



15 November, 2023

Via email: www.centralbank.ie/fundsurvey

Central Bank of Ireland
New Wapping Street
North Wall Quay
Dublin 1
D01 F7X3

**Re: Discussion Paper
An approach to macroprudential policy for investment funds**

Dear Sir or Madam:

Managed Funds Association (“**MFA**”)¹ submits these comments to the Central Bank of Ireland (“**Central Bank**”) in response to the Central Bank’s request for comments on the above-referenced discussion paper (“**Discussion Paper**”),² with a focus on the aspects of the Discussion Paper applicable to private funds and their investment managers,³ many of which are organized or domiciled in Ireland. We have set out our responses to the relevant questions in the Discussion Paper in the Annex hereto.

We have considered the Discussion Paper in context with efforts of other regulatory bodies such as the Financial Stability Oversight Council (“**FSOC**”) and the Financial Stability Board (“**FSB**”). MFA views the Discussion Paper in recognition of the considerable importance of Ireland in the global funds market as the fourth largest investment fund sector globally, and having seen considerable growth since the

¹ MFA, based in Washington, DC, New York, Brussels, and London, represents the global alternative asset management industry. MFA’s mission is to advance the ability of alternative asset managers to raise capital, invest, and generate returns for their beneficiaries. MFA advocates on behalf of its membership and convenes stakeholders to address global regulatory, operational, and business issues. MFA has more than 170 member firms, including traditional hedge funds, credit funds, and crossover funds, that collectively manage nearly \$2.2 trillion across a diverse group of investment strategies. Member firms help pension plans, university endowments, charitable foundations, and other institutional investors to diversify their investments, manage risk, and generate attractive returns over time.

² See Central Bank of Ireland, Discussion Paper: an approach to macroprudential policy for investment funds (July 2023), available at https://www.centralbank.ie/docs/default-source/publications/discussion-papers/discussion-paper-11/dp-11-an-approach-to-macroprudential-policy-for-investment-funds.pdf?sfvrsn=23059f1d_3.

³ The global alternative asset management industry, including hedge funds, credit funds, and crossover funds, has assets under management of \$4 trillion (Q4 2022). The industry serves thousands of public and private pension funds, charitable endowments, foundations, sovereign governments, and other global institutional investors by providing portfolio diversification and risk-adjusted returns to help meet their funding obligations and return targets.

2008 global financial crisis (“GFC”).⁴ Broadly, MFA agrees with the goals of seeking to mitigate against systemic risk; however, investment funds generally, and private funds in particular, are ill-suited targets for macroprudential policies aimed at reducing systemic risk. In our response, we highlight our concerns with seeking to apply macroprudential policy to private funds and ask the Central Bank to consider these facts as it moves forward with its macroprudential policy deliberations.

Executive Summary

MFA appreciates the efforts of the CBI in publishing the Discussion Paper as a means of continuing and focusing the dialog with the investment funds industry and related stakeholders regarding systemic risk. Appropriate risk management is a cornerstone of the private funds industry, and MFA is keenly focused on systemic risk discussions globally and welcomes the ongoing dialog of the CBI in this key area. For reasons set forth in the Annex, the premise of the Discussion Paper, respectfully, appears misplaced, as it seems to presume that *all* investment funds contain and generate systemic risk and then seeks support for the case for some form of macroprudential regulation that would apply to private funds.

As we discuss, if the goal of the regulation is to reduce systemic risk in the financial services ecosystem, macroprudential regulation should not be applied to private funds. A top-level response to the specific questions posed by the Discussion Paper, in the order presented, are as follows:

1. With respect to the Discussion Paper’s assessment of the potential channels of systemic risk, private funds historically have not been shown to generate systemic risks relating to liquidity or leverage.
2. Private funds employ a diverse range of strategies, many of which are non-correlated but all of which are heavily risk-managed by the fund, and as such the collective actions of private funds are dispersed among many smaller cohorts of related fund strategies.
3. As it relates to the current regulatory framework, which was designed with an investor-protection focus, current regulations contain ample measures to address the systemic issues. Private funds also provide considerable benefits to the markets and are subject to extensive systemic-related reporting requirements. The imposition of bank-like regulation on them could undermine broader stability goals.
4. As it relates to the key proposed objectives and principles of macroprudential policy, MFA urges the Central Bank to first focus on ensuring that it receives the data needed from investment funds, including private funds, and other market participants to assess the existence and source of risk. Reliable and complete data must serve as the predicate to any consideration of macroprudential regulation.
5. The issues highlighted pertaining to the design of potential specific macroprudential tools in the funds sector must be premised on the receipt of accurate and relevant data from investment

⁴ See Discussion Paper, *supra* note 2, at 10.

funds (including private funds); without accurate data it is premature to label any particular sector of the investment funds industry as posing systemic risk.

6. Counterparties mitigate interconnectedness risk of all investors (not just investment funds): they perform critical risk functions benefitting the broader system through collateral, margin, and related risk requirements. Private funds, moreover, open and close in an orderly fashion for a variety of reasons and it therefore cannot be said to create contagion risk in their unwinding. Private funds therefore are not appropriate targets of regulations protecting those “too big to fail.”
7. MFA concurs, as noted above, that it is critical that regulatory authorities receive robust, accurate, and timely data from investment funds that is harmonized across jurisdiction so that regulatory authorities can make an “apples to apples” comparison of fund data. Given the global nature of the investment funds industry, it also is of paramount importance that the Central Bank’s regulations are aligned with US, EU, and other regulators, with appropriate recognition of other jurisdictions’ regulatory standards.
8. In addition to governance and data considerations, our view is that it is critical that the Central Bank of Ireland appreciate that private funds themselves are not systemically risky and if the purpose is to reduce systemic risk, then it first is critical to identify the risk and its source to assess whether it is a risk that can be effectively and fairly addressed through activities-based regulation.

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MFA appreciates the opportunity to provide these comments to the Central Bank in response to the Discussion Paper. If you have any questions about these comments, or if we can provide further information, please do not hesitate to contact the undersigned or Jeff Himstreet (jhimstreet@managedfunds.org) at (202) 730-2600.

Sincerely yours,

/s/ Jillien Flores

Jillien Flores
Executive Vice President
Head of Global Government Affairs

ANNEX

Question 1 *Do you agree with the above assessment of the potential channels through which investment funds can generate systemic risk?*

MFA Response:

It is important to consider the different types of investment funds that may generate systemic risk, recognizing that not all investment funds create the same risks. An analysis of liquidity risk management and the use of leverage in the private funds industry necessarily is a fund-by-fund analysis.

A. Private Funds Manage Liquidity Risk Through Contractual Limitations

Private funds do not offer daily redemption to investors, and as such have not been susceptible to mass redemptions in times of stress. Private fund documents govern investor liquidity standards for investors.

Private funds' investors are typically large, sophisticated institutional investors such as foundations, endowments, and pension funds – and they understand the redemption limitations on the fund and often times have multi-generational investment horizons. We did not see mass redemptions from private funds during times of stress, largely because the funds' sophisticated private fund investors knew and appreciated the redemption limitations to which they agreed, and the private funds enforced fairly the redemption terms agreed to by investors.

The liquidity risk of a given private fund is correlated to the liquidity of the underlying assets. A typical hedge fund, which is invested in a portfolio of liquid securities and other investments, may offer redemptions quarterly, up to a stated percentage of the fund's assets. Once that stated percentage is met, no additional redemptions are permitted for that period. Managing redemption amounts by contract has proven an effective means for private funds to manage liquidity risk. Further, private fund investors agree to, and have the sophistication to, appreciate the limitations on redemptions required of the fund.

The less-liquid the portfolio holdings, the longer the contractual limits on redemptions tend to be. Private credit funds, for example, tend to have multi-year lock-up periods to reflect the less-liquid nature of the underlying investments. Private credit funds typically hold direct loans, for example, through maturity as there is no developed secondary market for these bespoke, individually negotiated loans. Frequent redemptions simply would not work in a private credit fund as they may with a private fund investing in large-cap, liquid equity securities.

B. The Use of Leverage by Private Funds Is Effectively Risk-Managed by Both the Fund and Its Counterparties

As noted above, counterparties to private funds manage their own risks and limit contagion risk through margin and collateral requirements. These requirements also create an economic disincentive for the investor to incur excessive risk. For funds that use leverage, it moreover is important to not conflate a fund's use of leverage across the financial system as a whole, or even with risk levels proposed by an organisation that manages a fund that uses leverage. Because asset classes each have

distinct risk exposures, leverage metrics based on a single aggregate number across asset classes do not provide a meaningful basis on which to assess the risks associated with an investment funds use of leverage and are likely to mislead regulatory authorities reviewing the data. The review of misleading data could result in regulatory authorities attempting to solve a non-existent problem, leading it to potentially miss areas of systemic risk that exist in the financial ecosystem in areas other than investment funds. Leverage measurements must be assessed on an asset class by asset class basis, rather than as a single aggregated number. It furthermore is critical that regulatory authorities consider the *purpose* of leverage: a bona fide hedging transaction mitigates risk (both the fund and systemically), whereas a speculative naked call option does not.

Across the fund industry globally, private funds are relatively limited users of leverage. The US Federal Reserve for example stated with respect to private credit that “[m]ost private credit funds use little leverage and have low redemption risks, making it unlikely that these funds would amplify market stress through asset sales.”⁵ Private funds are more commonly holders of long positions in debt and equity investments that are acquired through capital invested by investors, and leveraged positions are often times derivative positions to hedge against currency or interest rate risks. It therefore is far more common that the investors are bearers of counterparty exposure risk rather than transmitters of risk to the counterparties.

It should be noted that many institutional investors beyond investment funds use leverage in some form and it would be unfair to single out investment funds as the target of any macroprudential regulation in this regard.

Question 2 ***Do you agree with the assessment in this Discussion Paper that it is primarily the collective actions of investment funds that can generate systemic risks?***

MFA Response:

Systemic risk results from more complicated factors than a simple collective action problem. In the private funds sector, there exist a multitude of strategies that often are not correlated with each other and in fact, the diverse strategies serve to mitigate or diffuse collective risks because the strategies have different underlying risk profiles, assets, and liquidity constraints. Collective action risk exists in the global markets across the investment spectrum and cannot be fairly targeted to private funds, or investment funds more generally -- investors of all sizes trade securities in parallel based on news or economic events and it would be inappropriate to solely target investment funds in this regard.

Market forces also can dampen the impact of collective action across the broader marketplace. As an example, short interest in individual names is published by dealers regularly, and it is true that investors, whether they are private funds or investment managers of separately managed accounts, may engage in “copycat” trading strategies and short the same positions. Here, the markets effectively self-correct: as short interest grows, the rate charged to borrow the securities to effect the short sale increases, reflecting the finite quantity of securities available to cover and creating an economic disincentive for excessive shorting of the same name.

⁵ Financial Stability Report, *supra* note 6, at 47.

Question 3 *Do you agree that the current regulatory framework for funds -- which has primarily been designed at a global level from an investor protection perspective – has not been sufficient to reduce the propensity of certain fund cohorts to amplify shocks?*

MFA Response:

The current regulatory framework already addresses systemic risks for investment fund activities. The investor protection focus of the existing regulatory framework, including the UCITS Directive, is appropriate for funds with retail investors. The UCITS Directive contains provisions to ensure ongoing liquidity and limit fund holdings in illiquid assets for funds with daily liquidity requirements. Leverage limitations for investment funds are addressed both by the UCITS directive and AIFMD. AIFMD obligates private fund managers to report leverage and grants authority to impose limits on leverage under Article 25. Because existing regulatory requirements govern managers' uses of liquidity and leverage, additional regulations aimed at macroprudential issues for private funds would appear redundant to existing applicable regulatory requirements.

Macroprudential regulation, attempting to manage or mitigate risks, for private funds, is misplaced. The investment risks of private funds are shouldered by the sophisticated institutional investors of the funds. The activities of private funds are already subject to extensive systemic-related regulations; private funds' activities also are exceedingly unlikely to create stability risks for Irish or EU financial systems. In the US, as it relates to private credit funds for example, the Federal Reserve has stated that "financial stability vulnerabilities posed by private credit funds appear to be limited."⁶ We agree, as the activities of private funds are best suited to market and investor protection regulation by functional regulators, rather than bank-like supervision and regulation. Private funds historically have provided resilience to financial markets in the EU and US, often during stressed market conditions.

Critically, private funds differ from other financial market participants because they are ultimately vehicles for the management of others' assets. Private funds therefore do not maintain a large balance sheet of their own assets. Private funds facilitate access to particular financial instruments or strategies on behalf of sophisticated investors that understand the liquidity limitations of the fund and are capable of assessing and bearing investment risks. In the US, the Dodd-Frank Act already acknowledges this reality, which requires the US stability regulators in exercising its authority to consider "the extent to which assets are managed rather than owned by the company, and the extent to which ownership of assets under management is diffuse."⁷

MFA is committed to collaborating with the primary financial regulators of private funds and their advisers to mitigate emerging risks to U.S. financial stability. Existing regulations currently require robust liquidity risk management practices and liquidity limits, and allow regulators to monitor for leverage. MFA recommends that the Central Bank work alongside other market regulators to craft

⁶ FEDERAL RESERVE, FINANCIAL STABILITY REPORT 47 (2023) (Additionally, "most private credit funds use little leverage and have low redemption risks, making it unlikely that these funds would amplify market stress through asset sales.") ("**Financial Stability Report**").

⁷ 12 U.S.C. § 5323(a)(2)(F).

activity-specific recommendations to be applied to all market participants (not just investment funds) to the extent the data demonstrate the existence of a systemic risk suitable for a regulatory solution.

A. Private Funds Provide Resiliency to Financial Markets and Are Subject to Extensive Reporting Requirements

The risk management practices of private funds, prevailing market structure, and the existing regulatory framework all significantly limit the potential that private funds would act as a source of systemic risk. The private fund industry is characterized by low concentration, low contagion risk, and robust risk management practices. These characteristics alongside existing regulatory structures make private funds better suited to activities-based oversight.

The private fund industry is further characterized by diversity which has enhanced resiliency for financial stability. While global banking is intensely concentrated among the largest firms, private funds demonstrate much greater competitiveness. This diversity means that Central Bank concerns, such as interconnectedness and concentration, are of diminished relevance when applied to the private fund industry.

Considering the aforementioned characteristics of the private fund industry, MFA recommends that the Central Bank continue to focus on systemic risk monitoring activities. Private funds currently report extensive information to the European Systemic Risk Board (“**ESRB**”) on Annex IV under AIFMD.⁸ In the US, private funds similarly report extensive risk metrics to the Securities and Exchange Commission (“**SEC**”) and the Commodity Futures Trading Commission (“**CFTC**”), including stress tests, portfolio information including collateral, margin and cash reserves, counterparty exposures and myriad other details, all of which are available to FSOC. Given that the ESRB already collects systemic data for EU AIFMs and non-EU AIFMs marketing in the EU, the ESRB should lead any effort to expand the data AIFMs report on Annex IV. MFA encourages the Central Bank to continue its interagency coordination with US and other regulators as it relates to regulatory reporting of private fund data for systemic risk and related purposes. We recommend that the Central Bank continue to focus on these efforts and increase its dialogue with market participants and other stakeholders to foster efficient, transparent, fair, and effective policy.

B. Bank-Like Regulation of Private Funds Would Not Enhance Financial Stability

Private funds, regardless of strategy, are fundamentally different from banks. Private funds are not funded by liabilities like deposits, which are redeemable at par and on demand, and do not benefit from deposit insurance or typical government-sponsored liquidity. Instead, private fund investors commit long-term capital, take investment risk, and accordingly agree to redemption limits established and enforced by fund managers to manage liquidity. Private funds fundamentally are investment products limited to sophisticated parties that do not require daily or “on demand” liquidity, are typically advised by professionals, and understand the investment and related risks. Private funds should be regulated accordingly and are so regulated by applicable functional regulators in the US and EU.

⁸ See EMSA, Guidelines on reporting obligations under Articles 3(3)(d) and 24(1), (2), and (4) of the AIFMD (8 Aug. 2014) (avail. at <https://www.esma.europa.eu/sites/default/files/library/2015/11/2014-869.pdf>).

The Central Bank's evaluations of activities-based regulation or other action must consider costs and benefits to the affected investment fund(s). On this score, MFA remains deeply skeptical of suggestions to impose bank-like regulation onto a private fund. Risk management is a cornerstone of the private fund industry, and firms have taken steps to mitigate identified risks. For example, as evidenced in the quarterly Form PF reports filed with the SEC, financing for private funds is overwhelmingly obtained through collateralised arrangements from sophisticated counterparties with robust risk monitoring. In the US, considering the US private funds market, the US Government Accountability Office concluded that leverage lending had not contributed to bank (or other financial entity) distress,⁹ which suggests that banks are effectively managing exposure leverages to borrowers through collateral and other margin requirements, thus serving to mitigate any interconnectedness risk (i.e., risk of contagion). The GAO study is relevant to the Discussion Paper as many private funds organised in Ireland trade through US-based banks.

Private funds also manage liquidity risk by contractually controlling the timing and amount of redemptions given the investment strategy of the fund. Being able to control redemptions greatly mitigates fire sale concerns.¹⁰ In the US, Form PF reports provide detailed analyses of asset and liability liquidity, including redemption provisions.

While any determinative conclusions would require formal cost-benefit analysis on an entity-by-entity basis, the costs imposed by the capital requirements, supervision and resolution planning requirements that result from bank-like regulation would be significant and potentially fatal to the private fund, and wholly unnecessary and/or redundant to existing requirements. Elimination of private funds reduces the availability of capital for businesses and would adversely affect innovation and increase financing costs, reducing the resiliency of both the financial markets and the real economy. For investors such as pension funds, foundations, endowments, and insurance companies, a reduced market for private funds associated with markedly higher compliance costs would remove a critical source of uncorrelated returns and harm these institutional investors and their beneficiaries.

Question 4 ***Do you agree with the key proposed objectives and principles of macroprudential policy for funds as set out in this Discussion Paper? Are there additional principles, which need to be considered?***

MFA Response:

A key principle for investment fund regulators globally is access to reliable data from the investment funds to assess the level of liquidity and risk more accurately in the system. MFA appreciates the efforts of the Central Bank to expand the development of its portal ("**Portal**") to investment funds.¹¹

⁹ See GOV'T ACCOUNTABILITY OFFICE, FINANCIAL STABILITY: AGENCIES HAVE NOT FOUND LEVERAGED LENDING TO SIGNIFICANTLY THREATEN STABILITY BUT REMAIN CAUTIOUS AMID PANDEMIC, 34-35 (2020).

¹⁰ See MANAGED FUNDS ASS'N, THE ROLE OF PRIVATE CREDIT IN U.S. CAPITAL MARKETS 10 (2020).

¹¹ CENTRAL BANK OF IRELAND, REPORTING REQUIREMENTS FOR IRISH AUTHORISED INVESTMENT FUNDS (June 2018), available at www.centralbank.ie/docs/default-source/regulation/industry-market-sectors/funds-service-providers-aifm/onr-investmentfunds/guidance-note-regulatory-reporting-vol-4-0-june-2018.pdf.

Currently, investment funds submit financial statements, a fund profile, reports of derivatives usage, and material breaches or other material matters through the Portal.

Despite the use of the Central Bank’s Portal by investment funds to report information, the Discussion Paper notes that data is a “key challenge” to “facilitate[] risk identification, policy design, and evaluation.”¹² MFA agrees and supports the Central Bank’s recognition of an internationally consistent data framework – it should be an essential pre-requisite for any consideration of the exercise of macroprudential authority.

MFA encourages the Form PF and Annex IV reporting requirements to be harmonized where possible, and urges the Central Bank to advocate harmonized requirements to the ESRB. Inconsistent data sets in the Form PF and Annex IV data (such as derivatives trade reporting, as an example) severely limits the usefulness of the data itself. Without accurate data from private funds that is comparable across jurisdictions, it is difficult for regulatory authorities to obtain a clear picture of investment funds and their strategies, investments, size, and risks. Accurate, reliable data must serve as the predicate for any justification of the need for macroprudential regulation by the Central Bank or any other regulatory body to address activities or products that may present systemic risks.

Question 5 *Do you agree with the analysis and the issues highlighted pertaining to the design of potential specific macroprudential tools for the funds sector? Are there additional potential tools that could be explored?*

MFA Response:

When it comes to the design of macroprudential tools, if the goal is to reduce systemic risk, a healthy first step would be to understand what risks are presented. As we have discussed, there is nothing unique about either private funds’ structures or investment strategies that are harbingers of systemic risks. Without adequate data, however, it is difficult for any regulatory authority to assess risk, much less regulate and mitigate any such risk.

In addition, MFA suggests that if the Central Bank identifies information filed by a particular investment fund that would suggest the existence of systemic risk posed by that fund, it should engage with the investment fund directly and collaboratively to better understand the nature of the risk. If the Central Bank identifies collective characteristics of funds that pose systemic risks, then the Central Bank should engage with the SEC and other global regulatory authorities to take an activity-based approach, coordinated globally, to address the systemic risk(s) that fund data demonstrate are present. A “regulation by hypothesis” approach simply is not appropriate.

We do not agree that additional systemic tools should be explored. As we have seen in the US, designation of non-bank entities as systemically important, and thereby attempting to apply banking regulation to non-bank entities has been ineffective. Initial efforts by the FSOC to designate entities as

¹² Discussion Paper, *supra* note 2, at 51.

systemically important have been nullified by courts for failing to adequately consider the costs and benefits of such designation to the affected entity.¹³

Further, as noted above, the tools used by systemic regulators are ill-suited and redundant to existing regulatory requirements. US non-bank entities that have been deemed systemically important, before the FSOC guidance was revised in 2019,¹⁴ have been required to perform stress tests and maintain resolution plans to discuss how a failing non-bank entity would winddown its operations in an orderly manner.

On stress testing, we note that private funds in the US are currently required by Form PF to perform stress tests regularly and report the results of those tests to the SEC and FSOC.¹⁵ It is not necessary for the Central Bank to impose a duplicative stress test requirement. Resolution plans, as we discuss below in response to Question 6, are not applicable to private funds: private funds fail from time to time, for a variety of reasons. When they do, there is an orderly process that begins with the prime brokers and other counterparties declaring an event of default and closing out positions according to the underlying agreements. The fund assets are then liquidated, with the cash and securities proceeds distributed to the sophisticated investors on a pro-rata basis. There simply is no need to prepare a resolution plan that lays out this orderly, routine process.

Question 6 *Do you agree that tools could target the interconnectedness of funds as well as/instead of their vulnerabilities?*

MFA Response:

Investment funds, by their nature, require some degree of interconnectedness. They rely on executing dealers to buy and sell securities and financial products on their behalf. Investment funds rely on custodians to safekeep investment assets, and fund administrators to perform account on-boarding and related functions.

A. Private Fund Interconnectedness Does Not Result in Systemic Risk for Which Macroprudential Regulation Is Necessary or Appropriate

Private funds have been shown to pose modest, at best, interconnectedness risk partly because of the limited use of leverage and strong risk management controls. Margin and collateral requirements serve to limit the amount of leverage that a private fund can incur, and dealers can increase or adjust requirements to manage leverage and other risks as trading, credit, or market conditions warrant.

¹³ Metlife v. Financial Stability Oversight Counsel, 177 F. Supp. 3d 219 (D.D.C. 2016).

¹⁴ See Financial Stability Oversight Council, Authority to Require Supervision and Regulation of Certain Nonbank Financial Companies, 84 Fed. Reg. 71740 (De. 30, 2019).

¹⁵ Form PF, at Item 42 (available at www.sec.gov/about/forms/formpf.pdf).

The Discussion Paper states that macroprudential tools could target vulnerabilities such as a liquidity mismatch and leverage of fund cohorts.¹⁶ With this standard of “interconnectedness,” the key issue would appear to be not only whether an investment fund is “connected” to other market participants but whether the entity’s failure could force a disorderly unwinding of positions (both on- and off-balance sheet) that would result in a cascading series of failures among counterparties that could spread elsewhere within the counterparty firm or to the counterparties of that counterparty.

As a general matter, relationships with counterparties are an appropriate area of focus when considering the potential for transmission of risk throughout the system. Adequate risk management by both the private fund and the counterparty can and does mitigate the possibilities of losses resulting from risk transmission. The risk-mitigation reforms enacted globally after the GFC have done much to reduce transmission of risk throughout the system, with an emphasis on clearing derivatives transactions, prompt reporting of them to regulators, and requiring minimum margin amounts for uncleared transactions.

B. The Concept of “Too Big to Fail” Does Not Apply to Private Funds

All losses to a private fund that winds down its operations are borne by the sophisticated, institutional investors. There is no taxpayer “bailout” or concept of “too big to fail.” Private funds have and will continue to close and, each time, there is no systemic risk because the fund structure silos the losses, which are borne by the private fund investors.

Relatedly, each year there are private funds that wind down and they do not cause financial stability problems when doing so. No private fund closure during the 2008 financial crisis or since has threatened market functioning or financial stability. Regulations implemented because of the European Market Infrastructure Regulation (“EMIR”) and the Dodd-Frank Act, including derivatives clearing, margining, and reporting, have further bolstered the resiliency of the private fund industry and minimize the risk a private fund failure would spread to its counterparties or more broadly. Counterparty risk management practices also have strengthened considerably, further reducing the likelihood that counterparty exposures, even in periods of market stress, would have widespread impact on financial markets.

Any suggestion that the interconnectedness of private funds can amplify the effects of a shock to the financial system is,¹⁷ respectfully, misplaced and does not reflect the experience of private funds that actually have failed and the absence of any interconnectedness risk associated with the winding down of those funds. Private funds fail for a variety of reasons, whether from the failure to attract and maintain sufficient assets, mergers or reorganizations with other entities, or poor performance. Private funds unwind in an established and orderly process. Agreements such as prime brokerage agreements and trading agreements (such as ISDAs or master repurchase agreements) are terminated, closing positions are valued pursuant to those agreements, and the fund or the counterparty pay any difference

¹⁶ Discussion Paper, *supra* note 2, at 27.

¹⁷ *Id.* at 15.

owed. The fund then liquidates its assets and distributes the proceeds (either in cash and/or investments) to limited partners on a *pro rata* basis.

Question 7 *Do you agree with the governance and data considerations highlighted in this Discussion Paper when operationalising macroprudential policy for funds?*

MFA Response:

We discuss the need for accurate data reporting on AIFMDs in response to Items 3 and 4, above.

MFA concurs with the assessment of the Central Bank that the investment funds industry is global in nature. Irish-based funds offered in the EU may be available to investors in the US and elsewhere. As such, it is critical that regulators recognize substantially equivalent regulatory regimes in other jurisdictions to facilitate the global growth of the investment funds industry. The global investment funds industry benefits with appropriate reciprocity amongst jurisdictions as “[w]ithout this, there is risk of a fragmented macroprudential framework[] for investment funds which could limit effectiveness and unnecessarily increase costs for industry and, potentially its customers.”¹⁸

The actions of one regulatory authority can in fact impact other jurisdictions. A fund that is operating globally may find itself having to comply with the most burdensome common requirement amongst jurisdictions or attempt to offer a fund only in that jurisdiction that would operate in parallel to other funds with the same strategy that are offered in other jurisdictions. Regulatory inconsistencies that drive private fund organizational structures can dilute or eliminate economies of scale the manager has sought to achieve. MFA agrees that some degree of flexibility will be needed to “account for different conditions and circumstances across jurisdictions.”¹⁹

Question 8 *Beyond governance and data considerations, are there additional issues that need to be considered when operationalising macroprudential policy for funds?*

MFA Response:

MFA suggests that the Central Bank carefully consider the problem it is seeking to solve and whether any macroprudential policy for investment funds can appropriately be applied to private funds. Private funds manage liquidity risk by contract, based on the redemption limits investors agree to which, as discussed above, vary depending on the underlying strategy of the private fund. Leverage is risk-managed by both the private fund and its counterparties, consistent with applicable margin and collateral requirements.

To the extent there are *activities* of investment funds that the Central Bank, in consultation with other global regulators, deem to be systemically risky, MFA urges the Central Bank to consider working with functional regulators to develop and propose the necessary rules to limit the activity that it deems systemically risky. Designating an entity as systemically important would be misplaced and ultimately leave the macro-level systemic risk largely where it was: the designation would merely cause the target

¹⁸ *Id.*, at 48.

¹⁹ *Id.*

entity to seek to de-risk its activities by selling off business lines or ceasing activities, causing those systemic risks to be dispersed elsewhere in the financial ecosystem.

The markets have evolved considerably since the days of Long-Term Capital Management,²⁰ and citing it as an example of spillover risk is out of place in today's financial system. Global regulatory reforms, combined with vastly improved risk management practices at dealers and investment funds alike, reduce considerably the likelihood of a repeat event caused by a single fund. Global regulatory reforms in the areas of derivatives clearing, reporting, uncleared swap margin requirements, and enhanced central counterparty resilience have strengthened our markets and buy-side and sell-side participants' risk management considerably. Any effort to develop any macroprudential regulation for the investment funds industry, private funds in particular, must be viewed through a current perspective that reflects the regulatory regime and market participants risk controls, rather than the failure of a single, highly leveraged fund 25 years ago – before EMIR, before Dodd-Frank, and before swaps regulation generally.

²⁰ *Id.*, at 17.