Response to Central Bank of Ireland Discussion Paper: An approach to macroprudential policy for investment funds

10 November 2023

INREV* welcomes the opportunity to respond to the Central Bank of Ireland Discussion Paper: An approach to macroprudential policy for investment funds. Through our submission, we hope to make a constructive contribution to the important issues raised in the discussion paper.

Our comments fall broadly into three areas: the potential inconsistency between this consultation and the work and findings of CP145; the potential inconsistency between outcomes of the current consultation and new measures related to fund liquidity management introduced by the EU under the recently completed AIFMD Review; and recent FSB, IOSCO and ESRB reports and recommendations are based on incorrect assumptions regarding the real estate industry and therefore should not be used as the basis of the CBI’s analysis or recommendations.

Potential inconsistency between this consultation and the work and findings of CP 145

As a preliminary issue, we believe the intention and scope of the current consultation is not clear; specifically, does the CBI intend to include real estate funds within its scope? We note that the CBI recently focused intensively on real estate funds in CP145 and, therefore, we don’t understand whether the current consultation would override and/or replace the efforts and tentative findings and conclusions made in that consultation, or whether the current consultation would simply complement the work of CP145. We understand that in meetings, the CBI has expressed the view that issues in respect of real estate funds have been addressed in CP145 and are not the focus of the current consultation. If this is the case, it should be made clear.

In any case, we feel strongly that regulation resulting from the current consultation should not introduce further, potentially inconsistent, changes for real estate by accident. We would therefore urge the CBI to carefully assess the degree to which and areas in which the current consultation would apply to real estate investment funds. Any proposed measures that are not intended to apply to real estate investment funds should be expressly spelled out.

Potential inconsistency between outcomes of the current consultation and new measures related to fund liquidity management introduced by the EU under the recently completed AIFMD Review

In Brussels, trilogue discussions on AIFMD recently concluded with a political agreement and technical discussions. While the final agreed measures have not yet been published, it is clear that there will be significant new measures related to liquidity management by investment funds. It seems premature for the CBI to launch into the development of liquidity management requirements for Irish investment funds until the new EU measures are published and a proper gap analysis can be conducted that includes further consideration of whether additional measures are needed.

Beyond the need for additional regulations, the risk of introducing potentially inconsistent, or at the very least confusing or redundant, changes regarding liquidity management by funds is considerable and should be avoided. Rules relating to liquidity management by funds that are unique to Ireland when the EU is adopting measures applicable across the entire union should also be avoided because of the confusion, complexity and chilling effect on investment into Ireland that they could create.

Recent FSB, IOSCO and ESRB reports and recommendations are based on incorrect assumptions regarding the real estate industry and therefore should not be used as the basis of the CBI's analysis or recommendations

It is extremely unfortunate that the FSB, IOSCO and ESRB addressed the issue of fund liquidity management without full knowledge or accurate information, at least concerning the real estate investment funds industry. As we made clear in our response to the recent FSB and IOSCO consultations, both are based at least partially on incorrect assumptions regarding real estate and the conclusions are therefore generally flawed.

In our response to the FSB consultation, we noted that their proposals are rigid and difficult to be implemented in practice. In addition, they are not aligned with the broad message of the existing IOSCO Guidelines from 2018 and the proposed update from IOSCO to which the FSB consultation refers.

In our response to the IOSCO consultation, we noted that we do not see benefits in IOSCO making general changes to the 2018 recommendations at this stage. It is not clear to us whether the intention of the proposals is investor protection or to address systemic risk. The IOSCO consultation implies the former, the FSB consultation the latter. If the concern is systemic risk, then the focus should be on the types of funds and underlying asset types where the risk is felt to lie, rather than attempting to apply blanket rules to all OEFs.

We agree with the FSB that there shouldn't be a "one-size-fits-all" approach across all OEFs. The liquidity management of OEF depends upon the assets the fund is investing in and also, the type of investors, retail, or institutional, investing in the fund. We are pleased to see that in DP11, it is acknowledged that given the diversity of the funds sector a 'one-size fits all' approach is unlikely to be effective. Also, we would like to highlight that in the case of real estate funds, there shouldn't be a "one-size-fits-all" approach for all types of real estate funds. The liquidity of real estate assets varies considerably according to the underlying assets. The creation of categories of OEF based on their liquidity profiles will create rigid and arbitrary thresholds for such funds which however will in practice be difficult to manage, particularly for actively managed funds.

There is a wide universe of open-ended funds with differing liquidity profiles and dealing frequencies which would be difficult to shoehorn into three liquidity categories. Also, we have concern that such an approach will be applied differently across jurisdictions creating confusion for investors and supervisory authorities. It also creates a significant risk of regulatory cliff-edges.

We also find the following statement from the FSB, in relation to "illiquid" funds (Category 2 funds) confusing and lacking support: "The relevant authorities could also consider requiring that such funds be structured as closed-ended funds". Further, the references in the consultation to "daily dealing" are oversimplified and may be misleading. A fund may offer investors the opportunity to subscribe daily even if they are not allowed to redeem daily. A fund may allow investors to redeem daily if their redemption is being matched with an incoming investor, but provide for a longer redemption period if there are net outflows and a sale of an underlying investment is required.

We strongly agree with the FSB that managers of OEFs have the primary responsibility and are best placed to manage the liquidity of their portfolios. They should be given the discretion, within a liquidity management framework, of implementing appropriate liquidity management measures and tools.

Conclusion

In conclusion, we would urge the CBI to clarify that the current consultation does not apply to real estate funds, as they were recently addressed in CP145; to wait until new EU measures for fund liquidity management are adopted in the revised AIFMD and an analysis is conducted of what, if any, further measures are needed; and to not accept blindly the "facts" and conclusions supporting the FSB, IOSCO and ESRB recommendations that relate to real estate without further close scrutiny and fact checking.

* INREV is the European Association for Investors in Non-Listed Real Estate Vehicles. We provide guidance, research and information related to the development and harmonisation of professional standards, reporting guidelines and corporate governance within the non-listed property funds industry across Europe.

INREV currently has more than 500 members. Our member base includes institutional investors from around the globe including pension funds, insurance companies and sovereign wealth funds, as well as investment banks, fund managers, fund of funds managers and advisors representing all facets of investing into non-listed real estate vehicles in Europe and the UK. Our fund manager members manage more than 500 non-listed real estate investment funds, as well as joint ventures, club deals and separate accounts for institutional investors.