Amundi
ASSET MANAGEMENT

Amundi's response to FSB's consultative document on Proposed Policy Recommendations to Address Structural Vulnerabilities from Asset Management Activities

(September 21, 2016)

Amundi is thankful to FSB for this opportunity to express its views on topics that are so vital in our industry, notably liquidity and leverage as factors of risk for investor and financial stability. We would first like to recall that Amundi is the largest European and non US asset manager with more than 1 trillion € under management. We offer a diversified range of investment solutions designed to serve the needs of a great variety of clients, more than 100 million retail and thousands of institutional.

We would summarize our key messages in answering the present consultation as follows, presented in the order of the consultation and not of priority :

- We are recognizant that FSB has now better taken stock of the originality and specificities of our industry; to be clear, asset managers do not carry large balance sheets but act as agents for client investors who bear the market risks and pay a commission for our work ;
- We believe that FSB should give a global mandate to IOSCO and not limit it to some and not all the recommendations ;
- We stress that management of liquidity risk and of market risk (including the impact of leverage) are within the core business of an asset manager and have been for decades now ;
- We further underline that the EU has implemented a series of rules that in our opinion strongly limit the possibility of a risk for financial stability; we would encourage authorities to consider this corpus as a fair example of efficient ruling ;
- More specifically about liquidity risk, we regret that the present consultation does not go into the key relationship between valuation and liquidity: illiquidity appears when the investor considers that the price is not fair and it is particularly true when stressed market conditions prompt potential buyers to hope discounted prices; we suggest that FSB include the examination of the link between liquidity and valuation (so determinant in the first mover's advantage) in its mandate to IOSCO ;
- Liquidity management tools are efficient if we provide flexibility in their choice and use ; furthermore they should be easy to introduce in the prospectus of a CIS through a specific up-date with general information; we believe that their activation relies with the Board or

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the asset manager and that tools that keep some character of exceptionality should be used after information of the NCA ;

- Stress tests should not be too prescriptive, as they represent a risk management tool which is better calibrated by the asset manager at the level of the fund. There is a risk of herding in a “one size fits all” approach that could threat financial stability ;
- With regard to leverage, Amundi considers that the EU framework designed under UCITS and AIFM directives is far ahead of what is made in many other jurisdictions that follow balance sheet leverage only. The commitment method has been deep-proofed and some of its limitations have been addressed through the use of risk based measures like VaR, knowing that a relative VaR is an approximation of a leverage compared to the reference portfolio. We believe it to be a sound framework build over years in a pragmatic way and we expect international recommendations to validate it ;
- We are not sure that the aggregation of leverage of individual funds will be an easy task for authorities and we suggest that they focus on the very few funds that present a high leverage (that excludes in the EU UCITS and AIFS which do not use substantial leverage.
- Our general view about operational risk is that it is not critical when it comes for investors to transfer assets from one asset manager to another. We consider that there is operational risk in our activity but reject the conjectures that size is a factor (indeed we believe that a boutique may have lower risk control and recovery procedures) and that it may amount to a risk for financial stability. We however consider that a proper analysis of operational risk and a measurement of its possible impact based on historical data is a good way to proceed; we reckon that it is part of the risk assessment for banks and insist that the calibration for asset management must be totally different ;
- The question of indemnification provided by agent lenders provides an opportunity to express a strong belief: asset managers should not engage in activities that are usually conducted by banks and other prudentially regulated entities; the only route should be for them to set up a subsidiary that will be licensed and prudentially regulated. It is a matter of level playing field on the one hand and of investor protection on the other hand to stick to the pure agency model of asset management and avoid ancillary banking activities that carry balance sheet risk. The same applies for other activities like providing a guarantee to clients, intermediation or market making...

We now turn to the answer to the specific question of the consultative document.

Q1. Does this consultative document adequately identify the structural vulnerabilities associated with asset management activities that may pose risks to financial stability? Are there additional structural vulnerabilities associated with asset management activities that the FSB should address? If there are any, please identify them, as well as any potential recommendations for the FSB’s consideration.

Directly or through its professional associations, Amundi has participated over the last years to many consultations conducted by FSB, IOSCO and other regional and national entities on the asset management industry. We are very satisfied and grateful that the successive papers evidence a **far better understanding of the specificities of asset management.** When the first suggestions were to promote a regulation for funds and asset managers (AM) very similar to the banking regulation, we now see that the trend towards more relevant and appropriate measures taking stock of the reality of the industry is well established and we consider it as a very positive evolution. Just to make it clear once again, asset managers are not banks, they act as agents for the investors who entrust them with their money, pay a fee and carry the risks of the investments.

We agree that the main two factors to consider when assessing financial stability risk in the area of asset management are **liquidity and leverage as rightly** stated by FSB. We further agree that the focus on operational risk should not be abandoned and in our view it should not be limited to large complex entities but it should apply to all entities in a proportionate manner. In a small hedge fund boutique the consequences of an operational anomaly may have far more important consequences than in a large entity, where the quality of the procedures and the control of their observance might often be better organized. In any case the ability of any fund manager to be able to face the consequences of an operational failure should be examined at the level of the firm or the group and not the fund or portfolio. For operational risk linked to the use of larger platforms exceeding the limits of a group the adequate perimeter should be that served by the platform, be it dedicated to credit, risk or intermediation.

With regard to the other 3 areas mentioned by FSB, we agree that **sovereign funds** is an issue of sovereignty: they should not be exempt from regulation if we want to avoid them to take risks without limits. They are large in size, regulated through their internal rules under their own self-designated governance and can potentially present a risk for financial stability and create unleveled playing field and distortion of competition. They should not be allowed to compete with regulated entities. We support FSB's initiative to take sovereign wealth funds on board when considering global risk and see in Annex 2 a good contribution to the debate. We consider that the question when it comes to supervising pension funds is less political as there is no direct issue of sovereignty. We suggest that investor protection's rules very similar to those applying to CIS funds should be implemented.

Amundi will further express below its surprise to see FSB consider that the transfer of its assets by an investor from an Asset manager to another might be difficult and could generate specific risk. It is in our view a very standard decision that implies a minimum of agreement on the terms and delays but which does not create difficulties, even in stressed market conditions. As far as securities lending activities by asset managers are concerned, Amundi is very supportive of the idea that indemnification or guarantees if they are provided by asset managers should be **prudentially regulated in a way comparable to what applies to banks who carry that type of activities**. This remark is not limited to the SFT area but should apply more generally on all activities that are traditional banking activities and impact the balance sheet.

Q2. Do the proposed policy recommendations in the document adequately address the structural vulnerabilities identified? Are there alternative or additional approaches to risk mitigation (including existing regulatory or other mitigants) that the FSB should consider to address financial stability risks from structural vulnerabilities associated with asset management activities? If so, please describe them and explain how they address the risks. Are they likely to be adequate in stressed market conditions and, if so, how?

Amundi thinks that the high level recommendations issued by FSB in this document are sensible, but do not sufficiently take stock of the diversity of funds and client investors. The overarching principle should be put at the beginning that a **"one size fits all" approach is not what is**

intended by FSB. A proportionate and differentiated approach is the only way to develop an effective regulation.

Our first comment is to stress more clearly than done by FSB the **high level of efficiency of the regulatory framework existing in the European Union**. Both for liquidity and leverage, there are strict constrains in the UCITS and AIFM directives. For example, assets eligible in UCITS must be liquid, leverage is limited to 200% and liquidity stress testing is specifically foreseen in AIFMD. We feel that FSB should ask IOSCO to conduct a gap analysis in order to focus on grey areas where there could remain risk and avoid duplicating or changing efficient regulation.

There are two major risk mitigants when we discuss about liquidity that should not be disregarded. The first one is the **promoter's support**. Amundi believes that in many instances the intervention, limited in time and in size, of the promoter, manufacturer or distributor, of a fund may be a very appropriate tool. Typically, the distributor may have reasons to believe that a future subscription could come in a near future and would compensate a redemption: its decision to carry the position for a couple of days (with the possibility to hedge the exposure on its own balance sheet) would undoubtedly be to the benefit of investors. The limits must be clearly established and respected so as to not give way to "step in risk". The risk associated to this investment by the promoter must also be prudentially accounted for. The second one is the possibility to **exchange units directly between investors** outside the official redemption and subscription process. It allows for transactions to take place without respect of the official NAV and allows for a fair assessment of the price of liquidity of a portfolio at a given time. It is a market price resulting from the confrontation of offer and demand where 2 parties agree to trade and transfer future risks. If the promoter should not be obliged to organize such a secondary market it should not be prevented to do it and should make sure that the documentation and information available to investors is adequate.

Our following comment is to stress the **interconnection between liquidity and valuation issues**. The case of first mover's advantage is essentially an issue of fair valuation. The example of CNAV MMFs is the only one where this issue is of real importance and it is the only case in the fund industry where there might be a gap between official price and market valuation. When funds are distributed as funds and not as deposit like instruments, investors understand that the price may move and the valuation process is established to obtain a fair price. Tools like ADL or swing pricing do, also, evidence the link between valuation and liquidity concerns. We would like FSB to ask IOSCO to undertake specific research on this link with the help of the industry.

We further believe that the tools available for liquidity management should be further analysed and classified to better assess their efficiency in different types of circumstances and their appropriateness to different types of clients. We suggest that all of the 26 tools referenced in the December 2015 report published by IOSCO be given a definition (even if the document confesses that at least 3 of them have never been implemented) in order to develop cross discussions on best practices that could be copied in different jurisdictions. FSB should give a clear mandate to IOSCO to carry this work.

Concerning leverage, Amundi has a clear view that FSB should **focus on those funds where real leverage can be produced**. In other words such funds as UCITS should be out of scope as they must under the EU directive limit their net exposure to 200% of their capital. The same applies for AIFs that do not use extensive leverage, where the ratio is limited to 300%. Hedge funds and their relationship with their prime brokers (that usually refuse proper asset segregation of the funds in their books and through the custody chain) is the place to concentrate on. Furthermore, UCITS are prevented from any re-use and cannot create leverage through collateral or SFTs, and we work on a limited and calibrated relaxation of this requirement to facilitate central clearing of derivatives traded by UCITS.

Lastly, we fear that the energy developed by FSB on the issue of **transferring mandates** or client accounts even in stressed market conditions is misplaced. The production of a recommendation in that respect is **probably unnecessary**. In our view it relies on an inaccurate view of the organization of the relationship between the entity that gives the mandate, the entity that holds the corresponding account in its books and the asset manager. Each of those entities, including the client investor, should have predefined procedures to ensure a smooth process and if there are technical issues that may create delays they might be at any level. Apparently the security law that prevails in continental Europe is highly protective for the investor and could diminish the level of operational risk on such a transfer. Further assessment of the reality of risks should be undertaken before producing a recommendation that would be better designed. However, we do agree that business continuity planning is to be recommended.

Q3. In your view, are there any practical difficulties or unintended consequences that may be associated with implementing the proposed policy recommendations, either within a jurisdiction or across jurisdictions? If there are any, please identify the recommendation(s) and explain the challenges as well as potential ways to address the challenges and promote implementation within a jurisdiction or across jurisdictions.

The key concern with implementation of the recommendations is to maintain a **level playing field**. In order to reach that objective, there should be a strong coordination and a real harmonization of rules throughout the world. Asset management is more and more an international industry and the current globalization could lead to regulatory arbitrage. We would like to avoid it and urge authorities to concentrate on it. At first sight there is a grey area about ancillary activities of asset managers and we feel it should be fixed: activities that can be conducted by an asset manager or a prudentially regulated entity should be submitted to the same level of regulation. For example, a credit or a guarantee, even if included in a comfort letter, offered by an asset manager in a jurisdiction where it is possible should be subject to the same capital requirements as if they were granted by a bank. For operational risk also we do not deny the rationale for a minimum capital requirement at the level of the asset manager, provided that the calibration is representative of the asset manager’s activities. That type of regulation can only succeed if applied worldwide and simultaneously.

The recommendations proposed by FSB will have as a direct consequence new **reporting** requirements both to authorities and to the public. Over the last years, asset managers have suffered a heavy burden of reporting : each new regulation incorporated its own reporting requirement and they proved difficult to implement. The first reason is the lack of transversal view that leads to slightly different fields for very comparable information. The second reason was the divergence of methodology for producing and collecting reporting (directly, through intermediaries, through delegation, to a TR or to the NCA…). The third reason was the discrepancies in the reporting obligation and architecture between different countries (double reporting, single or double sided reporting, exact scope,...). The fourth reason was a result of the lack of time to implement the regulation and make the IT developments that could only begin when the authorities had determined what they expected. The fifth reason was that for some time authorities were not always able to use reported data and to issue recommendations for improvements needed. In a nutshell, our experience in the field of reporting is that it is not an ancillary activity it is very much in the center of the project management and a long delay should be granted to conduct broad consultations with market participants and to develop a coordinated and consistent view among authorities to avoid very costly developments for specific needs. Amundi strongly support IOSCO's suggestion in the statement of its board regarding data gaps in the AM industry (June 2016) to use internationally agreed standards such as LEI or UTI (and UPI) and to foster the development of centralized data hubs. Lastly about reporting, we insist on the stringent distinction that must be made between what is produced for the authorities and can be subject to confidentiality and what is of interest for the public. For instance, we believe that results of stress tests of the funds should not be made available to the public as they may easily be misinterpreted and create unnecessary stress that would act as a catalyst for systemic risk.

More specifically, we are not comfortable with **recommendations 9** that foresees a system wide stress testing and 13 dealing with operational risk. On stress tests, we believe that they are meaningful at the level of the basic entity, which is the fund in the AM industry. We can agree that a family of funds is also significant. But stress testing at the level of the asset manager, the industry or the entire system as foreseen in recommendation 9 is not workable and will suppose so many shortcuts and hypotheses that it will not show anything. The variety of investment strategies and the multiplicity of clients types in our industry is a key factor for stabilization and should not be overlooked. Furthermore, if we agree with **recommendation 6** on stress tests applied to funds, we nevertheless ask regulators not to be too prescriptive in their guidance : the asset manager is best positioned to properly calibrate the stress test and share the results with the NCA. With **recommendation 13**, we do not agree that operational risk is only an issue for larger firms. Contrary to banking and insurance industries, size is not a criterion in the asset management. And when it comes to operational risks the level of sophistication of procedures and embedded controls is usually growing with size. Thus we believe that if there should be a proportionality with the size it is inverse proportionality leading to a focus on smaller firms.

Q4. In your view, is the scope of the proposed recommendations on open-ended fund liquidity mismatch appropriate? Should any additional types of funds be covered? Should the proposed recommendations be tailored in any way for ETFs?

Amundi suggests that the analysis of the liquidity issue in CIS should include a much larger focus on the **micro view of the investor**. Funds pledge to grant their holders a possibility to cash their investment at market price and with reasonable delay. By design, a CIS offers to the investor a higher liquidity level than a direct investment, be it only because of the existence of cash cushion or the possibility to cover redemptions by new subscriptions. There are at least 2 different rationales for investors to ask for redemption and we think they should be examined separately. On the one hand, the investor wishes to arbitrage his or her holdings and move from one particular asset class to another or within the same asset class to change portfolio manager. In that case, there is no alternative but for the fund to produce cash in a timely manner according to the prospectus and redeem the investor. Conversely, when the investor is satisfied with his or her investment and keen to keep it, he or she may nevertheless need cash to face unplanned expenses for example. In that hypothesis, the investor has to choose from his investments those she or he would most easily be able to cash and open ended funds are obviously among the easiest choices to implement. But, there are alternative solutions. The investor could take a loan at good conditions since there are assets to pledge as a guarantee. We feel that Lombard credit should be developed and encouraged as it is an efficient way to conciliate long term investment and short term financial needs. In our opinion, there is a strong pedagogic impact in this approach and investors would more easily accept restricted liquidity in their investments if they were sure to be able to borrow up to 50%, for example, of their assets rapidly and at a good rate. Furthermore, we think that platforms where clients could trade CIS at a price that might diverge from the official NAV could soon develop. We consider them as a supplementary source of liquidity that should not be disregarded if they offer a minimum of investor protection rules.

Coming back to the liquidity of the funds and supposing that the investor has confirmed his or her will to redeem, we would like to challenge a few assertions that we read in the consultation paper §2.1.

- First, we think that FSB should be more specific and make it clear that there has been no historical evidence of financial stability concerns with funds except for CNAV MMFs. These funds' conception is fundamentally dangerous as the **CNAV funds are traded at a price that is not the market value of the assets**. They should not be called funds as they are sold as deposit like instruments and negate in their marketing the fundamental evidence that a fund takes risks to produce a return so that unit holders are subject to market risk and potential drop in the market value of their fund. We urge authorities to be more drastic about the CNAV MMFs.
- Second, we consider that, except for CNAV MMFs, the **first mover advantage is not a liquidity but a valuation issue**; if the NAV is calculated on the basis of prices on which the fund manager can trade the assets there is no incentive to exit first from a fund; that result can be achieved through different means including ADL or swing pricing.
- If FSB could notice a larger involvement of funds in the financial intermediation of US corporate bonds, we feel that it is not to be considered as good news; Amundi has a strong belief that **asset management is one specific talent and that trading bonds is a different activity**; we do not deny that bond portfolio managers may express an interest in such or such bond but we do not like the suggestion that the market liquidity for corporate bonds could rely on funds and fund managers; we do not feel that trading and investment exactly coincide and want to stick to what investors except from us: investment.

Otherwise, Amundi agrees with FSB's analysis of the ways fund managers mitigate the liquidity risk and the challenges that the activation of certain tools create. However, we experience that **cross transactions** between funds run by the same asset manager seem to be standard practice in some jurisdictions and are very difficult to implement in others and we would suggest some harmonisation in that respect. We would like to repeat that liquidity management is part of portfolio management and has always been. Asset managers are used to adapt the liquidity profile of a fund to the environment and to anticipate trends. Historical data show that accidents have only occurred on hedge funds and CNAV MMFs. Nevertheless, we agree that liquidity cannot be guaranteed in stressed conditions. The most responsible approach in that respect is to **teach investors** that liquidity risk exist and that he or she may suffer it in some extreme circumstances. The presentation of multiple liquidity management tools, some of which consisting in transferring the liquidity problem to the investor, is an opportunity to educate subscribers.

Amundi suggests that FSB take stock of the existence of non-liquid asset classes like infrastructures, long term loans, real estate, unlisted securities… that are not subject to temporary liquidity mismatches but to **structural illiquidity**. Those assets are rarely offered through open ended funds, but should be considered separately if they are. It is clear that some investors, even individuals, are keen to gain the liquidity premium that these instruments offer.

With regard to ETFs, the liquidity issue is managed by market makers who trade them and are the link between the investors and the funds. They are contractually engaged vis à vis the ETF manager to provide quotes for quantity and they subscribe or redeem in kind. The market makers may adapt their prices, to a limited extent, around the underlying instant NAV of the fund and that flexibility is another reason for ETFs' liquidity even in stressed circumstances. The question raised by regulators about ETFs is that of the accessibility of redemption in cash by investors directly without having to trade through a market maker. The case the regulators were worried about was the absence of liquidity due to a withdrawal of market makers that stop trading because of market instability. This is an extreme case and if it happens the ETF would under EU rules become comparable to other standard CIS. Consequently, **we do not consider that ETFs deserve a specific recommendation**. However we would like FSB to conduct its own comparative analysis and hope it would confirm our view that EU regulation is appropriate.

Q5. What liquidity risk management tools should be made available to funds? What tools most effectively promote consistency between investors' redemption behaviours and the liquidity profiles of funds? For example, could redemption fees be used for this purpose separate and apart from any impact they may have on first-mover advantage?

Amundi suggests the following route to be followed by asset managers when deciding pre and post –event tools in order to combine efficiency and flexibility :

- Identification of structurally illiquid asset classes and determination of the most useful tools, especially preemptive measures, for each type;
- Definition of standard liquidity profiles under normal circumstances and determination of the appropriate pre-emptive tools; identification of the risk profile of each fund;
- Close examination of those funds that cannot be assimilated to one of the predetermined profiles and definition of specific rules that would apply to each of them;
- Classification of the post event tools according to their efficiency and to the risk of contagion and damage on the image of the asset manager they create if activated; determination of the tools that nevertheless will be helpful to have at hand under extreme circumstances.

In any case, the adequacy of the tools must be reassessed on a regular basis as part of the task of the governance body of the liquidity risk management.

To be more specific, contingent extraordinary redemption fees belong to the category of tools that may create a panic and a feeling of deep injustice. If they are discretionary and charged only when the asset manager deems necessary, then, whatever the governance organization, the investor who will have to suffer them will be frustrated and feel the victim of a personal ill-treatment. If the redemption fees apply in all circumstances to all clients on the same basis they are no longer a flexible tool and lose their efficiency in stressed conditions. Nevertheless they are an adequate way to maintain fairness between entering, exiting and remaining holders. We do not consider that in most circumstances redemption fees are an adequate tool to adjust redemptions to the liquidity profile of a fund. We even fear that some asset managers may be feeble enough to accept to sign comfort letters to large institutional clients whereby they would find a way to avoid exit fees. The most efficient tools are to be found in the **definition of the terms of S/R** (frequency, notice period, NAV date, settlement date…). There is a need for education of the public as to the reasons for these tools to exist and be implemented.

Most post-event tools should be considered as **a way to organize a proper liquidation** of the fund if needed. And we feel that it will be the end result in many cases at least for several years, the time for investors to understand that these tools are protective. Among the tools mentioned page 12, Amundi does not agree to consider the use of a credit facility as an efficient post event tool. It should be seen as a facility limited both in time and amount and as such represent, when it is authorized, a standard instrument in the management of a fund subject to close risk management constraints.

Q6. What characteristics or metrics are most appropriate to determine if an asset is illiquid and should be subject to guidance related to open-ended funds' investment in illiquid assets? Please also explain the rationales.

As stressed in many instances, liquidity is moving and its dynamics makes it impossible to determine ex ante and once for all what is or is not liquid. Even T bonds and T notes proved illiquid on several occasions. As a result, we think that it is not helpful to try and determine what would be liquid in all times and to issue guidance. High level principle and appropriate supervision by authorities is the best way to proceed leaving it to asset managers to regularly review their limits in terms of liquidity. For example, we believe that a standard level of residual cash is part of the liquidity profile of a fund but that it should evolve with time and market conditions as well as anticipated redemption behaviours of the clients. Thus, **regulators should not decide of a standard cash cushion.** Margin calls must be stressed to make sure that cash enables the fund to meet them. Stressing redemptions however is not easy, it can only rely on historical peaks of redemptions over a short period of time. Actually it is extremely rare that the total of net monthly redemptions reaches a double digit percentage of the assets of a fund.

The proposed EU PRIIPs regulation covers the liquidity risk through the disclosure to the public of one of 3 levels of estimated liquidity of the majority of the assets. We think that a narrative and qualitative approach like that is appropriate to inform the public. Any further detail might be confusing for the public and dangerous for the asset managers responsible for the publication.

Q7. Should all open-ended funds be expected to adhere to the recommendations and employ the same liquidity risk management tools, or should funds be allowed some discretion as to which ones they use? Please specify which measures and tools should be mandatory and which should be discretionary. Please explain the rationales.

Due to the extreme variety of funds, the large number of asset classes and liquidity profiles and the high diversity of investor types, Amundi can only **recommend flexibility** with respect to the choice of the liquidity management tools that should apply to such or such fund. We think that it is up to the asset manager to decide which tool it is appropriate to have access to for each fund it manages.

However, we feel that there should be a minimum of post event **tools available in all cases** as a matter of public interest. Namely, the ability to suspend redemption must be included in the legal framework of the fund industry. It is the most radical tool and is necessary to protect investors. There is a moment when the asset manager is faced with a conflict of interests between the interests on the one hand of the redeeming investors and those on the other hand of the investors wo remain and keep their holding. Suspension of redemptions and subscriptions is the most simple and most efficient way to fix a situation and if necessary allow time to properly liquidate a fund. This tool, though, can be used very temporarily, like on 9/11 when prices for American shares were difficult to assess or after Brexit in the UK for real estate funds; it then gives time to cool down and restore confidence in prices and dealings.

Any fund is naturally confronted with the definition of the subscription/redemption practicalities. It is mandatory as well to fix them in a manner consistent with the dealing, pricing and settlement delays of the underlying assets. In that respect we support recommendation 3 which makes the point even if we would prefer it to be redrafted. We feel that the origin of the process is the underlying assets that according to the investment strategy will be in the portfolio that determine the structure of S/R and not the reverse as suggested in Reco 3.

As for the other tools, Amundi agrees with recommendation 4 that authorities should introduce the largest list of liquidity management tools, so that they are available if needed. But they should be accessible **at the discretion of the asset manager**. We are not sure that asset managers should develop procedures whereby tool C could only be applied after the activation of tools A and B: we have a strong view that tools have different impacts and that it is for the asset manager to use what it feels most appropriate. What is not escapable is a definition of the rules of activation and a clear governance of the process.

The same plea for individual responsibility of the asset manager for each fund applies for stress testing where we do not think it appropriate for regulators to impose a standard. In particular **we oppose recommendation 9** that confuses the role of NCAs to aggregate risk measurements to gain a global view of potential risk and the stress testing exercise that is only meaningful at the level of the fund, the identified entity in terms of liquidity. Liquidity risk and credit risk largely differ in that respect, one may not be aggregated at firm's level when the other may.

Q8. Should authorities be able to direct the use of exceptional liquidity risk management tools in some circumstances? If so, please describe the types of circumstances when this would be appropriate and for which tools.

Yes, Amundi sees liquidity management tools as protective devises to be used in the best interests of fund holders. Authorities share that concern for investor protection and are as well committed to ensuring financial stability. Hence, we believe that the activation of exceptional tools should be decided by the asset manager in concert with the NCA. When a firm activates a suspension of redemptions on one of its funds, it follows a process in which there is time for early information of the NCA and most often good practice includes a prior information of other fund managers through the professional association. The activation of other tools, for example side pocketing, needs a prior agreement of regulators in some countries. We believe that the more transparent with the regulator the asset manager is, the better it is for the whole community. In our view, the governance body of the liquidity management risk process should be responsible for supervision and decision on the basis of investors' best interest and, if we do not oppose NCAs having in last resort the power to require activation on the basis of risk for the financial stability but we think they should refrain from using it.

Amundi is concerned with an issue that is not discussed in the consultation paper: the procedure required to **introduce new tools** in the management of a fund. The official documentation will be modified and typically the prospectus will include a thorough presentation of the new liquidity risk management tools. We believe that the introduction of these new tools should be with immediate application and made known to the public by any means. It should not require a specific mail (nor electronic nor by post) to each holder. The next report would include an explicit mention of these new tools. Otherwise, these tools will not be implemented and ready for use in many funds and the next crisis will result in stressed liquidity conditions that funds will have the same old difficulties to manage.

Q9. In developing leverage measures (Recommendation 10), are the principles listed above for IOSCO's reference appropriate? Are there additional principles that should be considered?

As explained in the introduction in §3.1, there are different types of leverage : traditional balance sheet and repo leverage and larger exposure gained through the use of derivatives. Amundi totally agrees that the use of derivatives is not a factor of risk in itself; FSB rightly states that derivatives may be used with a view of "*hedging risk and establishing cost-effective investment positions*". Measurement of the balance sheet leverage should be, at first view, an easy task if one sticks to the nominal value of the credit received but proves tricky when considering the ability to reinvest proceeds of a Repo or the daily variation due to valuation and S/R flows. When considering leverage via derivatives it can only be assessed on a net basis as the example of hedging shows : it is a diminution of exposure and as such a deleveraging of the fund. However, some argue that gross figures are also very important as they show the level of interconnectedness and counterparty risks. Counterparty risk is a different issue that is now tackled when most derivative transactions are centrally cleared though CCPs closely monitored and supervised by competent authorities and non-centrally cleared transactions are included in an agreement whereby collateral is exchanged on a net basis as well. Other non-linear derivatives are difficult to assess without following a probabilistic approach leading to a reference to the VaR.

Amundi urges FSB to take a proportionate approach when assessing leverage and suggests to consider several measures of leverage. We think that IOSCO should be mandated to further examine the impressive work that has been conducted by European regulators in this field. Our view is that monitoring leverage is possible and effective in Europe despite the fact that at least 3 different measures coexist :

- **gross leverage which is more of a counterparty risk measure**,and gives an improper view of the risk implied by the leverage
- net leverage or **commitment approach** that reflects the notional and physical market exposure of the fund with standard netting possibilities that are not flexible and
- a **risk based measure related to VaR** which is complemented by stress tests and leads to a measure of leverage through the relative VaR of a fund compared to its reference portfolio.

The last two measures are of particular interest to assess the market risk of a fund and are used for different types of strategies. We strongly believe that the framework implemented in the EU should be maintained as a fair example. The AIFM Directive further foresees that NCAs communicate with ESMA and ESRB when, based on the reporting they receive, they are concerned with the development of a potential risk for financial stability.

Q10. Should simple and consistent measure(s) of leverage in funds be developed before consideration of more risk-based measures, or would it be more appropriate to proceed in a different manner, e.g. should both types of measure be developed simultaneously?

Amundi is not convinced that a difference between a simple measurement of leverage and a risk based measurements would be helpful. We think that they should be **used simultaneously or alternatively** and not in a sequence. The aim is to track leverage as a risk factor and a danger in terms of financial stability. Measurement is a way to put a warning and draw attention of the supervisor as well as the internal risk and compliance teams. In order to avoid false signals it is important to properly calibrate the measure and to choose the relevant methodology and scope.

In our experience the communication towards client investors cannot rely on a single and uniform measure. We know that the diversity of measures that the European legislation allows us to use is very helpful to avoid misrepresentation of the notion of leverage. The strict limitations on leverage that are expressed in the UCITS and AIFM directives make the probability of a risk to the financial stability very theoretical. We believe that FSB should focus on hedge funds and recommend a proportionate **'light' regime for funds like UCITS and AIFs not using substantial leverage**. We read that recommendation 11 suggests it and support that approach..

Furthermore, we insist on the fact that regulatory leverage, whatever measure is decided, should **not impact the present use of potentially different measures** in the official documentation and the marketing material of a fund. We believe that recommendation 10 should include that point.

Q11. Are there any particular simple and consistent measures of leverage or risk-based measures that IOSCO should consider?

FSB should not hope and find a unique standard measure for leverage. Alternative methodologies should be available for measuring leverage. FSB has to examine existing methodologies, especially those in use in the EU, and determine their pros and cons. Our conclusion is that some measurements are more informative than others depending on the type of funds. We are convinced that the specific derogation that exists for structured funds in Europe and the use of the scenarios is totally consistent with the requirement to illustrate different cases in order to offer subscribers information on the risk in each case. We also see the reference to

VaR, either absolute or relative, as totally justified for funds with non standard profiles. Our experience is very limited on hedge funds with high leverage, but if we do not manage that risk profile we understand the need for particular attention on leveraged funds and see the advantage of a gross measurement when confronted with many transactions conducted outside the central clearing system. A different focus leads to a different measurement.

Q12. What are the benefits and challenges associated with methodologies for measuring leverage that are currently in place in one or more jurisdictions?

We will refer to the EU regulation and more precisely the two directives, **UCITS and AIFM**, that address the question of leverage in a fund. As a first comment we insist on the fact that Europe has developed a strong regulatory framework that limits leverage of funds. This goes back to many years for UCITS and is more recent for AIFs. Contrary to other major jurisdictions, the EU has identified leverage as a risk in the asset management industry and addressed it in the following way:

- Balance sheet borrowing is the exception and is not allowed for funds offered to the public; UCITS for example can borrow up to 10% of their NAV and this facility is generally provided for by the depositary with a view to heal a breach in the settlement process of a transaction; the same applies for standard AIFs offered to the public (UCITS like);
- Those funds, UCITS and standard AIFs offered to the public, are also prevented from building leverage through SFTs since the ESMA regulation prevents them from reinvesting (except in very low risk, very high quality and liquidity assets) cash received from a Repo or as collateral for a securities lending for example;
- Derivatives can be used not only for hedging purpose but also in order to increase the exposure of the fund to the market ; this is allowed in as much as the net total exposure that will result from both cash and derivative positions will not exceed 200% of the NAV of the fund for UCITS and UCITS like funds and 300% for AIFs that do not use substantial leverage;
- AIFs which are authorized to exceed the 300% limit will be designated as using substantial leverage and as such subject to extra reporting and risk control requirements;
- The percentages are calculated according to a precisely defined methodology based on the commitment approach (see guidance provided by ESMA's predecessor, CESR/10-788) which estimates all positions on the basis of the market value of the underlying asset the derivative gives access to, introduces compensations among positions in opposite directions on exactly the same underlying (for example, long short equity do not compensate) or approaching maturities for fixed income instruments…;
- Some funds may not be properly captured by this approach and there are three substitutes based on scenarios for structured funds and VaR in absolute terms or relative to a reference portfolio; when using the VaR approach for one of the funds it manages, an asset manager must meet specific requirements in terms of risk and model management and control as well as stress testing.
- The AIFMD reporting requirement includes a measure of gross and net (commitment) leverage except for smaller funds and asset managers.

Amundi thinks that the restrictions on reinvestment of proceeds of a Repo or as collateral are too restrictive and harm the possibility for funds that hold assets not eligible as collateral like high yield or emerging market securities to use derivatives for the benefit of clients. We do not ask for total freedom of action and accept limitations that would authorize **re-use in order to constitute collateral at a CCP.**

We believe that FSB should ask IOSCO to take time to analyse existing regulations and measurements of leverage of funds in different jurisdictions and discuss with the local or regional authorities to gain a better flavour of possible outcomes. We suggest to capitalize on the experience of AIFMD and UCITS in the EU and allow for the choice of the most appropriate measure by the asset manager within a large sample of methodologies.

Q13. Do you have any views on how IOSCO's collection of national/regional aggregated data on leverage across its member jurisdictions should be structured (e.g. scope, frequency)?

Here again, Amundi suggests that FSB take stock of existing practices and include them in its recommendations: those jurisdictions that are ahead in the field of reporting of leverage should not be penalized by the introduction of new requirements before a full assessment of the existing system and its efficiency.

We believe that a **half yearly collection** of data is sufficient and that the scope should only include funds significant in gross size, i.e. total net commitment including all types of leverage. Funds combining high leverage and a proportion of assets with a low liquidity could justify a more frequent follow up, on a monthly basis.

Q14. Do the proposed policy recommendations on liquidity and leverage adequately address any interactions between leverage and liquidity risk? Should the policy recommendations be modified in any way to address these interactions? If so, in what ways should they be modified and why?

Amundi totally agrees that the **combination of excessive leverage and poor liquidity** creates the most acute potential for financial stability risk with regard to funds. Putting fraud aside, the failure of a fund that does not use leverage will never happen; at worst investors will lose their money but nobody on the financial markets will suffer damage from the liquidation of the fund, except for servicers that might not be paid. With the introduction of leverage there is a risk that some people suffer losses that are not covered by the capital paid to the fund by investors. It is theoretical, since in practice asset managers that use leverage have developed in parallel a strong risk management expertise. Poor liquidity will exacerbate the risk inherent to leverage. In case of stress and heavy redemptions the asset manager of a leveraged fund will seek cash to meet redemptions. He should also liquidate positions up to the level of leverage to maintain the same level of risk. He could even anticipate to deleverage in order to reduce risk. He needs to untie positions for 'n' times the amount of the cash needed if 'n' is the leverage of the fund. It may imply even more operations since 'n' is the net exposure and that reducing it may imply selling positions that partly compensate each other.

We believe that FSB should specifically draw the regulators' attention to the cumulative effect of leverage and liquidity issues through a **supplementary recommendation**. There should be an identification of those funds that use high leverage and a close monitoring of the liquidity of the assets, physical and derivative, they invest in. That could justify a reinforced reporting requirement and potentially higher frequency. It is a good case to explicitly introduce proportionality in the recommendations. Asset managers should also be required to have procedures whereby those funds would be monitored more attentively than others. FSB should make sure that the scope of these special requirements remains limited to effective high leverage, more than 10 times for example, and large exposure to numerous counterparties outside CCPs.

Q15. The proposed recommendation to address the residual risks associated with operational risk and challenges in transferring investment mandates or client accounts would apply to asset managers that are large, complex, and/or provide critical services. Should the proposed recommendation apply more broadly (e.g. proportionally to all asset managers), or more narrowly as defined in Recommendation 13? If so, please explain the potential scope of application that you believe is appropriate and its rationales.

Amundi does not see much risk for financial stability resulting from operational difficulties for an investor to change asset manager in the case of a fund or a mandate. On open ended funds liquidity conditions are defined in the prospectus and apply to all unit holders. When an investor wants to get out of a fund he simply asks for redemption gets his money back and reinvests in another fund managed by another fund manager. Eventually he will be out of the market for a couple of days (up to a week or more on illiquid funds) between the reference date for the calculation of the NAV of the initial fund and the reference date for the determination of the subscription price. It is up to the investor to decide to invest in a proxy (derivative for example) to maintain or gain the exposure to the market he wishes.

For a mandate, assets on the one hand are held by the custodian bank and portfolio is managed by the AM1. The investor wishes to change to AM2. The standard mandate in our experience includes a specific provision in that case whereby once the decision is notified to AM1, it will make its best efforts to accelerate the transfer of assets (in the case the bank changes as well) and powers to manage the fund (documentation with counterparties and registrars for example). In this action it will regularly report progresses to client and AM2. In the meantime a contradictory inventory is established so that the situation at the time of transfer is clarified and from this point in time, the AM2 will, typically, be in charge of asset management. For practical reasons it may transact through AM1 as long as all counterparties have not taken into account the transfer of powers. This plain procedure that has just been summarized does not carry specific risk, except if the custodian bank or AM1 fails before the termination of the transfer. For AM1 to fail it would require grave neglect on the part of the NCA in charge of supervision, since the NCA has the power to appoint an emergency interim manager to ensure continuity of the activity of an AM. If the investor is to change bank as well he may suffer if the initial bank is about to fail. However, if cash is not segregated all securities accounts are. Eventually, there is no risk linked to asset management but to transferability of account that has to be regulated.

For a fund that is dedicated to an investor who holds the entirety (at the exception of 1 unit sometimes) of the fund, its redemption will mean the liquidation of the fund. The time necessary for this liquidation will be a good test of the liquidity profile of the portfolio. However the client may decide to keep the assets and transfer the management to AM2 who will amend the existing portfolio and not start with cash. Technically, either there is a repayment and a subscription in kind (what is potentially easier) or a change of AM in the documentation of the fund (which has to be approved by the competent authority). The question to keep or change the depositary is open and must be answered anyway; it may create a further short delay.

Amundi does not agree with the proposed recommendation 13 and does not share the view to address the issue of transferring in a recommendation is relevant. If FSB nevertheless wants to make this point, we have a strong view that the recommendation should apply to all asset managers irrespective of their size. The risk to meet difficulties in our view is probably higher with a smaller firm who may have less precise procedures and less experience in transferring portfolios. Proportionality here should rely on the type of investment : no OTC derivative, no external fund were the subscriber would not be directly and totally identified, simple listed securities plus cash, … those are situations where proportionality would apply whatever the size of the fund or the AM.

If recommendation 13 aims at **addressing operational risk**, we think that it should encourage IOSCO to draft principles in this area that would go beyond the production of business continuity plans. In different countries Asset managers establish a map of their potential risks, quantify the impact they might have on their business, identify ways to reduce these risks and establish procedures to face them when they happen. We feel that what is required from asset managers in many jurisdictions should be considered as good practice and replicated in principles that would help enhancing the standard of the asset management industry. We know that prudentially regulated entities are required to post capital to face operational risk on the basis of a valuation of its impact in the past. We think that this approach could apply to asset management only if a fair judgment on the risks and their consequences would be expressed before targeting and calibrating any requirement. We consider that duplicating the banking approach is simply not acceptable.

Lastly, we would like to encourage FSB to go one step further following foot note 52 page 28. We do consider that **data providers present a systemic level of risk**. We acknowledge that we heavily rely on their information flows and that they tend to take advantage of their oligopolistic position, leaving only minimal space for new comers to address one micro market only. We feel that there is an urgent need for regulators to act and we suggest that FSB work on principles to better organize the profession and analyse their marketing practices of aggregated offers, the documentation and their contractual responsibilities and the concept of proprietary rights in the context of data and often public data.

Q16. In your view, what are the relevant information/data items authorities should monitor for financial stability purposes in relation to indemnifications provided by agent lenders/asset managers to clients in relation to their securities lending activities?

Amundi fundamentally believes that an asset manager should not engage in providing indemnifications to counterparties of funds it manages, with respect to securities lending. The only exception should be to act as an intermediary through a subsidiary that is authorized to conduct such transactions and **subject to prudential regulation, especially capital requirement**. Alternatively, if conducted directly at the AM company level it should be subject to the same prudential rules for this activity.

To bring further clarity to investors and the public at large, we suggest that asset managers providing indemnifications be identified as such and that it should show in their documentation as a specific risk category: asset manager with high risk on their own capital.

Q17. Should the proposed recommendation be modified in any way to address residual risks related to indemnifications? For example, should it be more specific with respect to actions to be taken by authorities (e.g. identifying specific means for covering potential credit losses) or more general (e.g. leaving to authorities to determine the nature of appropriate action rather than specifying coverage of potential credit losses)?

Yes, as mentioned in the answer to question 16 above, we do not agree with the idea that asset managers could be authorized to provide indemnifications in the framework of securities lending activities. Recommendation 14 should express the following principle: it is not an activity directly eligible for asset managers. The recommendation would continue by stating that asset managers may constitute and adequately capitalize subsidiary that would conduct such activities within the authorized framework of a banking status.

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