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Consultation response

FSB Public Consultation

Consultation on Leverage in Non-Bank Financial Intermediation)

28 February 2025

General comments

- Macro-level risk monitoring akin to the BoE's SWES is an important complement to risk management conducted by firms.
- Agree that authorities should ensure they have suitable and sufficient information to identify and monitor risks related to e.g. NBFI leverage.
- Where information gaps are identified in authorities' capabilities to monitor these macro-risks, NBFIs themselves should provide the information, not their intermediaries.
- Banks already face comprehensive risk management frameworks, with new CCR guidelines due to be implemented at national level. Where authorities believe gaps still remain in terms of the information/data banks receive from NBFI counterparties, focus should fall on NBFIs' disclosure - not additional requirements on banks.
- The FSB should clearly define the scope of firms intended to be captured under its proposals. NBFIs are a diverse set of market participants, with different business models and very different risk profiles. Measures that may be appropriate for some NBFIs would not be appropriate for others. In some cases, NBFIs are already subject to comprehensive regulation (e.g. Solvency UK/II on insurers and IFR/IFPR which covers proprietary trading companies (investment firms), both EU and UK) in certain jurisdictions. Rather than reopening that regulatory framework, the FSB should focus on international consistency of existing frameworks.
- NBFIs conducting activities resulting in equivalent levels of risk as banks should be subject to equivalent regulation.
- Care should be taken to exclude firms which do not use leverage (e.g. MMFs, non-leveraged pension funds and investment funds) from the proposals outlined in this consultation paper. In refining the scope or definition of NBFI, policy measures should be appropriately focused on the types of NBFI that have a significant contribution to systemic risk. We would highlight the recent speech given by Andrew Bailey in which he notes three dominant non-bank business models that have created potential vulnerabilities to financial stability, including the growing market share of non-bank market makers and associated shift in market dynamics..
- Market making in certain asset classes is now dominated by non-bank liquidity providers, which have a very different risk profile to other investment firms and funds. Regulatory treatment of Non-Bank Market Makers should reflect their growing position within markets and increased contribution to systemic risk. We would note the role of market-making as an economic function of critical importance with an impact on the real economy. Non-bank market makers are typically active across multiple markets, and we would highlight that the withdrawal/failure of a firm in one market has the potential to cause instability across all asset classes.

Recommendation 1

Authorities should have a domestic framework to identify and monitor vulnerabilities related to NBFI leverage and associated financial stability risks in an effective, frequent and timely manner. The domestic framework should be proportionate to the financial stability risks that such vulnerabilities may pose, particularly in core financial markets. Authorities should regularly review their domestic framework and enhance it as appropriate, including the risk metrics utilised, and take steps to improve international consistency in the definition and calculation of those metrics.

Question 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?

NBFIs play a vital role in financial stability, allowing risk to be distributed throughout the financial sector rather than focussed within banks' balance sheets. This is a welcome development that reduces the risks of institutions remaining "too big to fail", as seen during the financial crisis of 2007-08. In particular, post-crisis leverage constraints have reduced banks' capacity to provide funding or market making services and facilitated a dominance of several non-bank market makers, we would note that disruption and risk stemming from market-making activities would likely lead to the disruption of significant markets with a potential impact on financial stability. Consequently, we would suggest that market-making is a critical function on its own merit, and the identification of it as such would address existing gaps within the regulatory framework and address potential vulnerabilities within the NBFI sector.

Any measures that introduce frictions in NBFI markets should be weighed against the broader costs to the market in liquidity, diversification and capital for investment.

Depending on the measure, around 50% of total assets in financial markets are held by NBFI, and in some major jurisdictions more than 50% of lending to the commercial sector is provided by market-based finance. NBFI rely for their financing partially on banks. The financial system and the core financial system therefore displays a large degree of interconnectedness and displays a number of channels that can pose a risk to financial stability. The description of risks presented in the FSB report is comprehensive, however, as past financial crisis has shown contagion risk and network instability can arise from sources that might not have been identified previously and might remain unknown until they materialise. Having said that we would like to highlight the following risk channels as relevant from an industry perspective:

1. Spillover of default(s)
2. Price downward spiral
3. Loss of provision of critical services
4. Link to systemic institutions
    a. Micro links: idiosyncratic and institution specific
    b. Macro links: system-specific
5. Connectedness with banks
    a. Counterparty credit risk
    b. Margining

6. Crowded strategies / lack of diversification

While we identify the aforementioned risks and vulnerabilities as relevant and agree with the FSB analysis, we would like to emphasise that the response functions to mitigate identified risks and vulnerabilities are multi-facetted. A target-oriented calibration of these response functions and their individual components is key to an efficient policy response. Our suggestions to the consultation questions reflect our considerations in that respect.

The Industry would like to point out that in particular in the business of market making banks' presence in market making has been curtailed by post-crisis regulation and capital requirements, leaving a natural vacuum for non-bank liquidity providers. Market making in certain asset classes is now dominated by non-bank liquidity providers (e.g. non-banks in ESMA list of market makers and primary dealers[1]). The risk profile and contribution to systemic risk between these types of market makers and other types of investment firms is very different, and we believe that the level of granularity within existing regulation insufficiently addresses this. In light of recent crises, we would highlight the role that market-making plays as an economic function of critical importance and impact on the real economy. Non-bank market makers are typically active across multiple markets, and we would highlight that the withdrawal/failure of a firm in one market has the potential to cause instability across all asset classes[2].

Question 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?

The global financial crisis highlighted significant vulnerabilities in both derivatives (synthetic leverage) and repo (financial leverage) markets that can spill over to broader financial markets. Since then, the activity-level data available to authorities on **derivatives and securities financing transactions** (including repos) has been greatly enhanced.

The most effective risk metrics are

- High-frequency transaction data: By using comprehensive information on **daily transactions and trade depositories**, this activity-level data help authorities obtain more timely and comprehensive insights into these markets, helping them to develop policy responses that address financial stability risks.
- Combining entity-level and activity-level data: To measure and identify leverage risks appropriately, and understand the use of NBFI leverage and assess its implications for financial

1 https://www.esma.europa.eu/sites/default/files/library/list_of_market_makers_and_primary_dealers.pdf

2 See: IOSCO publishes results of examination of ETF behaviour during COVID-19 induced market stresses - "a subset of ETFs temporarily experienced unusual trading behaviours"; in times of stress. ETFs trade far more frequently than their component bonds; Bond ETFs suck liquidity out of market in a crisis, academics say (ft.com))

stability, **merging entity-level data from the Alternative Investment Fund Managers Directive (AIFMD with transaction-level data for derivatives and SFTs is considered effective**.

The information mentioned above is already available to authorities and allows authorities to develop a framework for flexibly analysing a range of risk scenarios.

An example of data availability and useability of data for supervisory analysis can be found, among others, in ESMA's ex-post analysis of derivatives risks in Archegos[3].

Question 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**
(ii) specific types of entities, such as **hedge funds, other leveraged investment funds, insurance companies and pension funds**
(iii) concentration and **crowded trading strategies**

Ad i) High-frequency transaction data (activity-based), in particular, transaction-level data for derivatives and SFTs; trade depositories and CCP data

Ad ii) entity-level data from the Alternative Investment Fund Managers Directive (AIFMD); banking regulation data, especially large exposure and supervisory data on CCR, including qualitative information

Ad iii) stress test techniques with 2nd round effects on system-wide level

Recommendation 3

Authorities should review the level of granularity, frequency, and timeliness of existing public disclosures and determine the degree to which additional or enhanced disclosures should be provided to the public, either by (i) authorities, including disclosure based on regulatory reporting data, (ii) the relevant financial market infrastructure providers or (iii) directly by financial entities, balancing the costs and benefits of doing so. This includes dissemination by authorities of data and information on aggregate market positioning and transaction volumes based on existing regulatory reporting. Such additional or enhanced disclosures should be designed and calibrated to increase transparency especially about concentration risk and crowdedness, with the aim to support market participants' ability to manage risks from NBFI leverage and estimate counterparty exposures and liquidation costs.

Question 4. What types of **publicly disclosed information** (e.g. transaction volumes, outstanding amounts, aggregated regulatory data) are useful for market participants to enhance

[3] https://www.esma.europa.eu/press-news/esma-news/esma-publishes-ex-post-analysis-derivatives-risks-in-archegos

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?

While the Industry acknowledges the usefulness of public disclosure or market transparency and enhancing market discipline, we would encourage policy makers to clearly define the purpose of NBFI disclosure requirements. Following on from that, we would welcome a "least cost" assessment, i.e. an analysis of how the goals can be achieved at the least possible costs to market participants, incl. banks, NBFI, the wider investor base and policy makers. This should also be weighed against the expected marginal benefits to authorities of having access to this additional data. In practice, this can mean that before introducing any new disclosure requirements, policy makers assess which information is already publicly available and whether it serves the disclosure purpose.

Any arrangements between NBFI supervisors and bank supervisors would provide benefits for supervisors considering the final output would be enriched. However, it should be noted that to the extent that exercises are already carried out by banks, it is key to avoid overburdening banks with duplicating/ additional information requirements.

Moreover, the Bank of England's SWES exercise highlighted the value of qualitative information in helping understand how firms will act in a crisis vs the type of information that can be garnered from reported data alone. We agree with this assessment and would encourage regulators and supervisors considering tailored one-off exercises as sources of information.

Before considering additional reporting requirements, authorities should assess the effectiveness of current reporting regimes and avoid creating reporting duplications. Simplified reporting procedures could also increase transferability of data between authorities.

Therefore, the priority for policymakers and regulators should be:

- identification of data gaps around the NBFI sector
- exploration of appropriate data sharing arrangements between different regulatory/ national authorities based on existing reporting channels across the banking/ non-banking sectors
- avoidance of new data collection requirements on banks – instead banking supervisors should have access to relevant market transaction data
- appropriate investment in their data analysis capabilities

On maximising existing data sources, by way of example:

- most data about derivatives, risk exposures and counterparties, although complex and not readily functional, is currently available to EU regulators and supervisors either through trade repositories or supervisory/regulatory reporting[4]. If used and shared appropriately among EU regulators and supervisors, this would enable a better understanding and limit the reporting burden on market participants.

[4] https://www.isda.org/2023/10/10/hidden-in-plain-sight-derivatives-exposures-regulatory-transparency-and-trade-repositories/

- in the EU Total Return Swaps (TRS) are within the scope of Securities Financing Transaction (SFT) Regulation (SFTR). A similar practice applied globally might have reduced the opacity around the exposures of a family office such as Archegos in March 2021. EU. On leverage, the case of so called "hidden leverage" might be considered as mitigated in the EU as many reporting requirements have been set in place the over the last decade (e.g. AIFMD/ Annex 4 on counterparty reporting).

- MiFiD/R requires firms in scope to report transaction data to supervisors .

- In relation to AIFMD reporting requirements, firms already report on leverage in terms of overall fund positions and by principal counterparty under Annex 4.

- Banks report a vast amount of counterparty information, credit risk – incl. large exposures, liquidity and market risk data and leverage information on a granular and regular basis to supervisors and regulators.

Many NBFIs are already subject to aforementioned data requirements. If data requirements were to be extended, focus should be on relevant NBFI's that aren't yet in scope.

In terms of information to be made publicly available, we would also recommend aligning with the current regulatory and supervisory stance regarding existing information. The same holds for frequency. In any case policy makers need to strike the balance between public disclosure for more transparency and counterparty credit risk management and the risk for amplifying shocks in periods of stress.

Recommendation 4:

Authorities should take steps to address the financial stability risks from NBFI leverage that they identify in core financial markets. Activity-based and entity-based measures and measures aimed at addressing concentration that amplifies risks related to NBFI leverage, should be reviewed periodically and enhanced where appropriate, including to address risks from a system wide perspective. The measures should be selected and calibrated to be effective and proportionate to the identified financial stability risks. Where existing legal and regulatory frameworks do not provide the necessary policy measures to address identified financial stability risks, authorities should consider adjusting or widening the scope of such frameworks, where appropriate.

Recommendation 5

When selecting policy measures to address financial stability risks from NBFI leverage in core financial markets, authorities should evaluate a wide range of measures, including both activity and entity-based measures, as well as concentration related measures. Authorities' choice of measures should be based on the nature and drivers of identified risks, taking into account their expected effectiveness and any potential costs or unintended consequences, as well as measures taken in other jurisdictions to address similar risks. Activity-based measures include (i) minimum haircuts in SFTs, including government bond repos, (ii) enhanced margining requirements between non-bank financial

entities and their derivatives counterparties, and (iii) central clearing mandates in SFT and derivatives markets. Entity-based measures include (i) direct limits on leverage, and (ii) indirect leverage constraints linked to risks that non-bank financial entities are exposed to. Concentration measures include (i) concentration add-ons for margins and haircuts in connection with exposures of non-bank financial entities in derivatives and SFT markets, (ii) concentration and large exposure limits, and (iii) large position reporting requirements.

Question 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?

Activity -based regulation are wide-spread (e.g. clearing, haircuts, margins) and constrains individual activities directly and on a standalone basis; and entity-based regulation can constrain a single or combination of activities at the entity level. The widespread adoption of entity-based regulation reflects the fact that excessive leverage and liquidity transformation, which lie at the core of financial instability, involve combinations of activities.

The choice between activity -based and entity-based regulation depends on where financial instability originates. Activity-based regulation is justified where authorities seek to ensure that the market in which risk associated with an activity is taking place– for example, a derivative transaction or a repo trade - is appropriately reflected by market participants, thereby influencing the cost of that activity and market behavior. Rules apply to all entities conducting that activity regardless of the risk profile of individual entities. Entity based regulation is justified where a risk can become disorderly or dysfunctional be attributed to a single or group of entities. The application of leverage limits for real estate investment funds in some markets or yield buffers on LDI funds are examples of this.

Activity-based measures can increase consistency when calibrated well. A nuanced calibration is particularly important to ensure that sets of activity-based measures interact effectively with each other. However, activity-based measures can have the potential to create an unlevel-playing field when they are inconsistently and/or incoherently constructed as firms have different capacities to absorb the costs.

In the past, the FSB has brought forward activity-based measures like minimum haircuts for SFT that due to their structural features and operational complexity have not been adopted in any major jurisdiction. In contrast, banks' internal risk management has advanced significantly to sufficiently capture any idiosyncratic risks stemming from lending and/or liquidity activities with NBFIs. The materialisation of systematic risks (e.g. "dash for cash", LDI crisis) in core markets over the last years might indicate that broader measures are required to address system-wide leverage and concentration.

We believe that alongside a consideration of the risks taken on by NBFIs, the FSB and national authorities should recognise the role of the banking prudential framework as a corollary to growing NBFI activity in certain markets. In some cases, banking regulation has had inadvertent consequences on market functioning, by making it more difficult for banks to act. For example, the Federal Reserve

took emergency action[5] to disapply the supplementary leverage ratio from US Treasuries, as it was preventing banks from intermediating in the market during the "dash for cash" episode in March/April 2020. The FSB should reconsider measures that are inadvertently displacing activities from banks to NBFIs, with a view to optimising liquidity in the market as well as distribution of risk across different market participants.

We do not believe though that the issues observed can be addressed with new or adapted activity-based measures alone as they may burden firms that are already in scope of far-reaching capital (e.g. counterparty credit risk), liquidity (LCR, NFSR) and structural constraints (leverage ratio) and hence would constitute double counting in the side of banks, and might introduce inefficiencies for counterparties and clients. We suggest therefore the combination of traditional activity-based measures with entity-based measures.

It is also noted that both entity- as well as activity-based measures can have a procyclical effect and lead to accelerated contagion in the system. Supervisory awareness and reactiveness in times of stress is needed to avoid any unintended consequences from measures as proven by various stress events in the past (e.g. relaxing of prudential valuation requirements in the EU in the beginning of Covid-19).

Question 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?

As an overarching principle, before looking to use activity-based measures, authorities should consider whether the proposed measure would give rise to arbitrage opportunities or market distortions. Failure to do so could result in the provision of the targeted activities being pushed into less regulated segments of the market.

Minimum haircuts

The BCBS minimum haircut rule for SFTs based on the FSB guidance has not been implemented in any major jurisdiction which hints at a problem with its construction. Given the complexity and its central role, we do not believe that a blunt tool such as the minimum haircut rule is appropriate to address financial stability risks unless the design is fundamentally enhanced. This is ultimately reflected in the decision taken by the major jurisdictions that have an active and vibrant SFT market that it would not be appropriate for jurisdictions to consider its adoption for the purposes of mitigating risks arising from NBFI leverage.

Minimum haircut floors for SFTs pose a number of challenges that would undermine the use of collateral as a tool for risk mitigation that provides significant benefits to financial stability. Implementation of a minimum haircut floors framework would adversely affect important financial markets, such as repo markets and securities borrowing and lending markets. Securities borrowing and securities lending enhance market liquidity and improve price

[5] https://www.federalreserve.gov/newsevents/pressreleases/bcreg20200401a.htm

discovery, important for a number of market participants beyond the scope of this paper. Increasing charges on securities financing transactions may have the effect of pushing these transactions outside of the traditional banking sector altogether, which would have the opposite of the intended effect and result in increased leverage. In this context the industry would point to previous advocacy outlining the concerns around the minimum haircut requirement as implemented by BCBS[6], highlighting the need for a very careful consideration of any unintended consequences.

Enhanced margin requirements

Margin requirements are a standard tool in risk management and widely used across market activities and counterparties. The key issue here would be the how the enhancement would look like given that margin requirements are inherently procyclical and could amplify a downward price spiral as well as lead to contagion across the financial system. Rather than introducing new measures in relation to margin requirements, authorities should focus on implementing the policy proposals coming out of the global work on margin practices led by BCBS-CPMI and IOSCO, both for centrally and non-centrally cleared markets. Given the risk of regulatory arbitrage, we would therefore encourage policy makers to pursue consistency in margining across different entities, so that margin requirements are set according to the risk of the product/market, not the contracting entity.

Regulators should amend rules on collateral so that they: i) take a holistic, and systemic, approach to the regulation of collateral, and of activities requiring collateral; ii) are consistent across different types of activity, and across different types of market participant; and iii) ensure that market participants can pool collateral. One example would be to allow central counterparties to diversify where they can hold collateral rather than restrict them to posting collateral with central security depositories.

Central clearing

Central clearing appears – by and large – an effective tool to preserve liquidity in the market. However, the problem with central clearing lies in providing the capacity for clearing especially for government bonds. Unless it can be ensured that the capacity is provided under severe stress, central clearing might lead to the unintended effect of becoming a bottle neck in times of crisis. In the context of capacity it is crucial to ensure that capital requirements are such that banks are not disincentivised to engage and offer. Mandated central clearing services. can also raise costs for participants (through clearing fund contributions, clearing fees, excess margin etc.) This could cause certain investors and firms to withdraw from markets subject to central clearing, further exacerbating illiquidity.

The appropriateness of centrally-mandated clearing depends on the type of instrument in question. In the case of government bond repo, the case study of the UST mandate shows that such mandates can be highly complex to implement. It is too early to draw conclusions from the

[6] Please see GFMA's response to the technical amendments to the BCBS Minimum Haircut Floors for Securities Financing Transactions

UST experience, in particular the implications for market liquidity and investors are still unclear and it would be premature to roll out in other markets.

In the case of broader mandates on more/all SFTs, design and implementation would become even more challenging since common and appropriate definitions would need to be agreed. In addition, where expansions of central clearing mandates are proposed for derivatives, it would be important for authorities to ensure that only appropriately liquid products are subject to the mandate. Lastly as mentioned above, it is also important to create sufficient capacity for the market to absorb a greater scope of cleared activity.

Question 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?

If activity-based measures or enhanced measures were considered, a dynamic approach might exacerbate procyclicality. Therefore, it is essential that while dynamic approaches provide an adjustment mechanism to increase market requirements in response to heightened volatility, policy makers, would need to consider unintended consequences as a result of procyclical effects that may increase financial stability risks.

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

n/a

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

Margin requirements are a well-established tool and already widely used across the Industry. The implementation costs would therefore be contained. Minimum haircut requirements have been proven to be fundamentally flawed in their construction and hence not adopted in any major jurisdiction. The industry does not believe a blunt tool such as the minimum haircut rule is appropriate to address the concerns around leverage in NBFI.

Question 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 make clear our understanding of entity specific measures that they are a tool that could be applied to a specific entity or group of entities in response to an identified risk. The consultation paper cites examples of structural limits for real estate funds that have been applied in some countries, entity level constraints on leverage, yield buffers in response to the LDI crisis and constrains on UCITS funds. All of these measures have in common their targeted nature and focus on an articulated risk. We do not interpret entity specific measures as referring to the application of a broader set of measures to an NBFI's entire business model, for example the porting of some, or all of the banking prudential framework. We would consider this as an inappropriate and insufficiently targeted intervention that would have multiple shortcomings.

We would also strongly discourage any measures where banks are expected to police NBFIs. Direct measures such as leverage caps on NBFIs should be applied directly and not through prime brokers as this would add unnecessary complexity and be impractical since prime brokers do not necessarily have full sight of their NBFI counterparty's portfolio to be able to apply those caps. As such, if leverage limits are to be applied, they should be applied at source on the NBFI. In contrast, indirect measures like yield buffers provide a more flexible framework.

We believe that structural measures like a leverage ratio/cap that is selectively applied to highly leveraged NBFIs that are exhibiting risks could be an effective tool, assuming it is not risk weighted. This has the advantage that is can be applied in a targeted manner to entities or groups of entities that exhibit specific risks. We would expect a clear process to be established around the application of any new leverage caps. ESMA's guidelines on how competent authorities should use the tools available under Article 25 of the AIFMD are a good example of such process as it involves a multiple stage process consisting of 1) identifying entities that pose risks to the financial system 2) evaluating the leverage related risks of entities identified in the first step and 3) applying leverage limits that are calibrated depending on the risk profile of the entity, e.g. if the risk is associated with a specific entity or a common exposure. ESMA has developed metrics and criteria to inform each step thereby ensuring consistent approaches.

Question 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?

Entity specific measures should only be applied where they respond to a clearly identified risk that poses a risk to financial stability. It should only apply to individual entities or groups of entities that pose a risk to financial stability, and be based on a risk-based scoping should be employed, e.g. systemically relevant NBFIs. Many highly regulated European asset managers are already subject to leverage limits in EU regulation (e.g. AIFMD) and it seems unlikely, therefore, that they would be subject to additional entity level restrictions except in the most extreme scenarios.

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

A thorough assessment of the design of entity-based and activity-based measures is crucial for understanding how effective they are in containing leverage-related risks. For instance, a system-wide leverage ratio might limit liquidity in times of stress. Unsymmetrically calibrated leverage ratios across market participants might affect the level playing field.

Question 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 believe that activity-based measures, when correctly calibrated, can be a useful way of improving resilience in particular markets across all participants. These can then be complemented by specific expectations on the small population of systemically important NBFIs.

Recommendation 6

Authorities should ensure the timely and thorough implementation of the BCBS's guidelines on counterparty credit risk which represents an important element of a comprehensive policy response to financial stability risks stemming from NBFI leverage. Authorities, in cooperation with SSBs, should monitor, including from a systemic perspective, ongoing and future developments in the way NBFI leverage is provided to ensure that the regulatory framework remains appropriate for the consistent treatment of risks.

Question 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 believe that there are existing counterparty credit risk guidelines that already address counterparty credit risk management on a global as well as on regional level.

- The BCBS Guidelines on Counterparty Risk Management were adopted in December 2024. The FSB should allow authorities time to implement the recently finalised BCBS CCR guidelines (including on disclosures) before creating further requirements on banks in this space.
- In Europe the EC have published the DA 2023/2779 which supports the consistent identification of shadow banking entities which are well embedded and underlying firm's counterparty credit risk management;
- The ECB has published a series of articles[7] in which the supervisor sets out their approach to monitoring NBFI counterparty risk and leverage in the system in particular.

Recommendation 7

Authorities, in cooperation with SSBs, should review the adequacy of existing private disclosure practices between leveraged non-bank financial entities and leverage providers, including the level of granularity, frequency, and timeliness of such practices. Where appropriate, they should consider developing mechanisms and/or minimum standards to enhance the effectiveness of these disclosure practices.

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?

A minimum set of disclosures would be helpful in setting leverage users' expectations of the information that a leverage provider will require of them. Presently, the quality and depth of disclosures can vary depending on the nature of the counterparty and the various constraints that they are operating within, including the legal framework. The heterogeneity of firms and

[7] Complex exposures to private equity and credit funds require sophisticated risk management; Strengthening risk monitoring and policy for non-bank leverage

underlying requirements means that it will be very difficult to standardise disclosures. However, creating a common set of disclosures that are seen as best practice would set expectations and help improve the quality and consistency of information that leverage providers receive.

It would also be helpful to promote common definitions, for example, different measures are used to calculate leverage and it would be helpful to have a consistent definition used by market participants.

The BCBS guidelines for CCR management provide a useful basis for information disclosure standards. Hereby, the guidelines mention that effective due diligence processes rely upon sound information disclosures, whereby banks should establish a risk-based disclosure framework taking into account the counterparty sector and risk profile of the counterparty, as well as an exceptions management process. In particular relevant to this consultation the BCBS guidelines refer to risky and complex counterparties such as hedge funds should provide additional disclosures and risk metrics – such as value-at-risk or stress test results – so that banks have visibility into the counterparty's own assessment of their underlying leverage and risk profile. The focus of the FSB workstream should be to promote consistency in the disclosure and presentation of this information.

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?

To avoid this risk, it may make sense to set out best practice disclosures that can be tailored to different types of entity, rather than a minimum set of disclosures that may not be appropriate for the full diversity of participants in scope.

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?

As mentioned under question 16, we believe that best practices for disclosure might be more effective than minimum standards.

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?

It might be useful for leverage users to provide enhanced disclosure where the information. We would emphasise that the information should always be shared and readily available. In that way leverage providers can plan their responses and actions should a stress situation arise and establish, for example, appropriate early warning systems and management information systems including internal limit setting and managerial actions.

We would also like to reference here the BCBS guideline for CCR management. The information requirements imposed on leverage providers should be equally applied to leverage users.

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?

The NBFI ecosystem comprises a wide range of entities performing different economic functions. This includes significant differences across entities in the level of leverage as well as the complexity in how leverage is obtained and used. In such a complex set-up, a cross industry-working group might present the best opportunity to gather best practices and represents the best way to create efficient policies with added-value for public authorities and the industry alike. An industry-based approach also increased the level of acceptance of any such practices and would allow policy makers to gain valuable insights in the practical aspects of the business and as well as risk management practices.

Recommendation 8

Authorities should adopt the principle of "same risk, same regulatory treatment" and identify incongruences in the regulatory treatment of NBFI leverage resulting from similar exposures, financial instruments or structures that may distort incentives and result in regulatory arbitrage. Where incongruences are identified, authorities, in cooperation with SSBs, should analyse the underlying causes to determine whether and how to address the identified incongruences, having regard to the treatment of similar situations in other jurisdictions, so that domestic remediation efforts do not create new disparities that could transfer risk across borders.

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 would emphasize that NBFIs are also part of the global financing landscape and to some extent their growth in certain segments of market activities that were typically the preserve of banks is the flipside to increasing levels of post-crisis bank regulation and capital requirements. This is particularly true in the context of the EU Capital Markets Union, where NBFIs provide a source of

diversification and alternative funding for the real economy. As such, it is important that regulation considers the extent to which risks have migrated from banks to NBFIs and how best to manage these risks. However, the range of products and services provided by NBFIs is vast: many are distinct and entirely dissimilar to conventional banking services and as such the regulatory approach to managing any risks arising from them would likely be different to that taken for banking risks. Therefore, we believe that the regulators should avoid a one-size-fits all approach to the potential design/ implementation of future regulatory initiatives – instead we think the focus should be on identifying and managing the risks arising from specific types of products and services provided by the NBFI sector, and the specific entities that are providing them.

About GFMA:

The GFMA represents the common interests of the world's leading financial and capital market participants, to provide a collective voice on matters that support global capital markets. We advocate on policies to address risks that have no borders, regional market developments that impact global capital markets, and policies that promote efficient cross-border capital flows, benefiting broader global economic growth. The Global Financial Markets Association ("GFMA") brings together three of the world's leading financial trade associations to address the increasingly important global regulatory agenda and to promote coordinated advocacy efforts. The Association for Financial Markets in Europe ("AFME") in London, Brussels and Frankfurt, the Asia Securities Industry & Financial Markets Association ("ASIFMA") in Hong Kong and Singapore, and the Securities Industry and Financial Markets Association ("SIFMA") in New York and Washington are, respectively, the European, Asian and North American members of GFMA.

Contact details:

Caroline Liesegang (AFME)
Managing Director, Capital and Risk Management
Caroline.liesegang@afme.eu
Direct: +44 (0)20 3828 2719