THE INVESTMENT ASSOCIATION

Basel Committee on Banking Supervision
Centralbahnplatz 2,
4051 Basel
Switzerland

28 August 2024

Dear Sir/Madam.

RE: BCBS Guidelines for Counterparty Credit Risk Management

The Investment Association (IA) champions UK investment management, a world-leading industry which helps millions of households save for the future while supporting businesses and economic growth in the UK and abroad. Our 270 members range from smaller, specialist UK firms to European and global investment managers with a UK base. Collectively, they manage £9.1 trillion for savers and institutions, such as pension schemes and insurance companies, in the UK and beyond. 46% of this is for overseas clients. The UK asset management industry is the largest in Europe and the second largest globally.

Our members, as part of the buy-side, are key counterparties of the credit institutions that the Basel Committee on Banking Supervision (BCBS)'s guidelines are aimed at. This reform package, although aimed at sell-side institutions, will undoubtedly impact on buy-side institutions. In view of the increased role of buy-side institutions, in particular asset managers, in the financing of the real economy and the management of capital, it is essential the downstream implications on the buy-side from these reforms are taken into consideration when determining Counterparty Credit Risk Guidelines for sell-side credit institutions. The IA therefore welcomes the opportunity to respond to the BCBS's consultative document.

Robust, well-capitalised credit institutions are vital to the stability of financial markets, and we recognise the importance of robust credit risk management in credit institutions. In that regard, we are very supportive of the work of the BCBS work in updating its guidelines to improve risk management and the proper assessment of counterparties.

While supportive of the overall work of the BCBS, as with other bank-led macroprudential policy, this framework has been developed by dividing financial institutions into two categories – bank and non-bank. The latter category, grouped together as "Non-bank Financial Intermediaries" (NBFIs), is broad and fails to recognise key differences between institutions falling into this category. In particular, the proposed framework fails to distinguish between NBFIs that are regulated, and the risk management requirements they are subject to, including risk limits and reporting requirements to their own regulators, and those who are unregulated and thus not subject to such requirements.

There are significant differences between different constituents of NBFIs. Some sectors within NBFI are heavily regulated, such as asset managers, insurers, pension schemes and investment funds. These are themselves subject to strict risk management requirements, must report information to regulators and

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must set strict internal risk limits and, in the case of regulated products, are also subject to regulatory risk exposure limits. Asset managers in particular are subject to strict asset segregation requirements, which mean that their clients are not exposed to balance sheet risks of the asset manager. Investment funds are also subject to strict asset segregation requirements, along with diversification and risk exposure limits – assets are ring-fenced from those of the manager and those of other investment funds.

This is very different to other NBFI sectors that are subject to little to no regulation, and for which regulators have very little visibility over their activities. It is notable that Archegos, which is cited as one of the primary drivers for recommending strengthening the guidelines, was established as a family office, and therefore was not a regulated entity.

We therefore suggest that the guidelines should identify the regulated status, and consideration of the regulations that counterparts are subject to, within the recommendations for the counterparty credit risk assessments that are performed by credit institutions. This is not to say that there should not be a credit risk assessment for regulated counterparties – this is a vital part of due diligence and is performed today. But not differentiating between regulated and non-regulated NBFIs will result in more onerous due diligence for regulated NBFIs than is needed, creating inefficiencies, increasing workloads and costs for both the credit institutions and these counterparties, for no measurable benefit. Given the activities and risk positions of these entities are already monitored and supervised by regulators, we suggest that a more proportionate approach should be permitted in the case of counterparties that are regulated.

This will ensure the focus is weighted to unregulated counterparties, which are not supervised and on which regulators have little information. Consequently, risks are likely to be higher where counterparties are not regulated, and this is where there should be a higher focus in understanding the activities, capital resources and risks of those counterparties.

The IA does not consider it appropriate to seek to control risks to credit institutions through placing additional restrictions on the activities of regulated NBFIs, whose activities are already subject to regulatory limits, along with supervision and monitoring by regulators. For asset managers (as well as for many other regulated NBFIs), derivative transactions are often undertaken to limit risks in the portfolios they manage for clients or investment funds or to efficiently gain exposure consistent with market risk (ie on a delta-one basis). Placing overly onerous barriers on the ability of regulated NBFIs to enter into these transactions would ultimately harm their end clients and potentially leave them exposed to higher portfolio risks.

It ultimately falls on credit institutions to be responsible for their counterparty risk management processes and ensure they do not take inappropriate risk exposures with individual counterparties. Any shortcomings in these processes must be addressed by the credit institutions themselves, where necessary strengthening governance to ensure that sound risk management decisions on limiting exposure to high risk, unregulated counterparties are not overridden by commercial considerations.

The IA would be happy to discuss the activities of asset managers, including the services they provide and products they offer, such as investment funds, with the BCBS.

Yours faithfully

Peter Capper
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