Banc Ceannais na hÉireann
Central Bank of Ireland
Eurosystem

Macroprudential Policy for the Property Fund Sector – Consultation Paper 145

Feedback from Northern Trust Fiduciary Services (Ireland) Limited 'NTFSIL").

Do you agree with the proposal in Consultation Paper 145 to limit leverage and introduce additional Guidance around liquidity mismatches as a means to meet the Central Bank's objective of safeguarding resilience of the property fund sector to shocks in the Irish CRE market? If not, which measures, or combination of measures, do you think best meet the objective of safeguarding resilience of the property funds sector, so that it is better able to absorb – rather than amplify – shocks in the Irish CRE market?

Response:
We do not believe the application of a leverage limit to all funds, regardless of their investor base, redemption facility and/or investment objective, is a reasonable approach to adopt. We also believe that a leverage limit should not be introduced on a retrospective basis. We would broadly welcome the introduction of the proposed liquidity measures. Please see further responses in respect of the proposed measures below.

Do you agree that the definition of property funds – for the purposes of the proposed macroprudential measures – should include all AIFs that are domiciled in Ireland, authorised under domestic legislation, and investing over 50 per cent directly or indirectly in Irish CRE, subject to the narrow class of exclusions noted in the consultation paper? If not, what do you see as a better alternative definition of property funds for the purposes of application of the proposed measures?

Response:
We believe it is reasonable for the Central Bank in conducting its analysis to have focused upon a threshold of 50% in terms of identifying funds that require consideration from a leverage perspective. However, we believe there are other fund characteristics that require consideration in the context of applying leverage controls. In our opinion, it is clear the guidance is based upon detailed analysis and is comprehensive in scope, identifying risks existing within the market, it does not however sufficiently consider its impact to all forms of property funds and in our view, further tailoring and consideration is required.

We believe the application of a 50% leverage limit to all Irish authorised AIFs, with more than 50% invested in Irish commercial real estate 'CRE") (collectively hereafter referred to as "Property Funds"), may have the unintended consequence, of transferring the investment in Irish CRE to funds located in other jurisdictions and/or Irish unregulated entities. We therefore believe that leverage controls should be tailored to the different types of Property Funds, taking into consideration a Property Fund's redemption facility, investor base and investment objectives. We also believe that such leverage controls, if possible, should be reflective of leverage levels at which banks are willing to lend on commercial terms to projects (based on their risk and security requirements). On that basis, we do not believe that it is appropriate to simply apply one leverage level to all forms of Property Fund.

Do you agree with the Central Bank's proposal to have a single leverage limit, irrespective of the type of property holdings? If not, how would you differentiate the limit with respect to property holding type, and what would be the practical implications of doing so (e.g. additional, more granular data collection)?

Response:
We believe further consideration is required in respect of Property Funds investing in development assets. Development funds have specific characteristics that need to be considered in the context of the guidance. A development fund is required to purchase an asset and drawdown on its capital and lending as the development progresses. The value of any lending relative to the development's valuation will be higher in the earlier stages of the development. Development funds are unusual therefore in that, for the duration of the development, the fund may have significant liabilities in comparison to its asset values. This can result in such funds maintaining very low NAVs during their development phase. Consequently, it is not appropriate to limit a development fund's leverage limit to 50% of its NAV and a more holistic approach is necessary to assess the reasonableness of the leverage position, in the context of these funds.

In the event the Central Bank was to apply the guidance to development funds without taking these characteristics into account, development funds would not be able to obtain the borrowing necessary to initiate and complete otherwise viable projects. The introduction of leverage controls in respect of development funds therefore warrants further consideration. In our view, it would be more appropriate to consider the final development value in the context of its lending. We therefore believe the leverage limit should be based on a percentage of the forecasted NAV and not the actual NAV existing at the time of leverage.

Do you agree with the proposed calibration of the 50 per cent total loan to total asset ratio as the appropriate leverage limit for property funds? If not, what level of leverage limit would you see as appropriate for Irish property funds, taking into account the risks the sector is exposed to and the levels of leverage employed by property funds throughout Europe? Please explain why you have suggested this level and the evidence that would support that.

Response:
Introduction

We do not believe the proposed leverage measure is the appropriate leverage control to be applied to Property Funds. We acknowledge the Central Bank's rationale in applying direct leverage limits on Property Funds, due to the variation of lenders in the market and the fact that the Central Bank does not supervise non-Irish banks. However, we would like to bring the following factors to the attention of the Central Bank, prior to proceeding with such an approach:

1. The proposal to (i) apply leverage controls retrospectively and (ii) adjust leverage levels on an on-going basis (depending on market conditions), is not conducive to the stable investment environment necessary for a Property Fund to effectively operate. Managers, promotors, investment managers and investors require a level of certainty that the parameters of their investment objectives will not be subject to continuous change. Such measures may diminish the

attractiveness of Irish regulated funds to the property sector, resulting in a potential reduction in investment / development;

2. A leverage limit applicable to Irish structures only, may result in the unintended consequence of directing ownership of Irish CRE to non-Irish or unregulated structures, which is likely to inhibit the regulation of leverage levels pertaining to Irish property investment;

3. Leverage arrangements involve contractual provisions that cannot be easily unwound, amended or re-financed without penalties and costs being incurred by the borrower. It is necessary to ensure the introduction of leverage controls does not result in Property Funds having to renegotiate their financing arrangements on a continual basis;

4. Where leverage is acquired, it is a crucial component of the Property Fund's investment strategy. Property Funds may be limited to the extent upon which they can subsequently adjust their leverage exposure, particularly where the portfolio contains concentrated holdings. Accordingly, leverage controls should not be introduced in a manner that results in Property Funds being rendered non-viable;

5. A Property Fund's investor base should be considered in the context of leverage limits, as well as its redemption cycle. Redemption cycles and the number of investors in a Property Fund will affect a fund's risk profile. As such, there should be different leverage controls applicable to open and closed-ended funds and the volume of investors should also influence leverage limits;

6. We believe it is necessary to take account of the leverage, currently within Property Funds, represented by shareholder loans. Shareholder loans do not present the same degree of systemic risk associated with third party bank loans and it is therefore necessary for the analysis to take such loan features into consideration;

7. The guidance would be more practical, to the extent that it addressed current commercial lending practices, including current loan to value ratios applied to lending arrangements;

8. Operational challenges would arise in the event leverage limits were applied on a fixed on-going basis, in a manner similar to an investment restriction. Decreases in property market values will inevitably lead to increases in percentage leverage levels. Any

leverage control should take account of such market fluctuation, thereby reducing the time managers, depositaries and the Central Bank would otherwise have to spend reviewing and responding to inconsequential leverage breaches. We also do not believe that a fund should be required to create a buffer, as referenced in the guidance, in respect of its leverage, as this is the de facto establishment of a leverage level below the actual threshold.

Point 1: The Necessity of a Stable Investment Environment

For Property Funds to succeed, investment managers need to be able to structure their investment strategies in an environment that is stable. Where a jurisdiction introduces additional regulatory requirements during the life cycle of a Property Fund, particularly those that significantly challenge a fund's ability to fulfil its objectives, managers are not likely to continue to structure new investments in that jurisdiction.

We note the Central Bank's intention to continue to keep any leverage limitation applied under review and to tighten and relax such limit as market conditions demand. Whilst we understand the rationale for considering such an approach, in our view, this approach would similarly bring about a level of uncertainty within the market that is not conducive to a stable investment environment.

Point 2: Re-directing Ownership of Irish Property

The suggested approach may be an appropriate measure to address leverage risk in the medium-term but in the long-term, the same measures may remove the Central Bank from having a supervisory role over Irish property investments, as the guidance may result is an increase in Irish real estate being held by non-Irish or Irish but unregulated parties. In our opinion, unless this issue is addressed at an EU level, the measures introduced may only serve to move the regulation of leverage outside of the jurisdiction. The introduction of leverage levels for Property Funds, is worthy of consideration at an EU level.

As the CBI is aware, the most significant competitor from a fund perspective to Ireland is Luxembourg. Luxembourg and Ireland are the leading jurisdictions within the EU for the establishment of regulated funds. Accordingly, whilst it is informative to be aware of leverage positions elsewhere within the EU, the most critical jurisdiction for comparison purposes is Luxembourg. Luxembourg has not adopted any leverage limitation on property funds either from a regulator or industry guidance perspective. In our view, there is a real concern; therefore, that managers will consider Ireland to be less attractive than Luxembourg when launching Property Funds. This may result in Irish AIFMs initiating re-domiciliation proceedings, re-establishing their strategy and existing leverage arrangements as a Luxembourg based fund.

The increase of international ownership of Irish CRE may also arise in the event the guidance results in distressed selling of assets by (Irish) Property Funds at the end of the transition period. We anticipate that in such circumstances (Irish) Property Funds may experience capital and resource constraints due to the impact of the guidance and as a result be poorly positioned to take advantage of such market event, unlike international funds.

Such developments would have the combined effect of removing the Central Bank from its ability to directly oversee fund market participants holding Irish property. Accordingly, the leverage controls to be applied need to be sufficient from a Central Bank perspective but also manageable from an industry one.

Point 3: The Ability to Adjust Leverage Arrangements

Leverage positions, once established, are not easily unwound and in the situations in which they can be, such process can result in significant costs to a fund. The loan arrangement will be governed on a contractual basis, imposing on-going obligations on both parties. Such obligations will include repayment schedules that are aligned to agreed interest rates. In the event the Property Fund requests a departure from the agreed arrangement, in order to reduce its lending, such request is likely to result in the fund incurring financial penalties and a requirement for re-financing. These costs are not in the best interests of investors.

The holding of Property Fund assets is reliant on both a fund's equity and committed lending arrangements. A fund's liquidity and cash management policies will be based on agreed lending contracts and such policies will not incorporate rebalancing requirements arising from leverage limit breaches (driven by cyclical fluctuations in property values). As such, even where it is possible to amend contractual lending arrangements, there are other aspects of the fund's strategy that require the retention of the leverage agreed under the fund's initial agreements.

Point 4: The Impact upon Property Funds with Concentrated Portfolios

A significant number of Property Funds have concentrated portfolios, holding, at times, one or two properties. Where a Property Fund has a concentrated portfolio and has a leverage limit imposed on a retrospective basis, such fund may not be able to sell part of its portfolio, to reduce its leverage position. Accordingly, the only other means available to a fund to reduce its leverage, is the introduction of additional capital and this is not always possible. In addition, a Property Fund may be closed-ended and therefore have no or limited means of acquiring further capital and/or it may be structured as a single investor fund for privacy purposes.

Accordingly, where an increase in capital is not feasible, such funds will have a limited ability to reduce their leverage position, irrespective of how long a transition period is introduced for compliance. Such funds may be left with no alternative but to terminate prematurely as they have no means of maintaining their strategy within the new parameters. On this basis, we believe we may see several Property Funds having to dispose of significant property holdings at the same time.

In our view, it is important to ensure that additional leverage controls considered under the guidance are applied on a forward basis only.

Point 5: The Investor Base and Redemption Facility

We do not believe it is appropriate to apply a single leverage limit to all Property Funds, we do not believe â€œa one size fits allâ€ approach is the best way to proceed. There are specific characteristics arising within sub-sets of Property Funds that elevate the risks associated with leverage.

Closed-ended funds, with low numbers of investors, will not face the same redemption demands as open-ended funds, with a high number of investors. Such closed-ended funds have a lower risk profile when it comes to managing their leverage position, as they are not required to use fund liquidity to satisfy unforeseen redemption requests. In our experience, in times of market stress, closed-ended funds have not been pressured into selling assets into a distressed market, in order to manage leverage arrangements.

Where a fund is closed-ended, such fund is protected against investor redemption demands and in principle, should be better positioned to maintain its leverage commitments. Accordingly, where the fund is considerably less likely to experience default, such risk differential should be reflected within the leverage limitations applied.

Point 6: The Distinction between Third Party Bank and Shareholder Debt

We also believe, in the context of assessing systemic risk pertaining to Property Funds, that it is relevant to distinguish between third party bank debt and shareholder debt for two reasons. Firstly, the Central Bank has introduced prohibitions on the further establishment of shareholder debt and as such, has taken measures to reduce the extent of leverage available to a fund, which shall have a direct impact on leverage used by Property Funds. And secondly, the risks associated with third party bank loans, do not arise to the same extent in respect of shareholder loans.

In our experience, where a Property Fund holds a very high leverage exposure, often, such levels arise, as a result of the fund having an amalgamation of both third-party bank and shareholder loans. However, in our opinion, shareholder loans have a lower risk profile from a leverage perspective. Market risk analysis with respect to leverage should be more focused upon third party bank loans. Shareholder loans have characteristics that are not equivalent to third party bank loans and consequently, these loan types present different risks to a Property Fund, that need to be accounted for, in the context of any leverage assessment.

Where a third party bank extends a loan facility to a Property Fund, the bank has performed a detailed credit assessment on the Property Fund, is satisfied with the nature of collateral being provided and it has ensured it has the appropriate rights in place to execute a right of enforcement upon the collateral.

Comparatively, shareholder loans are generally unsecured or if secured, subordinated and will have minimal rights in terms of any enforcement proceedings. As a result, the actions of shareholders as lenders and the providers of leverage, are less likely to result in the forced sale of assets, compared to bank lending.

The difference between the two loan types is relevant to any leverage assessment, as shareholder loans are considerably less likely to result in enforcement action, in the event a fund default. In our view, the leverage represented by shareholder loans does not create the same systemic risk as bank lending, with respect to the potential for the forced sale of assets to meet lending obligations.

Point 7: The Experience of Property Funds in Challenging Markets

There have been several market events in the last two years that have tested the resiliency Property Funds, most notably the Covid-19 pandemic. During the pandemic, Property Funds experienced a decrease in values, however, such decreases did not result in the material fire sale of Irish property into distressed markets.

Since the 2008 financial crisis, credit institutions have significantly enhanced their lending controls. However, notwithstanding such enhancements, lenders continue to provide lending in excess of a 50% loan to value ratio, to finance high-quality property developments and acquisitions. Such practices are based on informed risk determinations with respect to their lending activities and the provision of high-quality collateral. In our view, it would be beneficial for all parties concerned, if the commercial basis on which lenders are providing such finance was incorporated and evaluated as part of the supporting analysis of the guidance, as leverage levels above 50% are reflective of commercial lending practices. We believe there is a strong rationale to adopt tiered leverage controls in respect of qualifying investors and we believe a blanket leverage limit may deter investment in high-quality property investments.

Point 8: The Operational Challenge with a Fixed Limit

The value of property holdings shall fluctuate during the term of a lending arrangement. A decrease in the valuation of a property will increase the leverage percentage. However, where the leverage increase is not significant, the fund's risk profile will not have materially changed and it should be able to continue to manage its loan repayments. In our view, due to the constraints referred to above with respect to the fund's contractual obligations, it would be a disproportionate, in terms of mitigating against leverage risk, to require a fund to adjust its leverage arrangements, due to subsequent market fluctuations, where such fluctuations give rise to insignificant changes in the leverage exposure. In addition, such a requirement may place the fund under further strain and de-stabilise its performance. Accordingly, we do not support the proposal of imposing a leverage limitation to operate in a similar manner as an investment restriction and we would similarly oppose the proposal to require funds to prepare remediation plans and engage with the Central Bank every time there is a fluctuation in excess of the leverage limit. In our view, the engagement by all parties on fluctuations in leverage levels above a certain level will consume resources in situations where the market risk is minimal.

Our Overall Assessment of the Proposed Leverage Limitation of 50%

We believe that (i) the restrictive nature of a blanket application of a 50% leverage limit; (ii) the uncertainty associated with the potential for amendments to the limit, depending on market condition; and (iii) the continual application of the 50% leverage limit in the same manner as an investment restriction; will ultimately encourage managers to structure their Irish property investments in other jurisdictions in unregulated entities.

Our Suggested Approach to the Initiation of Leverage Controls

We believe it would be more appropriate for a point in time leverage control to apply at the time of a fund's leverage acquisition, as a systematic ex ante control measure. Property Funds should be afforded flexibility to take account of market value fluctuations. In our view, if Property Funds are not afforded this flexibility, the leverage limit may act to exacerbate market stress as opposed to reduce it.

We believe there should be varying leverage permissions depending on characteristics of the fund. We believe:

i. The leverage control relevant to development funds should be based on the completion value of the development; and

ii. Leverage controls should take account of the fund's redemption facilities (i.e. whether it is open or closed-ended) as well as its investor base.

We believe leverage controls need to be tailored to specific fund characteristics such that the leverage control applicable to a closed-ended fund with a small number of investors (i.e. a low risk fund) is much more expansive in scope than the leverage control applicable to an open-ended fund with large number of investors.

We understand that whilst leverage controls may have been introduced in other EU jurisdictions, such jurisdictions have differentiated leverage limits based on investor type and their leverage levels exceed 50% for qualifying investors. For example, Germany has introduced leverage limits that reach 150% for closed-ended retail schemes and are 60% for non-retail schemes.

We also believe it would only be appropriate to require funds to engage with the Central Bank where their leverage exposure significantly exceeded the leverage limit applied. We believe such engagement should be focused on the fund's ability to manage its leverage arrangements and not solely on the reduction of leverage within the fund.

Conclusion

In our view, it is in the interest of Property Funds, investors, managers, service providers and the market alike to ensure a careful balance is maintained between investment facilitation and leverage risk control. We do not support the blanket application of 50% leverage limit, and we believe such limits requires tailoring to certain fund types. We believe the limit should be set at the point of acquisition and we do not believe that a fund should be required to engage with the Central Bank unless it has materially exceeded its initial limit. In our view, such engagement, should be focused, on a case by case basis, on the viability of the fund and its position as a going concern and should not necessarily require immediate action to reduce its leverage position.

In our view, if the Central Bank introduces a leverage limit that is inconsistent with other EU jurisdictions and out of step with the current bank lending terms, it will result in managers structuring their Irish property investments off shore and in unregulated entities.

Do you consider three years to be a sufficient amount of time to undertake any deleveraging in a gradual and orderly manner to meet the leverage limit as proposed, without the need to sell property assets over a short period of time? If not, what would an alternative transition timeframe be? Please explain why you have suggested this alternative length of time.

Response:
No.

We believe any application of a leverage limit on a retrospective basis would be disproportionate. A retrospective application of a leverage limit, however gradual, has the potential to undermine a fund's ability to achieve its objectives, which amounts to a very unfair outcome for both investors and managers alike. We would be concerned that such measure could result in the forced sale of properties held by Irish regulated funds, which is contrary to the objective of the guidance and it could create rather than reduce market stress.

The retrospective introduction of a leverage limit could have a negative impact on investors in existing Property Funds. Funds that are currently meeting their investment objectives and in compliance with their loan covenants, may be forced to sell property holdings or obtain additional capital. The disposal of assets or the dilution of an investor's interest, is not in the best interests of the funds or their investor. If a fund is meeting its objectives and in compliance with its loan arrangements, it should not be forced to take actions that are not in the investors' best interests.

A number of issues arise:

Point 1: Single Investor Funds

In respect of single investor funds, the strategy in place is dependent solely on the capital of the single investor. As such, it may not be possible for such funds to obtain additional capital to reduce their leverage levels.

In our view, if additional capital is obtained, the guidance will result in an unnecessary dilution of single investor's interest in a fund. The dilution is unnecessary on the basis that such funds, in most circumstances, have a viable capital and lending structure in place and will be operating on a going-concern basis. Accordingly, such funds, are not presenting a systemic risk issue that warrants such dilution.

In our view, single investor funds that have leverage in excess of 50% and are meeting their lending covenants or in exceptional cases in discussions with their lenders, should be afforded the opportunity to continue with their investment strategy, without been forced into a position over a three year period, where they have to obtain additional capital or dispose of their property holdings.

Point 2: Market Impact

As mentioned above, closed-ended funds have limited ability to generate further capital and accordingly, in order to decrease their leverage position, such funds are likely to be under greater pressure to sell assets within their portfolios. In addition, as Property Funds can tend to hold concentrated portfolios, any necessary asset sales to facilitate a reduction in lending, could potentially lead to the fund having to terminate prematurely.

We would therefore anticipate Property Funds, either at the commencement or the end of the transitional period, having to sell Irish property assets into the market. This could result the fire sale of Irish CRE to non-Irish fund structures or unregulated entities.

If the guidance is introduced in its current format, with a three-year time horizon for compliance, Property Funds will be required to dedicate their resources to complying with an arbitrary leverage limit, that will have been introduced retrospectively. This will result in Property Funds having to sell assets over that three-year period, whilst ignoring the fact, that they have viable capital structures and do not pose a systemic risk to the market.

Point 3: Shareholder Loans

As mentioned above, the Central Bank introduced measures last April, that prohibit Property Funds from obtaining new shareholder loans. In our view, the leverage created by shareholder loans does not pose systemic risk to same extent as bank lending. We also believe, that Shareholder loans will significantly decrease in value over the medium-term, as funds repay this form of lending. We therefore believe, there will be a significant decrease in the leverage position of Property Funds as result of the natural reduction in shareholder lending. Accordingly, the current leverage levels are not reflective of where the leverage position will be in three years, even without any further controls being added. On the basis that the reduction in shareholder loans will diminish the levels of leverage in the market, there is no necessity to impose the leverage guidance retrospectively.

Conclusion

In our view, leverage controls should not be applied retrospectively, as such an unforeseen requirement would cause considerable disruption to a fund's investment objective to the point that it will trigger property sales and could bring about fund terminations.

Do you consider the proposed approach to adjusting the leverage limit in response either to large, unanticipated adverse price shocks and/or significant overheating to be appropriate? If not, what do you see as a better alternative approach to adjusting the leverage limit to reflect cyclical risk developments in the Irish CRE market?

Response:
No. For the reasons outlined above, we do not believe it will be workable to proceed with an on-going leverage limit that may fluctuate based on market movements. We similarly believe that a static leverage limit applied across the lifetime of the fund, would also be problematic. Accordingly, as mentioned previously, we believe the most prudent means of addressing this issue is to introduce a point in time leverage control under EU legislation.

In our view, the prohibition of shareholder loans will reduce the levels of leverage in Property Funds substantially. In addition, the risks related to bank lending are carefully assessed in terms of the quality of the investment portfolios. We believe, the leverage levels across Property Funds will align with levels reflective of bank lending standards.

Do you agree with the use of Guidance on liquidity timeframes (with a focus on longer notification periods) to reduce liquidity mismatch in property funds? If not, how would you propose to reduce liquidity mismatch in property funds?

Response:
Yes. We agree the proposed measures in this regard are appropriate to be applied to funds that are not already adhering to such practices. However, we do not believe that the liquidity timeframe should impact upon the director's ability to permit redemptions at their discretion. In other words, if a fund is in a liquidity position to meet an investor's redemption request in a timeframe of less than 12 months, without causing liquidity stress to the portfolio or resulting in a valuation dilution to existing investors, this should be permitted, subject to board approval.

Do you agree that 12 months is an appropriate liquidity timeframe (notification period plus settlement period) for property funds, to ensure that a sufficient timeframe is available to meet unexpected redemptions without requiring forced sales, even under conditions of collective market stress? If not, how long of a liquidity timeframe period do you think would be sufficient to reduce liquidity mismatch, even under conditions of collective market stress?

Response:
Yes. We believe 12 months is an appropriate timeframe.

Do you have any additional evidence on the time it takes to sell property assets in Ireland, both in normal market conditions and in times of stress?

Response:
No.

In addition to the analysis provided in Consultation Paper 145, what potential unintended consequences do you see from the proposed measures, and how could these be mitigated?

Response:
As referred to above, we believe the following may arise as unintended consequences of the introduction of a leverage limit:

1. The creation of an unstable investment environment necessary for Property Funds to operate;
2. Property Fund structures may become unattractive to investors, as leverage levels are not set for investor types at a single level in other EU countries;
3. A migration of Irish CRE to non-Irish funds or unregulated entities;
4. Possible asset fire sales; and
5. Possible fund terminations

If there are any significant operational difficulties envisaged by AIFMs in complying with leverage limits imposed via Article 25, please provide brief details, including any possible solutions if appropriate.

Response:
As mentioned above, we believe it would be more effective if a suite of more tailored leverage controls were introduced at an EU level, for example by way of ESMA Questionnaire.

We also believe that funds will be challenged to constantly stay in line wi

If there are any significant operational difficulties envisaged by AIFMs in complying with the draft guidance (Annex 1 of CP 145),

please provide brief details, including any possible solutions if appropriate.

Response:
No comment.

Additional data in support of any of your responses to the previous questions.

Response:

If you have any further thoughts or considerations on the proposals outlined in Consultation Paper 145, please share them below.

Whilst, we do not believe that a 50% leverage limit should be introduced, we would point out that as the guidance currently stands, the proposed introduction of the leverage limit is somewhat confusing. It appears the leverage limit shall only be considered a "binding limit" the year after the fund had first exceeded a leverage threshold of 50%. We request clarity therefore as to whether the 50% limit existing under the proposed guidance is being suggested to operate as a guiding limit from a technical perspective.

In our view the intended scope of the guidance is also unclear. It is unclear whether the "indirect" references included in the paper extend to:

1. leverage arrangements that benefit the AIF directly or indirectly;
2. leverage arrangements of the AIF in respect of direct or indirect holdings.

In the event the Central Bank intend to incorporate leverage arrangements pertaining to underlying entities (i.e. scenario (i) above), we believe it is necessary for the guidance to stipulate whether the rules are to be applied on a combined or respective entity basis.

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