment funds or their manager. After all, funds are inherently risky. Rather, banks must assess and evaluate their own risks. The European banking regulations in the CRD/CRR contain sufficient rules for this. We therefore see no need for further action here. Rather, what is needed is consistent and appropriate supervision of compliance with the existing rules.

Recommendation 7

15. **Would a minimum set of disclosures to be provided by leverage users to leverage providers be beneficial in improving counterparty credit risk management and reducing financial stability risks from NBFI leverage, including concentration risks? If so, which types of information and what level of granularity should (and should not) be included in this minimum set and why?**

    We do not see the need to further work on additional standard tools for private disclosure between the financial entities. These are professional market participants who are well able to demand the information they need from the counterparty for their own risk management.

16. **What are the main impediments that leverage users face in sharing additional or more granular data with their leverage providers? Is there a risk that a minimum recommended set of disclosures may lead leverage users to limit the information they share with their leverage providers to that minimum set?**

    We do not see the need to further work on additional standard tools for private disclosure between the financial entities. These are professional market participants who are well able to demand the information they need from the counterparty for their own risk management.

17. **Should such a minimum set of disclosures rely on harmonised data and metrics to ensure transparency and efficiency in the use of such information for risk management purposes? Do respondents agree that such a minimum set of disclosures should be based on the list of principles outlined in the consultation report? If not, which principles should be added, deleted or amended?**

    We do not see the need to further work on additional standard tools for private disclosure between the financial entities. These are professional market participants who are well able to demand the information they need from the counterparty for their own risk management.

18. **Should leverage users be required or expected to provide enhanced disclosures (beyond that provided in normal market conditions) to their leverage providers during times of stress?**

    We do not see the need to further work on additional standard tools for private disclosure between the financial entities. These are professional market participants who are well able to demand the information they need from the counterparty for their own risk management.

19. **Should authorities design a minimum set of harmonised disclosures and guidelines on its application, or should they convene a cross-industry working group to do so? How do respondents believe such a standard should be incorporated into market practice? Through regulation, supervisory guidance, and/or via a Code of Conduct or similar approach?**

We do not see a need for international guidelines to harmonise the disclosure of leverage to users of leverage. In the case of funds, these are the investors or the competent authorities. In both cases, the AIFM and UCITS directives already provide sufficient and efficient disclosure requirements for the European market. If efforts are to be made at the international level, no additional standards should be set.

Recommendation 8

20. Are there areas where the principle of "same risk, same regulatory treatment" should be more consistently applied? Are there circumstances in which the principle should not apply or should not apply comprehensively?

We cannot identify any areas where the principle of "same risk, same regulatory treatment" could be more consistently applied to the NBFI sector. Managing investment funds differs fundamentally from business models of banks or other types of financial entities such as insurance companies.

Asset managers are neither banks nor insurance companies, but a separate pillar of the financial economy. They act as agents on behalf of their investors and are subject to fiduciary duties to act in the best interest of investors. They do not have custody over the assets, as these are "safe-kept" by separate depositary institutions. The fund assets are thus never part of the asset manager's own balance sheet. Therefore, own capital of asset management companies is not required to bail out struggling funds. Importantly, the investment results of investment funds – whether positive or negative – belong to the investors. Own capital is only needed to ensure that the operational and potential professional liability risks are appropriately covered. That includes risks resulting from asset managers' activities such as damage or loss caused by staff members, events resulting from negligent actions, errors or omissions, failure to prevent, by means of adequate internal control systems or fraudulent behaviour within the organisation. Moreover, in a context of continued investor inflows and growth of the asset management sector, it is self-explanatory that growth of professional liability risks is continuing to be proportionate. The increase of own capital of asset managers, observed in the current practice, is therefore due to cover increased professional liability risk resulting not least because of much stricter organisational requirements for asset managers established after the financial crisis.

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Frankfurt,
28 February 2025

BVI[1] position paper on FSB's consultation report on leverage in non-bank financial intermediation

We take the opportunity to present BVI's views on the FSB's consultation report on leverage in non-bank financial intermediation (NBFI).

Recommendation 1

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In fact, the use of leverage via investment funds is rather low in Germany, but also in the EU as a whole (please see ESMA's TRV Risk Analysis, Financial Stability, Assessing risks posed by leveraged AIFs in the EU). Only the **European hedge fund sector** has high leverage and this may pose a risk of market impact. However, hedge funds account for only a very small share of the total European market. In 2022, they are only account for 2 percent of the total AIF market, which in turn accounted for around 36 percent of the NAV of the EU fund industry at the end of 2022. Moreover, most hedge funds domiciled in two EU Member States (not in Germany) also dispose of large levels of cash to address potential margin calls, which limits the risk of fire sales.

Irrespective of this, we generally support the FSB's approach of establishing policy recommendations to address financial stability risks arising from leverage in the entire NBFI sector and analysing any need for further action. However, after many years of using the term 'shadow banking' after the 2008 financial crisis, which was introduced at the time without any pejorative meaning,[2] it is important to emphasise that many of the entities covered by the NBFI concept are themselves subject to strict regulations in the European Union. **Compared to other legislators in other countries, the EU Commission has already done its homework**. This applies in particular to investment funds managed by managers who fall under the AIFM and UCITS Directives and account for a good 21 per cent of the NBFI sector in the EU. **The well-functioning European regulatory system should not be overloaded with new and different international recommendations just because jurisdictions outside the EU are maybe not able to establish adequate rules or monitor compliance with these rules and therefore cases may arise that have an impact on the financial market in certain countries (such as the Archegos debacle and the UK gilt crisis in 2022).**

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[1] BVI represents the interests of the German fund industry at national and international level. The association promotes sensible regulation of the fund business as well as fair competition vis-à-vis policy makers and regulators. Asset managers act as trustees in the sole interest of the investor and are subject to strict regulation. Funds match funding investors and the capital demands of companies and governments, thus fulfilling an important macro-economic function. BVI's 115 members manage assets of EUR 4.4 trillion for retail investors, insurance companies, pension and retirement schemes, banks, churches and foundations. With a share of 27%, Germany represents the largest fund market in the EU. BVI's ID number in the EU Transparency Register is 96816064173-47. For more information, please visit www.bvi.de/en.

[2] Cf. footnote 3 of the Recommendations of the Financial Stability Board, Shadow Banking: Strengthening Oversight and Regulation, 27 October 2011.

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Recommendation 5

5. Do Recommendations 4 and 5 sufficiently capture measures that would be used to address the scope of non-bank financial entities under consideration in this report? In what ways may the policy measures proposed in the consultation report need to be adjusted to account for different types of non-bank financial entities?

We refer to investment funds as NBFIs. They play a significant role in financing the real economy. They bring together the money provided by millions of savers and institutional investors and match it with the capital demands of companies and governments. They therefore enable growth and innovation. Moreover, we consider investment funds to diminish systemic risks in general as they balance between investors who want to divest and those who want to invest in a financial market. In general, the European fund industry is resilient and able to absorb economic shocks. One of the reasons for this is that the AIFM and UCITS Directives already contain comprehensive measures to address the handling of

relevant financial risk on a micro level and any systemic risks on a macro level. In addition, other EU frameworks such as the CRD/CRR and Solvency II Directive impose strict regulatory requirements on investments by institutional investors such as banks and insurance companies in funds, so that the interconnectedness between institutional investors and their investments in funds is already considered. Moreover, with the updated European Market Infrastructure Regulation (EMIR), the European legislator has established strict cross-sectoral rules to curb systemic risks in the European derivatives market. This results in further comprehensive obligations for certain parties, including investment funds.

In our view, these existing sector-specific requirements in the European NBFI sector already cover the requirements and measures demanded by recommendations 4 and 5. There is no need for additional macro-prudential tools similar to the ones existing in the banking sector. In particular, we are strictly opposed to extending rules or measurements that the banking supervisors have developed solely for banks to the fund industry. There are fundamental differences in the business models and risk assessments, so that the macro tools developed for banks are in no way suitable for transfer to NBFIs. This applies in particular to the margin requirements, minimum haircuts in securities financing transactions and large exposure reporting requirements for individual asset classes and markets established for banks only. The same applies to the calibration of reporting limits on the basis of stress tests or liquidation cost analyses.

Moreover, narrowing down the range of eligible assets is not a commensurate measure to address any perceived shortcomings identified in individual cases with internal and external governance failures on fulfilling the strict framework for asset managers. The same applies to liquidity buffers in investment funds. Instead, we are in favour of further developing the governance requirements while retaining the flexibility in terms of eligible exposures and liquidity management.

6. In what circumstances can activity-based measures, such as (i) minimum haircuts in securities financing transactions, including government bond repos, (ii) enhanced margin requirements between non-bank financial entities and their derivatives counterparties, or (iii) central clearing, be effective in addressing financial stability risks related to NBFI leverage in core financial markets, including government bond markets? To what extent can these three types of policy measures complement each other?

In general, we welcome a global discussion on activity-based measures, such as liquidity preparedness for margin and collateral calls during times of stress. However, we do not agree with the result of the analysis laid out in the FSB's consultation report that – based on individual cases – the fund sector as part of the NBFI sector is not adequately prepared with respect to spikes in margin and collateral calls and therefore new and strict rules are necessary. The European legislator has already provided a highly regulated framework for investment funds and their liquidity management including margin calls and collateral management. In fact, strict rules and practises on liquidity management of margin and collateral have been in place for many years for European investment funds. In this context, we refer to our position paper on that FSB consultation.

However, regarding interconnectedness, for both banks and non-banks, due to the current dispositions of some regulations on eligible assets for meeting margin calls, the interconnectedness can also have the role of a stress canal, especially when the margin call volumes are unexpected. For instance, being required to only use cash as collateral for meeting variation margin calls implies to sell assets and can have an unintended procyclical effect and amplify stress on the markets. Being able to put as collateral for cleared markets' variation margin calls, along cash, highly liquid assets (in particular investment grade government bonds) would significantly limit contagion during stressed moments on the markets and hence contribute to financial stability.

7. Are there benefits to dynamic approaches to minimum margin and haircut requirements, e.g. where the requirements change based on changes in concentration or system-wide leverage? If so, what types of indicators capturing concentration or system-wide leverage should the requirements be linked to?
8. Are there any potential unintended consequences from activity-based measures beyond those identified in the consultation report?
9. For non-centrally cleared securities financing transactions, including government bond repos, what are the merits of margin requirements compared to minimum haircuts?

We refer to our answers to questions 5 to 6.

10. In what circumstances can entity-based measures, such as (i) direct and (ii) indirect leverage limits be effective in addressing financial stability risks related to NBFI leverage in core financial markets?

We would like to point out that it makes no sense to apply the toolkit metrics at the entity-level to all NBFI. In the case of investment funds, the focus should be exclusively on the **use of leverage at the fund level**. Here, too, the AIFM and UCITS Directives already provide appropriate measures to assess any systemic leverage risks of funds. This also includes the reporting obligations to the supervisory authorities laid down therein and the exchange of data between the relevant authorities, which is now addressed by the AIFMD review.

According to the AIFMD, managers of AIFs are required to set leverage limits for the funds they manage, to monitor the leverage and to disclose information regarding the overall level of leverage employed vis-à-vis investors and competent authorities. UCITS are legally restricted in using leverage methods such as use of derivatives and borrowing agreements. In addition, national legal requirements might limit the use of leverage in certain funds. Even if the acceptable methods by which the fund manager may increase the fund's exposure differ among investment funds in order to protect investors, the calculation of the market exposure should be based, in principle, on the same method for both UCITS and AIFs. Such an approach would ensure a sustainable and meaningful understanding and monitoring of leverage for financial stability purposes. However, it is important to highlight that the use of leverage by investment funds is limited within the European market, with the notable exception of hedge funds.

11. Are there ways to design and calibrate entity-based measures to increase their risk sensitivity and/or their effectiveness in addressing financial stability risks from NBFI leverage?
12. Are there any potential unintended consequences from entity-based measures beyond those identified in the consultation report?
13. To what extent can activity-based and entity-based measures complement each other? What are the main considerations around using these two types of measures in combination?

We refer to our answers to questions 5, 6 and 10.

Recommendation 6

14. How could counterparty credit risk management requirements for leverage providers be enhanced to be more effective in addressing financial stability risks from NBFI leverage in core financial markets, such as government bond repo markets? In what circumstances can they be most effective?

We request that recommendation 6 be amended to indicate that it only applies to the authorities of banks that fall within the scope of the new BCBS guidelines for managing counterparty credit risk and that leverage the NBFI sector (proposed amendment in recommendation 6: *"Authorities **of banks** should ensure …"*). In fact, the BCBS has stated that these guidelines "are intended to apply to [...] banks". Therefore, as the proposed recommendation has a broader scope (i.e. authorities of NBFI and their debt providers), they could be misunderstood to imply that the BCBS guidelines should also apply to authorities of NBFI.

Moreover, the European requirements (such as the CRD/CRR) already comprehensively cover any significant risks from exposures of banks to NBFIs. It is the interlinked bank's responsibility (here: acting as a lender) to appropriately evaluate their exposure – not only to NBFI – and to integrate it into their internal risk management systems. In particular, banks are responsible for how they hedge NBFI transactions as part of their own risk processes. If they cannot keep their promises to pay because investment funds are potential 'risky', this must not lead to tighter rules for investment funds or their manager. After all, funds are inherently risky. Rather, banks must assess and evaluate their own risks. The European banking regulations in the CRD/CRR contain sufficient rules for this. We therefore see no need for further action here. **Rather, what is needed is consistent and appropriate supervision of compliance with the existing rules.**

Recommendation 7

15. Would a minimum set of disclosures to be provided by leverage users to leverage providers be beneficial in improving counterparty credit risk management and reducing financial stability risks from NBFI leverage, including concentration risks? If so, which types of information and what level of granularity should (and should not) be included in this minimum set and why?
16. What are the main impediments that leverage users face in sharing additional or more granular data with their leverage providers? Is there a risk that a minimum recommended set of disclosures may lead leverage users to limit the information they share with their leverage providers to that minimum set?
17. Should such a minimum set of disclosures rely on harmonised data and metrics to ensure transparency and efficiency in the use of such information for risk management purposes? Do respondents agree that such a minimum set of disclosures should be based on the list of principles outlined in the consultation report? If not, which principles should be added, deleted or amended?
18. Should leverage users be required or expected to provide enhanced disclosures (beyond that provided in normal market conditions) to their leverage providers during times of stress?

We do not see the need to further work on additional standard tools for private disclosure between the financial entities. These are professional market participants who are well able to demand the information they need from the counterparty for their own risk management.

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19. Should authorities design a minimum set of harmonised disclosures and guidelines on its application, or should they convene a cross-industry working group to do so? How do respondents believe such a standard should be incorporated into market practice? Through regulation, supervisory guidance, and/or via a Code of Conduct or similar approach?

We do not see a need for international guidelines to harmonise the disclosure of leverage to users of leverage. In the case of funds, these are the investors or the competent authorities. In both cases, the AIFM and UCITS directives already provide sufficient and efficient disclosure requirements for the European market. If efforts are to be made at the international level, no additional standards should be set.

Recommendation 8

20. Are there areas where the principle of "same risk, same regulatory treatment" should be more consistently applied? Are there circumstances in which the principle should not apply or should not apply comprehensively?

We cannot identify any areas where the principle of "same risk, same regulatory treatment" could be more consistently applied to the NBFI sector. **Managing investment funds differs fundamentally from business models of banks or other types of financial entities such as insurance companies.**

Asset managers are neither banks nor insurance companies, but a separate pillar of the financial economy. They act as agents on behalf of their investors and are subject to fiduciary duties to act in the best interest of investors. They do not have custody over the assets, as these are "safe-kept" by separate depositary institutions. The fund assets are thus never part of the asset manager's own balance sheet. Therefore, own capital of asset management companies is not required to bail out struggling funds. Importantly, the investment results of investment funds – whether positive or negative – belong to the investors. Own capital is only needed to ensure that the operational and potential professional liability risks are appropriately covered. That includes risks resulting from asset managers' activities such as damage or loss caused by staff members, events resulting from negligent actions, errors or omissions, failure to prevent, by means of adequate internal control systems or fraudulent behaviour within the organisation. Moreover, in a context of continued investor inflows and growth of the asset management sector, it is self-explanatory that growth of professional liability risks is continuing to be proportionate. The increase of own capital of asset managers, observed in the current practice, is therefore due to cover increased professional liability risk resulting not least because of much stricter organisational requirements for asset managers established after the financial crisis.