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European Systemic Risk Board
European System of Financial Supervision

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ECB-PUBLIC

ESRB/2021/0007

ESRB response to the European Commission consultation on the review of AIFMD

29 January 2021

Dear Commissioner McGuinness, Dear Mairead,

I am writing to you with reference to the consultation your services are conducting on the review of the Alternative Investment Fund Managers Directive (AIFMD)[1]. This letter sets out the position of the General Board of the European Systemic Risk Board (ESRB) on the AIFMD.

The AIFMD contributes to the safety of the financial system, including by providing the ESRB and supervisory authorities with important data to help analyse systemic risks. Nevertheless, there are some areas in which the regulatory framework could be improved. Many of the shortcomings were previously outlined in the ESRB's letter of 3 February 2020[2], and the review of the AIFMD provides an important opportunity to address these.

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1 Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011 on Alternative Investment Fund Managers and amending Directives 2003/41/EC and 2009/65/EC and Regulations (EC) No 1060/2009 and (EU) No 1095/2010 (OJ L 174, 1.7.2011, p. 1).

2 See letter outlining ESRB considerations regarding the AIFMD, ESRB, 3 February 2020.

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National competent authorities (NCAs) and authorities with a financial stability mandate need to be able to monitor and manage the extent to which the investment fund sector could contribute to systemic risk. The AIFMD has a financial stability objective and provides authorities with a reporting framework to facilitate risk monitoring as well as macroprudential instruments. Where deemed necessary in order to ensure the stability and integrity of the financial system, NCAs can impose leverage limits or other restrictions to limit the extent to which the use of leverage contributes to the build-up of systemic risk in the financial system or risks of disorderly markets. Moreover, in exceptional circumstances NCAs have the possibility to suspend redemptions in the interest of unit-holders or of the public. On all these points, the AIFMD should be improved so that the mandate of the different authorities can be better fulfilled.

The ESRB identified the operationalisation of the existing macroprudential instruments in the AIFMD as a key priority.[3] To this effect, the ESRB made several recommendations to the Commission and the European Securities and Markets Authority (ESMA) in 2017.[4] [5] The importance of having a harmonised operational framework in the EU has increased in the light of the EU's Capital Markets Union initiative, the growing role of the investment fund sector in financial intermediation and the ongoing coronavirus (COVID-19) pandemic. Such a harmonised framework would benefit from the full implementation of the 2017 ESRB Recommendation, including: (i) the development of a common set of liquidity management tools for investment funds across EU jurisdictions, (ii) further setting out the role of NCAs and ESMA when authorities use their power to suspend redemptions, (iii) measures to limit the extent to which the use of liquidity transformation in open-ended alternative investment funds (AIFs) could contribute to systemic risks, and (iv) enhancements of data reporting requirements under both the AIFMD and the Undertakings for Collective Investment in Transferable Securities Directive (UCITSD)[6].

Particularly on UCITS reporting, the ESRB highlighted the need for UCITS and UCITS management companies to regularly report data to competent authorities, especially to better assess liquidity risks and

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3 See Macroprudential policy beyond banking: an ESRB strategy paper, ESRB, July 2016.

4 See Recommendation of the European Systemic Risk Board of 7 December 2017 on liquidity and leverage risks in investment funds (ESRB/2017/6) (OJ C 151, 30.4.2018, p. 1).

5 ESMA has made substantial progress in addressing the ESRB recommendations. It has published Guidelines on liquidity stress testing in UCITS and AIFs conducted a stress simulation exercise for investment funds and published a Final Report on Guidelines related to the operationalisation of the leverage limit under Article 25 of Directive 2011/61/EU.

6 Directive 2009/65/EC of the European Parliament and of the Council of 13 July 2009 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS) (OJ L 302, 17.11.2009, p. 32).

leverage. To allow for effective monitoring of systemic risks, such data would need to be reported on a quarterly basis by a sufficiently relevant proportion of UCITS.

The AIFMD review provides an opportunity to further enhance the reporting framework and operationalise the macroprudential framework for investment funds. In line with the letter sent in February 2020, and reflecting on recent developments in the investment fund sector, this letter provides the ESRB's considerations regarding (i) the suitability of the reporting framework and access to data for monitoring systemic risk, (ii) the need to operationalise existing macroprudential policy instruments, and (iii) the ongoing development of the macroprudential policy framework for investment funds. For each of these three focus areas, Section 1 of the enclosed response provides proposals for amending the AIFMD. For each proposal, the relevant AIFMD (or delegated regulation) articles and the rationale are included. Section 2 provides an overview of which parts of this letter address the various questions in Section IV of the consultation concerning financial stability matters.

We remain available to you and your staff should you wish to discuss any of our proposals.

Yours sincerely,

[SIGNED]

Christine Lagarde

Chair of the European Systemic Risk Board

Encl.

ESRB response to the European Commission consultation on the review of the AIFMD

ESRB response to the European Commission consultation on the review of the AIFMD

1. AIFMD reporting: Outline and rationale for specific proposals

1.1 Suitability of the reporting framework and access to data for monitoring systemic risk

1.1.1 Availability of fund identifiers

Relevant AIFMD provisions

- Directive 2011/61/EU[7] Article 3 – Exemptions
- Directive 2011/61/EU Article 24 – Reporting obligations to competent authorities
- Delegated Regulation (EU) No 231/2013[8] Annex IV – Reporting Templates

Rationale

The availability of unique entity identifiers would substantially enhance financial stability risk monitoring, while entailing few costs for fund managers. First, it would allow authorities to better understand complex fund group structures and interdependencies between funds. Second, because the availability of entity identifiers would facilitate the mapping of investment fund data (AIFMD) with other data sources, such as transaction data under the European Market Infrastructure Regulation (EMIR)[9], the

[7] Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011 on Alternative Investment Fund Managers and amending Directives 2003/41/EC and 2009/65/EC and Regulations (EC) No 1060/2009 and (EU) No 1095/2010 (OJ L 174, 1.7.2011, p. 1).

[8] Commission Delegated Regulation (EU) No 231/2013 of 19 December 2012 supplementing Directive 2011/61/EU of the European Parliament and of the Council with regard to exemptions, general operating conditions, depositaries, leverage, transparency and supervision (OJ L 83, 22.3.2013, p. 1).

[9] Regulation (EU) No 648/2012 of the European Parliament and of the Council of 4 July 2012 on OTC derivatives, central counterparties and trade repositories (OJ L 201, 27.7.2012, p. 1).

Markets in Financial Instruments Directive II (MiFID II)[10]/Markets in Financial Instruments Regulation (MiFIR)[11] and the Securities Financing Transactions Regulation (SFTR)[12], it would improve authorities' ability to assess funds' interconnectedness with other parts of the financial system as well as possible direct and indirect contagion risks. An ESRB analysis of AIFMD data shows that around half of the alternative investment funds (AIFs) do not report or possess a Legal Entity Identifier (LEI). Of the funds that report using derivatives, 25% do not report their LEI, although they would need to do so under EMIR. The costs of obtaining an LEI seem low; e.g. for NL and DE the annual costs would be around €50-60 per LEI. Moreover, the European Securities and Markets Authority (ESMA) indicated that only 16% of fund managers report their LEI in the ESMA Register[13], although most of them are likely to have an LEI under other regulations (EMIR, MiFID II/ MiFIR, SFTR).

Proposal

(A) The Commission should consider requiring all alternative investment fund managers (AIFMs) to acquire and maintain an LEI for themselves and the AIFs they manage. This should apply to all types of AIFM and their AIFs, without exemptions. Article 24(2) could then be amended to include an obligation to report the AIFM LEI and AIF LEIs.

1.1.2 Fund classification

Relevant AIFMD provisions

- Directive 2011/61/EU Article 24 – Reporting obligations to competent authorities
- Delegated Regulation (EU) No 231/2013 Annex IV – Reporting Templates

Rationale

Systemic risk analysis would also benefit from a revised approach to fund classification that better reflects the type of funds registered as AIFs and any applicable regulation (in addition to the AIFMD). The

[10] Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU (OJ L 173, 12.6.2014, p. 349).

[11] Regulation (EU) No 600/2014 of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Regulation (EU) No 648/2012 (OJ L 173, 12.6.2014, p. 84).

[12] Regulation (EU) 2015/2365 of the European Parliament and of the Council of 25 November 2015 on transparency of securities financing transactions and of reuse and amending Regulation (EU) No 648/2012 (OJ L 337, 23.12.2015, p. 1).

[13] https://registers.esma.europa.eu/publication/searchRegister?core=esma_registers_upreg#

fund classification under the AIFMD emphasises hedge funds and their various strategies. Around 60% of aggregate net asset value is, however, classified as "other funds", which comprises mostly equity, fixed income and mixed funds. Better alignment of fund classifications across reporting regimes, such as the ECB investment fund statistics (Regulation ECB/2013/38)[14] would allow for a more effective monitoring of systemic risks. In particular, following the introduction of the AIFMD, the European Long-Term Investment Funds Regulation (Regulation (EU) No 2015/760)[15] and the Money Market Funds Regulation (Regulation (EU) 2017/1131)[16] were adopted. It would be helpful to identify MMFs, European long-term investment funds (ELTIFs), European venture capital funds (EuVECAs) and European social entrepreneurship funds (EuSEFs) that also need to report under the AIFMD. To the extent applicable, and in addition to the above, it would be helpful from a risk monitoring perspective to be able to categorise funds according to applicable national regulations, since such regulations may impact the risk characteristics of funds. Finally, reflecting the growing importance of passive investment structures, managers of AIFs should indicate whether the funds follow active or passive investment strategies.

Proposals

(B) The Commission should consider amending Article 24(2) of Directive 2011/61/EU to allow for the reporting of applicable regulatory regimes. This includes the European Long-Term Investment Funds Regulation (Regulation (EU) 2015/760), the Money Market Funds Regulation (Regulation (EU) 2017/1131), the European Venture Capital Funds Regulation (Regulation (EU) No 345/2013)[17] and the European Social Entrepreneurship Funds Regulation (Regulation (EU) No 346/2013)[18] as well as national regimes. Delegated Regulation (EU) No 231/2013 could then be adjusted accordingly, e.g. by including money market funds (MMFs), ELTIFs, EuVECAs, EuSEFs and national regimes (either as a new category or a subcategory to an existing fund type).

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14 Regulation (EU) No 1073/2013 of the European Central Bank of 18 October 2013 concerning statistics on the assets and liabilities of investment funds (recast) (ECB/2013/38) (OJ L 297, 7.11.2013, p. 73).

15 Regulation (EU) 2015/760 of the European Parliament and of the Council of 29 April 2015 on European long-term investment funds (OJ L 123, 19.5.2015, p. 98).

16 Regulation (EU) 2017/1131 of the European Parliament and of the Council of 14 June 2017 on money market funds (OJ L 169, 30.6.2017, p. 8).

17 Regulation (EU) No 345/2013 of the European Parliament and of the Council of 17 April 2013 on European venture capital funds (OJ L 115, 25.4.2013, p. 1).

18 Regulation (EU) No 346/2013 of the European Parliament and of the Council of 17 April 2013 on European social entrepreneurship funds (OJ L 115, 25.4.2013, p. 18).

(C) The Commission should consider the following fund classification to reduce the large category of "other" funds:

- Funds of funds (sub-categories: funds of hedge funds; funds of private equity funds; funds of equity funds; funds of bond funds; other funds of funds)
- Hedge funds (keep current sub-categories)
- Private equity funds (keep current sub-categories)
- Real estate funds (keep current sub-categories)
- Equity funds
- Bond funds (government / corporate / other)
- Mixed funds (with a focus on: bonds; equity; other)
- Other (sub-categorised into commodity funds; infrastructure funds; pension funds; loan funds; other funds)

(D) The Commission should consider requiring AIFs to report whether a fund follows an active or passive investment strategy.

1.1.3 Fund interconnectedness

Relevant AIFMD provisions

- Directive 2011/61/EU Article 3 – Exemptions
- Directive 2011/61/EU Article 24 – Reporting obligations to competent authorities
- Delegated Regulation (EU) No 231/2013 Annex IV – Reporting Templates

Rationale

More complete information on fund investments and investors would allow authorities to better assess the risk of fire sales or disorderly markets and spillovers to financial institutions. Three areas of the current reporting regime hamper risk detection and could be greatly enhanced at little cost.

- The AIFMD requires fund managers to report information on the main categories of assets in which the AIF is invested, which allows authorities to assess general trends and vulnerabilities. To facilitate monitoring of potential spillovers to other parts of the financial system, the AIFMD requires the reporting of the top five traded instruments, the top ten principal exposures, and the top five portfolio concentrations. There are several drawbacks to using a "top X" approach:
  - (i) Since most funds have highly diversified portfolios, the top five exposures on average cover less than 25% of funds' net asset values. This coverage decreases to 18% for larger funds that have portfolios with net asset values in excess of €1 billion.
  - (ii) Reconciling financial instruments, exposure and concentration is impossible, because of the partial information.
  - (iii) The cost to compute the "top X" instruments/ exposure/ concentration is non-negligible for managers.

  Reporting the whole portfolio would in fact not add much cost. Indeed, the remaining N-X instruments/exposures/concentrations also have to be computed and are therefore available to

managers but not to supervisors. Moreover, around 38% of funds in scope of the AIFMD already report granular security level data for ECB investment fund statistics.
- The AIFMD also requires fund managers to provide information on funds' investment exposure to large regions (e.g. Europe, Asia Pacific). The use of large regions does not allow for the monitoring of cross-border exposures, in particular within the Union. Computing geographical regions is a cost for fund managers and provides little benefit for supervisors.
- The AIFMD also requires fund managers to provide a breakdown (in % of net asset value, NAV) of investor types. There are two drawbacks of the current reporting regime. First, there is no requirement to report the domicile of investors. This lack of geographical breakdown limits the analysis of cross border exposures. Second, some funds are owned by one or only a few institutional investors. The risk profile of these funds differs from funds owned by many investors. Knowing the identity (via the use of the LEI) of the institutional investors would allow for better monitoring of interconnectedness.

More detailed reporting on investments as well as investors may be less costly for fund managers, compared to reporting aggregate statistics. Reporting on a more granular level could make the computation and reporting of certain aggregate statistics (which are based on more granular data) redundant. Reporting more granular data may therefore be less costly for fund managers. This would in particular be the case for funds that already report granular portfolio data to authorities, for instance under the Money Market Funds Regulation, for securities holdings statistics or under the ECB's investment fund statistics framework. Lower-cost data reporting may also allow for an extension of reporting requirements for firms which currently fall under exemptions in Articles 3(3)d and 24(1) of the AIFMD. Many smaller investment funds falling under these exemptions make up a significant portion of the total net asset value in some jurisdictions.

Proposal

(E) The Commission should consider amending the reporting template (Annex IV of Delegated Regulation (EU) No 231/2013) with a view of improving information on funds' interconnectedness, while giving due consideration to minimising fund managers' reporting burden by:

- on the main categories of assets:
  - extending the top 5 main instruments to ALL instruments traded;
  - for physical real estate assets, extending to ALL instruments with three additional fields – country, postcode, property type (residential, industrial, office, retail, other) – while requesting the address to be reported under the existing field "instrument name";
  - including some metrics under Articles 3(3)d and 24(1) which are identified as fundamental from a financial stability monitoring perspective, such as leverage and liquidity measures;
- on the geographical focus:
  - extending geographical focus to country level, in lieu of area level;
- on investor concentration:
  - for AIFs with top five beneficial owners >50% of NAV (existing field), requesting the LEIs of those five owners.

1.1.4 Liquidity

Relevant AIFMD provisions

- Delegated Regulation (EU) No 231/2013 Annex IV – Reporting Templates

Rationale

Some fund managers can use liquidity management tools to manage liquidity risks in funds, but which tools are availability to fund managers is not reported under the current framework. The AIFMD reporting framework requires fund managers to report on the active use of these instruments, but does not require them to report which tools they have at their disposal. The AIFMD reporting shows that less than 3% of funds used liquidity management tools, such as redemption gates, in 2018, which is understandable because these tools are only used in exceptional circumstances. However, since the reporting does not show which tools are available to fund managers and under which conditions, it is difficult for authorities to gauge the possible use of these tools and the implications for financial stability in times of stress.

Fund managers need to report on the alignment of investment and investor liquidity, but there is no harmonised framework for such an assessment of liquidity. The AIFMD reporting provides fund managers' subjective views on the liquidity of their investments and on investors' ability to redeem funds. A harmonised, more objective perspective is not available. For instance, there is no common understanding of how asset managers determine the liquidity profile of portfolios and assign a corresponding liquidation period.

Proposal

(F) The Commission should consider amending the reporting template in Delegated Regulation (EU) No 231/2013 to include:

- for each of the funds managed by the fund manager, an overview of the liquidity tools that the fund manager can apply based on the fund's prospectus – some commonly available tools include redemption fees, redemption gates, redemptions in kind, swing pricing, side pockets, and suspensions of redemptions;[19]
- information on whether the tools are triggered at the discretion of the fund managers, or whether there are automatic (rules-based) triggers and, in the latter case, information on these rules.

[19] It is however noted that in certain EU jurisdictions, commercial companies that are both AIFMs and AIFs can be governed by commercial codes and not national AIFs legislation. It may therefore not be possible to adjust the rules governing unit-redemptions to all the liquidity management tools identified above. As a result, reporting templates may need to be adjusted to such circumstances.

(G) The Commission should consider introducing additional specification on how liquidity profiles should be established and reported and giving ESMA a mandate to develop guidance on the assessment of investment and investor liquidity by fund managers. A harmonised framework for assessing investment and investor liquidity could, for instance, include:

- how fund managers should assess the liquidity profile of assets and assign a corresponding liquidation period – the assessment should take into consideration asset liquidity under stressed market conditions;
- how fund managers should assess investor liquidity, including how to take into account stressed conditions.

1.1.5 Leverage

Relevant AIFMD provisions

- Delegated Regulation (EU) No 231/2013 Annex IV – Reporting Templates

Rationale

Adequate information on leverage and related risks is crucial for the operationalisation of the macroprudential leverage limit. Article 25 of the AIFMD requires authorities to use the information reported under the AIFMD to assess the extent to which the use of leverage contributes to the build-up of systemic risk or disorderly markets. Authorities should then use this assessment to inform decisions on the use of the macroprudential leverage limit.

ESMA has developed a harmonised monitoring framework based on AIFMD data in line with international standards. Following-up on the ESRB's recommendations, ESMA has developed guidance[20] on the operationalisation of the leverage limit. This includes the development of a risk monitoring framework based on AIFMD data, taking into account international guidance from the International Organization of Securities Commissions (IOSCO).[21] [22] The monitoring framework proposed by ESMA includes internationally consistent leverage measures as well as additional risk metrics:

- **Proposed leverage measures** are gross, gross adjusted, net (commitment) and financial leverage, which IOSCO has identified as internationally consistent. These measures can be computed on the basis of the

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20 See Final Report on Guidelines on Article 25 of Directive 2011/61/EU, ESMA, 17 December 2020.

21 See Recommendations for a Framework Assessing Leverage in Investment Funds – Final Report, FR18/2019, IOSCO, December 2019.

22 See ESRB Public Comment on IOSCO Report: Leverage, ESRB, 2019.

existing AIFMD reporting. While these measures provide insight into the level of leverage at the reporting date, they do not provide insight into possible fluctuations between reporting dates. Moreover, the current reporting framework does not include the internal leverage limit set by fund managers, although national competent authorities (NCAs) need to assess whether these limits are reasonable.

- **Proposed risk metrics** include a broad set of indicators to assess the risk of fire sales, spillovers to financial institutions, disruptions in credit intermediation, and market impact. The existing AIFMD reporting framework can be used to compute these metrics, although some improvements could be made:
    - **Potential liquidity demands from market shocks**: NCAs have the discretion to ask fund managers to report additional risk metrics such as value at risk (VaR). Moreover, if VaR is reported, this measure may not be comparable across funds because there is no guidance on the methodology to compute VaR.
    - **Other potential liquidity demands (collateral calls)**: The AIFMD requires fund managers to report their uncollateralised and collateralised borrowings and cash as well as non-cash collateral posted. However, because the data are reported at an aggregated level, the borrowings and collateral information cannot be attributed to specific activities.

Proposals

(H) The Commission should consider amending the reporting template in Delegated Regulation (EU) No 231/2013 to include:

- the internal leverage limit set by fund managers for each of their funds;
- the average leverage over the reporting period for each of the leverage measures;
- indicators for the fluctuation of leverage over the reporting period, such as the minimum and maximum level of leverage for each of the leverage measures;
- a breakdown of collateral posted into variation, initial and excess margin posted, and having these measures reported separately for each activity;[23]
- indicators for the fluctuation of borrowings and collateral over the reporting period, such as the minimum, maximum and average of uncollateralised and collateralised borrowings, and margins posted.

(I) The Commission should consider making the reporting of VaR obligatory in Delegated Regulation (EU) No 231/2013 and harmonising the calculation of VaR between UCITS and AIFs. For instance, this new legislation could state the length of the historical window to base the VaR and include a requirement to

[23] E.g. centrally cleared derivatives, bilaterally cleared derivatives, centrally cleared repurchase agreements (repos), bilaterally cleared repos and triparty repos.

include a stress period. Any new guidance should also pursue the objective of harmonising the calculation of VaR between UCITS and AIFs. Considering the impact on reporting, the Commission might wish to consider giving ESMA a mandate to revise the reporting guidelines accordingly.

1.1.6 CLOs and leveraged loans

Relevant AIFMD provisions

- Delegated Regulation (EU) No 231/2013 Annex IV – Reporting Templates

Rationale

The ESRB has previously highlighted the risks and vulnerabilities emerging from the increase in collateralised loan obligations (CLOs) and leveraged loans in recent years.[24] Ease of accessing debt finance, as indicated by the rise of covenant-lite leveraged loans, increases the likelihood that some borrowers will take on excessive leverage. This increases the risk that highly leveraged borrowers will not be able to fulfil their repayment obligations in the case of an unexpected economic downturn. To help address this, the ECB issued guidelines on leveraged transactions in May 2017 which apply to all significant banks supervised by the ECB under Article 6(4) of the Single Supervisory Mechanism (SSM) Regulation[25].[26] The guidance asks the banks to prepare reports and to define their risk appetite concerning leveraged transactions. It is important to also monitor developments in this market beyond the banking sector, as most financing for leveraged loans is provided by the non-bank sector, where wider sell-offs could trigger rapid contagion to other high-yield markets. UCITS are typically targeted at retail investors and have some limitations on investments in leveraged loans, though restrictions are less stringent for investments in CLOs. In contrast, AIFs are typically targeted at professional investors and have no restrictions on leveraged loan exposures.

The use of common identifiers can help to avoid duplication of reporting obligations existing under other regimes. In addition to reporting of LEIs and international securities identification numbers (ISINs),

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24 See Box 3 in EU Non-bank Financial Intermediation Risk Monitor 2019, No 4, ESRB, July 2019.

25 Council Regulation (EU) No 1024/2013 of 15 October 2013 conferring specific tasks on the European Central Bank concerning policies relating to the prudential supervision of credit institutions (OJ L 287, 29.10.2013, p. 63).

26 See Guidance on leveraged transactions, ECB, May 2017.

the unique securitisation identifier developed under Article 11 of Delegated Regulation (EU) 2020/1224[27] is also particularly relevant. There are already detailed disclosure requirements for CLOs under the Securitisation Regulation[28]. Reporting is already compulsory and will be available once the first securitisation repository is registered. However, non-EU CLOs may not necessarily be captured by these reporting requirements.

Proposals

(J) The Commission should consider developing consistent definitions and regular reporting requirements for leveraged loans, including the identification of covenant-lite leveraged loans, to facilitate the regular monitoring of risks and vulnerabilities in the sector. Such harmonising requirements for loan-originating AIFs would allow more effective monitoring of credit intermediation activities by AIFs.

(K) The Commission should consider extending existing securitisation disclosure requirements to non-EU CLO and collateralised debt obligations (CDOs). In addition, a separate CLO category could be considered as opposed to the current reporting regime, where CLOs and CDOs are grouped together.

1.1.7 *Reporting frequency*

Relevant AIFMD provisions

- Directive 2011/61/EU Article 24 – Reporting obligations to competent authorities
- Delegated Regulation (EU) No 231/2013 Annex IV – Reporting Templates

Rationale

From a financial stability perspective, the low and differentiated frequency of reporting as well as the long time lag between collection and provision of the data can hinder the timely monitoring of risks. The existing reporting framework aims to be proportional by differentiating the reporting frequency based on fund size and type. As a result, fund managers may have to report at different frequencies for the various funds they manage. Harmonising the reporting frequency at a quarterly interval would benefit financial stability monitoring and may also be less cumbersome for fund managers who otherwise need to report at

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27 Commission Delegated Regulation (EU) 2020/1224 of 16 October 2019 supplementing Regulation (EU) 2017/2402 of the European Parliament and of the Council with regard to regulatory technical standards specifying the information and the details of a securitisation to be made available by the originator, sponsor and SSPE (OJ L 289, 3.9.2020, p. 1).

28 Regulation (EU) 2017/2402 of the European Parliament and of the Council of 12 December 2017 laying down a general framework for securitisation and creating a specific framework for simple, transparent and standardised securitisation, and amending Directives 2009/65/EC, 2009/138/EC and 2011/61/EU and Regulations (EC) No 1060/2009 and (EU) No 648/2012 (OJ L 347, 28.12.2017, p. 35).

different intervals for each of their funds. Reducing the time between the collection and provision of the data would also be beneficial.

To facilitate timely monitoring of risks in stressed conditions, a harmonised and concise set of indicators could be defined, which authorities could request at a high frequency. Article 24(5) of the AIFMD allows authorities to request additional information from fund managers to facilitate financial risk monitoring on an ad hoc basis. Especially in crisis scenarios, authorities require up-to-date and high-frequency data to monitor risks and to inform policy decisions. These data should be harmonised and easily accessible to all relevant authorities, allowing timely action by and coordination among authorities. The quarterly (or lower frequency) AIFMD data are not sufficient to assess financial stability risks in times of stress. During recent market events, authorities relied heavily on market data and market intelligence to gain insights into risk developments. While these are valuable sources of information, market data tend to cover fewer funds and may be of lower quality than regulatory data. Authorities may therefore benefit from the development of an “ad hoc data template” which contains a concise minimum set of metrics that authorities would need in crisis scenarios. These metrics may be a selection of data fields already reported under the current AIFMD framework, possibly complemented by some additional information items. By establishing an “ad hoc data template”, both authorities and fund managers could anticipate and prepare for the eventuality of these data needing to be reported in exceptional circumstances.

Proposal

(L) The Commission should consider establishing a reporting of high-frequency information to authorities in crisis scenarios. This information could include:

- A baseline reporting template that includes a minimum set of indicators that would be relevant in stress scenarios, taking into account differences in fund type where relevant, and that could be taken from the AIFMD reporting regime as much as possible. This would ease the implementation, as it allows the IT infrastructure already in place to be re-used. Different stakeholders should be consulted on the content and operational aspects of this specific reporting so that a set of principles (e.g. when to put in place this reporting, how frequent it should be) and parameters (which data) are determined. By way of example, the following information would be valuable under stress (non-exhaustive):
  - AIF assets under management (AUM)
  - NAV
  - Fund flows (inflows and outflows)
  - Investor type and domicile in terms of NAV
  - Leverage metrics
  - Liquidity metrics (e.g. cash buffers, borrowings, margins, portfolio liquidity)
  - Any sponsorship linkages, guarantees, committed credit lines
  - Use of liquidity management tools by the fund
  - Breakdown of collateral posted into variation, initial, and excess margin reported separately for each activity as suggested in the footnote in Section 1.1.5, Proposal H

ESMA's proposed risk monitoring framework for the operationalisation of Article 25 of Directive 2011/61/EU may provide inspiration for specific indicators.

- A governance framework by which authorities could coordinate ad hoc information requests in crisis scenarios and share information with other authorities. Such a framework should also take into account how to manage potential signalling effects.

1.1.8 Access to data

Relevant AIFMD provisions

- Directive 2011/61/EU Article 53 – Exchange of information relating to the potential systemic consequences of AIFM activity

Rationale

Recent events in the context of the COVID-19 crisis highlighted that not all relevant authorities have access to AIFMD data, which hampers the ability of these authorities to carry out their financial stability mandate. Moreover, the absence of access to AIFMD data also hinders the cooperation and coordination of policy responses between supervisors, authorities with a financial stability mandate, and central banks. Henceforth, all relevant ESRB member institutions with responsibilities in the area of financial stability should be able to access relevant datasets. This includes cross-border data to ensure that authorities supervising the end-investors have access to the necessary information.

Proposal

(M) The Commission should consider amending Article 53 of Directive 2011/61/EU to facilitate data sharing by NCAs to ensure that all relevant ESRB member institutions with responsibilities in the area of financial stability have access to relevant AIFMD data, including the high-frequency information reported to authorities in crisis scenarios (see Section 1.1.7, Proposal L). The modalities of how to share the data between these institutions would need to be worked out. Relevant ESRB members include:

- The ESRB
- The European Central Bank (ECB)
- The Single Resolution Board (SRB)
- The European Supervisory Authorities (ESAs)
- National central banks (NCBs)
- National macroprudential authorities

1.2 Operationalising existing policy instruments to address the contribution of AIFs to systemic risk

1.2.1 The availability of liquidity management tools for fund managers

Rationale

Fund managers are the first line of defence in managing liquidity risk in funds. Recently, several investment funds faced severe liquidity issues due to the COVID-19 crisis, with some funds having to use exceptional measures to cope with large outflows. Quantity-based measures, such as suspension of redemptions and redemption gates, were activated by a small number of funds in response to the large outflows. Other funds used price-based measures, such as swing pricing and redemption fees, to ensure that trading costs were borne by redeeming investors. In most Member States fund managers are solely responsible for the activation of liquidity management tools – regulators play only a minor role in the process and cannot activate tools, except for suspension of redemptions in the interest of the public. It is therefore important that fund managers face no legal impediments in national law that would prevent them from having the full range of liquidity management tools at their disposal. Moreover, since fund managers are bound by the prospectus of the funds they manage, fund managers should be required to include the potential use of liquidity management tools in their prospectus.

Proposal

(N) Please refer to the ESRB recommendation (ESRB/2017/6) proposing that Union legislation incorporates a common Union legal framework governing the inclusion of additional liquidity management tools in the design of investment funds regulated under both the AIFMD and UCITS Directive.

1.2.2 The use of suspension of redemptions by authorities

Relevant AIFMD provisions

- Directive 2011/61/EU Article 46(2)(j) – Powers of competent authorities
- Directive 2011/61/EU Article 47 – Powers and competences of ESMA
- Directive 2011/61/EU Chapter VI – Rights of EU AIFMDs to market and manage EU AIFs in the Union
- Directive 2011/61/EU Chapter VII – Specific rules in relation to third countries
- Delegated Regulation (EU) No 231/2013

Rationale

The power to suspend redemptions provides authorities with an (ex post) crisis management instrument to halt runs in exceptional circumstances. The broad-based sale of assets to meet investor redemptions or margin calls may contribute to systemic risk through increased risk of fire sales, direct spillovers to other financial institutions, and disruption of credit intermediation. By requiring fund managers to suspend redemptions in exceptional market conditions, authorities would be able to effectively halt investor runs that may contribute to financial stability risks.[29] While fund managers themselves would be able to suspend redemptions, they are mandated to act in the interest of investors, which may not be fully aligned with the public interest and financial stability, and may therefore be subject to inaction bias. Moreover, fund managers lack the necessary information to monitor possible avenues for contagion with other funds, and could overlook the financial stability implications of selling assets or applying liquidity management tools. Hence, there is a need for authorities to have the mandate to suspend redemption in the public interest. For this mandate to be effective, authorities would need clear (yet flexible) guidance on how to operationalise this instrument. In the absence of guidance, authorities may be hesitant to act when needed because of reputational and legal risks.

The AIFMD provides NCAs with the power to suspend redemptions in the public interest, but further guidance is needed on how to operationalise this instrument. The ESRB has recommended that the Commission clarifies NCAs' role when using their powers to suspend redemptions in situations where there are cross-border financial stability implications, as well as ESMA's general facilitating, advisory and coordination role.[30] Coordination among authorities – across EU Member States as well as with third countries – would be particularly relevant in cases where the fund manager is located in a different jurisdiction than the funds it manages or the markets it invests in. In these circumstances, the financial stability implications of broad-based runs may be felt in jurisdictions other than the jurisdiction of the competent authority of the fund manager that can order the suspension of redemptions. Moreover, since fund managers can easily relocate their fund business, a coordinated approach is needed to mitigate the risk of regulatory arbitrage, and to minimise the risk of cross-border spillovers. In this regard, further consideration should be given to the possible need for reciprocation.

Proposals

In line with the ESRB's recommendations, the Commission should consider:

(O) clarifying competent authorities' power to suspend redemptions in the public interest in Directive 2011/61/EU by:

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[29] See Macroprudential liquidity tools for investment funds – A preliminary discussion, *Macroprudential Bulletin*, Issue 11, ECB, October 2018.

[30] See Recommendation of the European Systemic Risk Board of 7 December 2017 on liquidity and leverage risks in investment funds (ESRB/2017/6) (OJ C 151, 30.4.2018, p. 1), Recommendations A(2) and A(3).

I. clarifying the objective suspension of redemptions in the public interest by:
   i. separating competent authorities' power (*Article 46(2)(j) of Directive 2011/61/EU*) to suspend redemptions in the interest of the public from their power to suspend redemptions in the interest of the shareholder, thereby acknowledging that these tools have different objectives;
   ii. clarifying that competent authorities may consider the suspension of redemptions of a fund or group of funds in the interest of the public under exceptional circumstances, including, but not limited to, scenarios in which broad-based redemptions from a fund or group of funds, on their own account or in interaction with other parts of the financial system, contribute to the build-up of systemic risk in the financial system or risks of disorderly markets;
   iii. including provisions that the Commission will adopt, by means of delegated acts, measures setting out principles specifying the circumstances in which competent authorities could consider applying suspension of redemptions in the interest of the public;

II. clarifying the respective roles of NCAs, and cooperation between them and in interaction with third countries, with regard to suspension of redemptions with cross-border financial stability implications, in line with the scenarios and provisions laid down in:
   - *Chapter VI of Directive 2011/61/EU*, governing scenarios where there could be differences in the location of the AIFM and the location of the AIF within the EU, and
   - *Chapter VII of Directive 2011/61/EU*, governing interaction with third countries, such as cases where EU AIFMs manage or market funds in third countries, or conversely, when non-EU AIFMs manage or market funds in the EU;

   and including provisions specifying:
   i. which authorities can initiate a (reciprocation) request for the relevant competent authority to suspend redemptions for a fund or group of funds;
   ii. an obligation for competent authorities to notify other relevant NCAs (including macroprudential authorities), ESMA and the ESRB prior to exercising the power to suspend redemptions in the public interest;

III. setting out ESMA's general facilitation, advisory and coordination role in relation to NCAs' powers to suspend redemptions where there are cross-border financial stability implications.

   To facilitate this with respect to cooperation with third countries, Article 47(4)(b) and Article 47(4)(c) could be generalised, in accordance with Article 47(5), to allow ESMA to impose restrictions on non-EU AIFMs in relation to the management of an AIF in cases where there are risks of (i) fire sales, (ii) direct spillovers to financial institutions, (iii) disruptions in credit intermediation that could pose a risk to the orderly functioning and integrity of the financial market or financial stability.

(P) developing delegated acts that lay down guiding principles specifying the circumstances in which competent authorities apply suspension of redemptions in the interest of the public under Delegated Regulation (EU) No 231/2013.

I. Similar to the provisions laid down in Delegated Regulation (EU) No 231/2013 for the imposition of leverage limits (Article 112), the Commission might wish to consider formulating guiding principles along the following lines:
When considering the use of suspension of redemptions to mitigate the risk that redemptions from a fund or group of funds, on their own account or in interaction with other parts of the financial system, could contribute to the build-up of systemic risk in the financial system or risks of disorderly markets, competent authorities shall take into account at least the following aspects in their assessment:
   - the extent to which redemptions could contribute to forced sale of assets which may dislocate prices and reduce liquidity in financial markets (fire sales channel);
   - the extent to which redemptions could result in direct losses to other parts of the financial system that are substantial enough to disrupt financial intermediation (direct spillovers to counterparties);
   - the extent to which redemptions could contribute to constrained funding conditions for financial and or non-financial entities (disruption in credit intermediation);
   - the proportionality of the use of the instrument in relation to the risks to be mitigated, including an assessment of potential unintended consequences of using the instrument (both domestic and cross-border);
   - the potential need for coordinated action with other authorities (e.g. other NCAs, ESMA, the ESRB), including the need for reciprocation.

1.2.3 *Leverage limit*

Relevant AIFMD provisions

- Directive 2011/61/EU Article 25 – Use of information by competent authorities, supervisory cooperation, and limits to leverage
- Directive 2011/61/EU Article 47 – Powers and competences of ESMA
- Directive 2011/61/EU Chapter VI – Rights of EU AIFMDs to market and manage EU AIFs in the Union
- Directive 2011/61/EU Chapter VII – Specific rules in relation to third countries
- Delegated Regulation (EU) No 231/2013 Article 112

Rationale

The AIFMD provides authorities with a macroprudential instrument to limit the extent to which leverage in funds can contribute to the build-up of systemic risk. Excessive leverage in the financial system contributes to the build-up of systemic risk that may materialise via fire sales, direct negative spillovers to financial institutions and reductions in financial intermediation. The use of leverage by investment funds may also contribute to systemic risk, even at low levels when combined with other structural vulnerabilities, such as short-term redemptions and liquidity mismatches. Since fund managers do not internalise the potential costs that their strategic actions impose on the financial system, there is a role for macroprudential authorities to monitor risks associated with leverage and consider imposing leverage measures or other restrictions in the interest of financial stability.

Further guidance by ESMA will help authorities to operationalise the macroprudential leverage limit. In order to facilitate authorities' assessment of the risks associated with leverage and the need to implement measures, ESMA has been recommended by the ESRB[31] to (i) develop a harmonised framework for the assessment of financial stability risks stemming from the use of leverage, (ii) provide guidance on the design, calibration and implementation of a macroprudential leverage limit, (iii) issue guidance on the notification process, and (iv) benchmark practices by NCAs to ensure a harmonised approach across the EU. In response to this recommendation, ESMA has drafted Guidelines on Article 25 of Directive 2011/61/EU.[32] With respect to the design, calibration, and implementation, the ESRB has recommended that leverage limits are based on the leverage measures provided by the AIFMD. This would ensure a consistent application of the instrument within the EU and enhance transparency. A regular review of the measures – via the AIFMD review process – would ensure consistency with international standards. In this regard, the leverage measures in the AIFMD are consistent with the measures currently considered by IOSCO, pending the adjustment proposed by ESMA.[33]

Proposals

To further facilitate the operationalisation of the leverage limit, in line with the ESRB's Recommendations and with ESMA Guidelines, the Commission should consider:

(Q) including provisions in Article 25 of Directive 2011/61/EU to clarify that leverage limits are to be based on the leverage measures set out in Directive 2011/61/EU, while allowing for flexible interpretation of the use of "other restrictions";

(R) clarifying the respective roles of NCAs and cooperation between them and in interaction with thirds countries (via ESMA) with regard to their power to impose leverage limits when there are cross border financial stability implications in line with the scenarios and provisions laid down in:

[31] See Recommendation ESRB/2017/6, op. cit., Recommendation E.

[32] See Final Report: Guidelines on Article 25 of Directive 2011/61/EU, ESMA, December 2020.

[33] See item 6 of the Letter on the review of the AIFMD, ESMA, 18 August 2020.

- *Chapter VI of Directive 2011/61/EU*, governing scenarios where there could be differences between the location of the AIFM and the location of its AIFs within the EU;
- *Chapter VII of Directive 2011/61/EU*, governing interaction with third countries, such as in cases where EU AIFMs manage or market funds in third countries or, conversely, when non-EU AIFMs manage or market funds in the EU;

including provisions specifying which authorities can initiate a (reciprocation) request for the relevant competent authority to consider leverage limits for a fund or group of funds.

1.3 The ongoing development of the macroprudential policy framework "beyond banking" and for investment funds in particular

Relevant AIFMD provisions

- Directive 2011/61/EU Article 69 – Review

Rationale

The development of the European macroprudential framework for investment funds – and non-banks more generally – is still at an early stage. Ultimately, the macroprudential framework "beyond banking" should facilitate the beneficial role of non-bank financial intermediation as a valuable alternative to bank finance, while at the same time ensuring resilience by mitigating risks related to leverage, liquidity and maturity mismatches, procyclicality and contagion.

Further reflection on the adequacy of the macroprudential framework is warranted. The current regulatory framework relies strongly on the use of liquidity management tools by fund managers. While fund managers form an important first line of defence in managing liquidity risk, the actions by fund managers may not always be sufficient to maintain financial stability during crisis events. While authorities could use suspension of redemptions in exceptional circumstances to stop outflows, this ex post instrument may have unintended consequences. For instance, the market turmoil at the onset of the COVID-19 pandemic made it clear that suspension of redemptions could limit the ability of firms and other financial institutions to raise liquidity at precisely the time when they needed cash the most. It may therefore be worthwhile exploring whether authorities should be able to guide the use of other liquidity management tools by funds. This would be in line with the recommendation made by the Financial Stability Board (FSB) in 2017 that authorities should consider assuming a macroprudential role in providing direction on the use of liquidity risk management tools by funds in extraordinary circumstances. Moreover, alongside such ex post instruments, it would be worthwhile, from a macroprudential perspective, to further assess policy options allowing authorities to mitigate the build-up of structural vulnerabilities in funds.[34] The COVID-19 crisis has shown that some investment funds entered the recent stress episode with a significant liquidity mismatch and difficulties in accommodating outflows. In this regard, the FSB recommended, for instance, that authorities outline requirements for the alignment of funds' assets and investment strategies with redemption terms.

Work is ongoing at the European level with the aim of developing the macroprudential framework for investment funds. Going forward this work could benefit greatly from the lessons learned from the COVID-19 crisis. At the same time, it should be acknowledged that the investment fund sector is very heterogeneous and that different stress scenarios may require different responses. Given the need to reflect further on all these issues, there would be a need to review the adequacy of the macroprudential framework in the AIFMD in a subsequent review process.

Proposal

(S) The Commission should consider including provisions in Directive 2011/61/EU to allow for the regular review of the macroprudential framework for AIFs, e.g. by extending Article 69 to include a review of the macroprudential toolbox and governing framework for AIFs. The review should allow for an assessment of existing tools (Articles 25 and 46(2)(j)) and the need for possible additional instruments. In doing so, developments in international standards should be considered.

[34] See, for example, Carney, M., "Addressing the Growing Challenges in the International Monetary and Financial System", Bank of England, 18 October 2019; and de Guindos, L., "Macroprudential policy ten years after the crisis", keynote speech at the CIRSF Annual International Conference 2019 "Financial Supervision and Financial Stability Ten Years after the Crisis: Achievements and Next Steps", Lisbon, 4 July 2019.

2. List of AIFMD consultation questions and cross-references to ESRB response

Consultation question	ESRB response section
Question 56. Should the AIFMD framework be further enhanced for more effectively addressing macroprudential concerns?	1.3
Question 57. Is there a need to clarify in the AIFMD that the NCAs’ right to require the suspension of the issue, repurchase or redemption of units in the public interest includes financial stability reasons?	1.2.1, 1.2.2
Question 58. Which data fields should be included in a template for NCAs to report relevant and timely data to ESMA during the period of the stressed market conditions?	1.1.7, 1.1.4
Question 59. Should AIFMs be required to report to the relevant supervisory authorities when they activate liquidity risk management tools?	1.2.1, 1.2.2
Question 60. Should the AIFMD rules on remuneration be adjusted to provide for the de minimis thresholds?	N/A
Question 61. Are the supervisory reporting requirements as provided in the AIFMD and AIFMR’s Annex IV appropriate?	1.1.1 - 1.1.7
Question 62. Should the AIFMR supervisory reporting template provide a more comprehensive portfolio breakdown?	1.1.3
Question 63. Should the identification of an AIF with a LEI identifier be mandatory?	1.1.1
Question 64. Should the identification of an AIFM with a LEI identifier be mandatory?	1.1.1
Question 65. Should the use of an LEI identifier for the purposes of identifying the counterparties and issuers of securities in an AIF’s portfolio be mandatory for the Annex IV reporting of AIFMR?	1.1.1
Question 66. Does the reporting data adequately cover activities of loan originating AIFs?	1.1.2
Question 67. Should the supervisory reporting by AIFMs be submitted to a single central authority?	1.1.8
Question 68. Should access to the AIFMD supervisory reporting data be granted to other relevant national and/or EU institutions with responsibilities in the area of financial stability?	1.1.8
Question 69. Does the AIFMR template effectively capture links between financial institutions?	1.1.3
Question 70. Should the fund classification under the AIFMR supervisory reporting template be improved to better identify the type of AIF?	1.1.2
Question 71. What additional data fields should be added to the AIFMR supervisory reporting template to improve capturing risks to financial stability?	1.1.1 - 1.1.7

Question 72. What additional data fields should be added to the AIFMR supervisory reporting template to better capture AIF's exposure to leveraged loans and CLO market?	1.1.6
Question 73. Should any data fields be deleted from the AIFMR supervisory reporting template?	1.1.3
Question 74. Is the reporting frequency of the data required under Annex IV of the AIFMR appropriate?	1.1.7
Question 75. Which data fields should be included in a template requiring AIFMs to provide ad hoc information in accordance with Article 24(5) of the AIFMD during the period of the stressed market in a harmonised and proportionate way?	1.1.7
Question 76. Should supervisory reporting for UCITS funds be introduced?	Cover letter, page 2
Question 77. Should the supervisory reporting requirements for UCITS and AIFs be harmonised?	Cover letter, page 2
Question 78. Should the formats and definitions be harmonised with other reporting regimes (e.g. for derivatives and repos, that the AIF could report using a straightforward transformation of the data that they already have to report under EMIR or SFTR)?	1.1.2
Question 79. Are the leverage calculation methods – gross and commitment – as provided in AIFMR appropriate?	1.1.5
Question 80. Should the leverage calculation methods for UCITS and AIFs be harmonised?	1.1.5
Question 81. What is your assessment of the two-step approach as suggested by International Organisation of Securities Commissions ('IOSCO') in the Framework Assessing Leverage in Investment Funds published in December 2019 to collect data on the asset by asset class to assess leverage in AIFs?	1.2.3
Question 82. Should the leverage calculation metrics be harmonised at EU level?	1.1.5
Question 83. What additional measures may be required given the reported increase in CLO and leveraged loans in the financial system and the risks those may present to macro-prudential stability?	1.1.6
Question 84. Are the current AIFMD rules permitting NCAs to cap the use of leverage appropriate?	1.2.3
Question 85. Should the requirements for loan originating AIFs be harmonised at EU level?	1.1.6