

MEMO# 30003

June 23, 2016

FSB Proposes Policy Recommendations to Address "Structural Vulnerabilities" from Asset Management Activities

[30003]

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TO: ACCOUNTING/TREASURERS MEMBERS No. 15-16
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CLOSED-END INVESTMENT COMPANY MEMBERS No. 9-16
COMPLIANCE MEMBERS No. 19-16
ETF (EXCHANGE-TRADED FUNDS) COMMITTEE No. 13-16
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ICI GLOBAL REGULATED FUNDS COMMITTEE No. 41-16
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SMALL FUNDS MEMBERS No. 27-16
UNIT INVESTMENT TRUST MEMBERS No. 4-16
VARIABLE INSURANCE PRODUCTS ADVISORY COMMITTEE No. 13-16 RE: FSB PROPOSES
POLICY RECOMMENDATIONS TO ADDRESS "STRUCTURAL VULNERABILITIES" FROM ASSET
MANAGEMENT ACTIVITIES

For the past several years, the Financial Stability Board ("FSB") has been examining whether the asset management sector poses risks to global financial stability. In 2014 and 2015, the FSB issued for public comment proposed assessment methodologies for identifying non-bank, non-insurer global systemically important financial institutions ("NBNI G-SIFIs"), including investment funds and (in the 2015 proposal) asset managers. The FSB also began a separate workstream in 2015 focusing on asset management activities. In July 2015, the FSB announced that it was setting aside the NBNI G-SIFI project until after completion of the activities-based work. Over the next eight months, the FSB made known its specific areas of focus regarding asset management activities and its intention to develop and launch a public consultation on policy recommendations in the first half of 2016.

As anticipated, on June 22, the FSB issued a consultative document (“consultation”) regarding “structural vulnerabilities” in asset management activities. [\[1\]](#) A brief description of the consultation follows below. Comments are due to the FSB by September 21. ICI intends to submit a detailed letter responding to the consultation.

The consultation notes at the outset that money market funds are excluded from its scope, in light of “regulatory reforms that have been implemented (or are in the process of being implemented) in many jurisdictions to address financial stability issues that arose during the 2007-09 global financial crisis.” The consultation begins with an overview of recent trends in the asset management sector. It then focuses on four areas: [\[2\]](#)

1. liquidity mismatch between fund investments and redemption terms and conditions for fund units;
2. leverage within investment funds;
3. operational risks and challenges in transferring investment mandates in a stressed condition; and
4. securities lending activities of asset managers and funds. [\[3\]](#)

For each of these areas, the consultation describes the purported vulnerability, analyzes existing mitigants to address the vulnerability, and sets forth proposed policy recommendations to address “residual risks” to global financial stability associated with that vulnerability (after taking existing mitigants into account). In total, there are 14 proposed policy recommendations, nine of which relate to liquidity mismatch and three of which relate to leverage. According to the FSB, “issues associated with liquidity mismatch and leverage are considered key vulnerabilities.” A copy of Annex 1 to the consultation, which lists all of the proposed policy recommendations, is attached.

Many of the recommendations call for follow-up work by the International Organization of Securities Commissions (“IOSCO”). In a related action, the Board of IOSCO on June 22 issued a statement outlining IOSCO’s priorities regarding data gaps in the asset management industry. [\[4\]](#)

The consultation indicates that the FSB intends to finalize its policy recommendations by year-end. It also reconfirms the FSB’s plan, jointly with IOSCO, to “revisit[] the scope of NBNI G-SIFI assessment methodologies” after the recommendations in the consultation are finalized. The consultation states that for asset management, the focus will be on “any residual entity-based sources of systemic risk from distress or disorderly failure that cannot be effectively addressed by market-wide activities-based policies.”

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[Attachment](#)

endnotes

[\[1\]](#) Financial Stability Board, Consultative Document, Proposed Policy Recommendations to Address Structural Vulnerabilities from Asset Management Activities (22 June 2016),

available at

<http://www.fsb.org/wp-content/uploads/FSB-Asset-Management-Consultative-Document.pdf>.

[2] The FSB initially identified five areas of focus. As to the fifth area—potential vulnerabilities of pension funds and sovereign wealth funds (“SWFs”)—the consultation states that any financial stability risks posed by these funds “may be better assessed when the FSB revisits the scope of NBNI G-SIFI assessment methodologies.” Annex 2 to the consultation sets forth preliminary results of the FSB’s analysis regarding potential vulnerabilities of pension funds and SWFs.

[3] Similarly, in its ongoing review of potential financial stability risks in asset management, the US Financial Stability Oversight Council is focusing on: liquidity and redemption risk in investment funds; use of leverage; operational risk; securities lending; and resolvability and transition planning. See Financial Stability Oversight Council, Update on Review of Asset Management Products and Activities (April 18, 2016), available at <https://www.treasury.gov/initiatives/fsoc/news/Documents/FSOC%20Update%20on%20Review%20of%20Asset%20Management%20Products%20and%20Activities.pdf>.

[4] Board of the International Organization of Securities Commissions, Statement on IOSCO’s Priorities Regarding Data Gaps in the Asset Management Industry (June 2016), available at <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD533.pdf>.

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