EFAMA

European Fund and Asset Management Association

# EFAMA RESPONSE TO THE EUROPEAN COMMISSION'S CONSULTATION ON THE REVIEW OF AIFMD

29 JANUARY 2021

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EU transparency register: 3373670692-24

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## INTRODUCTION

The AIFMD is one of the pillars of EU regulation for investment funds, which will be crucial to the development of the Capital Markets Union (CMU) and the post Covid-19 economic recovery in the European Union.

The Commission's Report to Council and Parliament assessing the application and the scope of Directive 2011/61/EU on alternative investment fund managers provides a balanced analysis leading to the conclusion that, overall, the AIFMD regime is working well**.** Against this solid analysis, also underpinned by the conclusions of the report mandated to KPMG, EFAMA calls on the European Commission **to follow a set of three overarching principles** when reviewing the AIFMD framework to ensure that the framework is adequately revised without undermining the foundations on which the framework stands:

- **Don't fix something that is not broken**: The ongoing review of AIFMD should be targeted only at addressing material shortcomings which are clearly demonstrated and that cannot otherwise be addressed through supervisory convergence or Level 2 harmonisation;
- **Keep the AIFMD a "manager" regulation**: The AIFMD was designed as a "manager" regulation, and not as a "product" regulation, because the alternative investment fund management sector is too diverse to include in a regulation product-specific rules for each category of AIFs. It follows that NCAs need to have the required flexibility to appropriately supervise that diverse universe;
- **Focus on supervisory & enforcement convergence**: Effective supervision and enforcement across Member States is as important as ensuring consistency across national rules. We would encourage the European Commission to ensure that ESMA makes full use of the existing powers at its disposal (including enforcement powers at Level 4) to promote greater supervisory and enforcement convergence.

EFAMA therefore advocates for the European Commission to focus on a limited number of areas where targeted amendments to the AIFM Regulation could be introduced and calls on ESMA to make full use of its current powers to ensure supervisory convergence and effective enforcement throughout the European Union.

**AIFMD framework**

The AIFMD sets a high standard of harmonisation in the alternative investment fund management sector and ensures a consistent regulatory approach to potential risks of the financial system, better coordinated supervision, a high level of investor protection, and facilitates the market integration of EU AIFs.

We see the need for few targeted amendments through Level 2 and Level 3 to improve the effectiveness of AIFMD by avoiding different approaches at national level. Such targeted amendments will be further outlined in our consultation response. It is important in any case to ensure a consistent application of rules across Member States. In order to ensure a level playing field among AIFMs, NCAs should be bound to apply similar interpretations at national level.

**AIFM Passport**

EFAMA does not believe that the cross-border marketing and investor access rules for AIFs (as well as for UCITS) need to be reviewed, pending the application of the most recent amendments to both UCITS and AIFM Directives, published in June 2019. We note in particular that the amending Directive (2019/1160) is presently awaiting Member States' transposition and will only apply as from 2nd August 2021.

**Investor Protection**

The AIFMD provides a high level of protection to investors. The existing issues with access to AIFs for certain types of investors are rather linked to the very restricted manner in which MiFID has defined 'professional investors' very often excluding more sophisticated retail investors such as HNWIs, family offices and others from that definition. Consequently, it is difficult for these types of investors to access AIFs which may be more suitable to their particular investment needs. These necessary changes to the investor classification must be achieved through the upcoming MiFID II/MiFIR review, rather than through the AIFMD review as consistency with the former is of utmost importance. To address this issue, the creation of a fourth client category should be avoided in order to keep the current processes and procedures unchanged; instead the requirements to qualify as 'professional investor' should be lowered.

Given that AIFs are generally aimed at professional investors, flexibility must be given to AIFMs to provide relevant and meaningful information to their investors. We must avoid a situation, as is currently the case with MiFID, where retail investor-type disclosures are mandated for all types of clients. This leads to a situation where non-relevant information is disclosed to professional investors and eligible counterparties without taking into account that bilaterally agreed and more targeted information is already being provided.

**AIF Retail Passport**

We believe that a passporting regime for retail AIFs is not necessary. Despite the existence of a retail AIF domestic distribution regime in a few EU jurisdictions, cross-border retail demand for AIF products remains low compared to other fund products (i.e. UCITS). By comparison, AIF products are naturally less standardised, requiring on average a higher degree of financial literacy, and are thus usually less suitable for the needs of retail investors. This is coupled with a greater degree of flexibility for AIFMs to invest and operate, compared with the UCITS limitations. In our view, these features remove the need for product regulation, and consequently for an AIF passport. In addition, we consider that UCITS already offers those retail investors a very wide range of different investment opportunities. These come with a recognised brand that third-party intermediaries and fund distributors are more familiar with when explaining their product features to investors. For retail investors looking to invest in less liquid asset classes – especially in view of longer-term investment returns – we believe that a preferred solution could become the ELTIF structure, once appropriately amended through the Commission's ongoing review of the ELTIF Regulation.

**Depositary Passport**

With respect to the introduction of a depositary passport, our views are resolutely against such option. Since the introduction of detailed depositary requirements with the AIFMD, as later mirrored to a large extent in the UCITS framework, we believe that the requirement for the depositary to share the same domicile as the fund is an important safeguard in the interest of investor protection. In the event of a loss of the fund's assets, or any investor harm provoked by the depositary's negligence or misconduct, legal certainty can only be enhanced by having the depositary in the same jurisdiction as the fund, allowing investors swift means of redress through any litigation and ultimately compensation. Proximity also better serves the depositary itself by facilitating its safe-keeping, oversight and cash monitoring duties, as well as all communication with the fund's managers and respective supervisory authorities. The latter are also able to carry out their supervisory mandate more efficiently, relying on the depositary to readily assist them while conducting inspections, examinations or enforcement actions *in loco*.

**International Relations**

Despite evolving in a competitive environment, the AIFMD succeeded to impose itself as a global brand for several reasons, among which delegation. As regards the latter, EFAMA believes that the AIFMD establishes a very clear and robust delegation framework, as further specified by its delegated Regulation 2013/231 (AIFMR). Article 82 thereof establishes a series of clear parameters against which a management company could be considered to be a "letter-box" entity. Such parameters are in our view exhaustive enough, striking an optimal balance between the twin objectives of investor protection and the preservation of a management company's need to structure its business as most appropriate when serving its investors.

**Macro-prudential tools**

The Covid-19 pandemic has demonstrated the resilience of the investment management sector as the industry has successfully managed the large outflows experienced during March 2020 stressed market conditions. It further reinforced EFAMA's longstanding view that the full set of Liquidity Management Tools (LTMs) should be made available in all EU jurisdictions. We would caution however against including restrictive definitions or rules on the deployment of LMTs. The ongoing development of industry standards reflect changes in markets and technology that appears to be more effective than rigid rules on how to apply these tools under stressed market conditions. The choice of tools must be always at the discretion of the manager because of existing different fund types and structures.

**Supervisory Reporting**

Our view is that the AIFMD regulatory reporting requirements have been working well so far and the framework has gone through various market events (euro crisis, Brexit referendum, COVID-19 March turmoil) without significant failure. In addition, from a worldwide competitiveness perspective, the EU must not generate new implementation costs for the industry – and for their ultimate investors – also in light of the uncertain outcome of the co-decision process.

As a way to improve the monitoring and supervision of AIFM activities in the EU, there are a number of opportunities for European (micro and macro) supervisory authorities to work on their own data-sharing practices, by allowing more efficient sharing and cross-referencing of data already provided by AIFMs (AIFMD, EMIR, detailed fund inventories received by central banks, detailed fund annual and semi-annual reports). EFAMA would encourage the European Commission to undertake further technical work with the support of industry experts.

**Leverage**

We believe that a matrix of leverage calculation metrics is the right approach in order to achieve a better representation of a fund's economic exposure on micro-level and allow regulators to draw the right conclusions for financial stability purposes. EFAMA firmly supports the current European regulatory framework, which has proven its risk-resilience and value through the diverse market events since the global financial crisis and is among the most advanced in the world.

**Sustainable Finance/ ESG**

The broader EU sustainability framework already introduces detailed rules on the integration of sustainability factors and transparency. As the new requirements remain to be defined and implemented, we do not find merits in tightening standards for AIFMs only. We recommend addressing the questions in this consultation after the effects of SFDR and the delegated regulation under UCITS and AIFMD can be assessed. This would enhance coherence, streamline the requirements, facilitate the implementation of the new rules, and support end-investors decisions with meaningful and reliable disclosures.

We recommend avoiding disproportionate requirements on AIFMs and adding compliance costs to those introduced by SFDR. AIFMs should retain the possibility to provide qualitative disclosures to investors. In addition, the integration of principal adverse impacts (PAIs) and other non-financial considerations in the investment process should always depend on the investment objectives and preferences of fund investors. Extending this obligation to any AIFM and potentially any product independently of its investment features may cause the manager to act against its fiduciary duties towards the investors.

**Supervision**

Although EFAMA supports greater supervisory convergence under the AIFMD framework, we are firmly opposed to attributing additional competences and powers to ESMA via the present AIFMD review. Through amendments to its founding regulation as part of the 2019 ESAs Review, ESMA has already received additional powers to foster convergence in the EU. As this reform only came into force in January

2020, we believe ESMA should rely firstly on these new tools to bring about greater convergence by using them to their full potential. In particular, actions by ESMA and the European Commission through their Level 4 powers would accelerate in practice convergence among regulators.

**UCITSD/AIFMD Merger**

Lastly, we are not in favour of the proposal to merge both Directives into a single EU regime**.** The existing body of norms for asset management companies is built on the recognition that fund product types differ substantially from one another other, as do their investor bases. The current difference between a product (UCITS) versus a manager (AIFM) Directive is thus justified in that it best reflects these differences. Worth noting is that a merger must be considered against the complexity of the current EU body of norms for asset management companies, including interdependent and very specific Level 2 and Level 3 measures. Any change at this stage will also inevitably distract considerable resources from the achievement of more important and pressing EU objectives.

## SECTION I: FUNCTIONING OF THE AIFMD FRAMEWORK

The central pillar of the AIFMD regulatory regime is a European licence or a so-called AIFM passport. EU AIFMs are able to manage and market EU AIFs to professional investors across the Union with a single authorisation. This section seeks to gather views on potential improvements to the AIFMD legal framework to facilitate further integration of the EU AIF market. The objective is to look at the specific regulatory aspects where their potential refining could enhance utility of the AIFM passport, gathering data on concrete costs and benefits of the suggested improvements, at the same time ensuring that the investor and financial stability interests are served in the best way. A number of questions focus on the level playing field between AIFMs and other financial intermediaries.

***Question 1. What is your overall experience with the functioning of the AIFMD legal framework?***

☐ Very satisfied

☒ Satisfied

☐ Neutral

☐ Unsatisfied

☐ Very unsatisfied

☐ Don’t know / no opinion / not relevant

***Question 2. Do you believe that the effectiveness of the AIFMD is impaired by national legislation or existing market practices?***

☐ Fully agree

☐ Somewhat agree

☐ Neutral

☒ Somewhat disagree

☐ Fully disagree

☐ Don’t know / no opinion / not relevant

***Question 2.1 Please explain your answer to question 2, providing concrete examples and data to substantiate it:***

| |
|---|
| Broadly speaking, the adoption of the AIFMD has introduced a strong level of harmonisation by imposing the same requirements across Member States, while giving access to the management and marketing passport. The framework has set out a high standard of harmonisation in the alternative investment fund management sector by ensuring a consistent regulatory approach to potential risks to financial stability, by a better co-ordinated supervision, a high level of investor protection and by facilitating the market integration of EU AIFs. In addition, several templates have been designed to |

harmonise the data and the format of information to be reported for review by ESMA. As a result, the framework for AIFMs (and indirectly for AIFs) is much more satisfying today than before the introduction of the Directive.

At the same time, there are still some areas where NCAs have maintained/added some national specificities, in particular regarding the distribution of AIFs at a national level. Difficulties are still encountered when marketing AIFs on a cross-border basis (even though the review of the cross border distribution of funds has addressed most of those issues). In particular, the level of fees charged by NCAs to passporting firms remains a cause of concern. We welcome the ongoing ESMA work on guidelines on marketing communications under the Regulation of cross-border distribution of funds to correct different local approaches on this subject[1]. In order to ensure a level playing field among AIFMs, NCAs should not apply stricter interpretations at national level. A consistent application of rules is crucial for a pan-European regime like the AIFMD.

A key request from our perspective – and as outlined further in our response - would be to make all liquidity tools set out in IOSCO's report[2] available to funds under stressed market conditions. ESMA has a major role to play – through its supervisory convergence powers – in building a single market by facilitating a common tool-kit and consistent interpretations among NCAs of the relevant EU rules. We would like to emphasise that national divergences do not require a reopening of the Level 1 to be solved; all issues identified in our response can be addressed either at Level 2 or Level 3.

***Question 3. Please specify to what extent you agree with the statements below:***

***The AIFMD has been successful in achieving its objectives as follows:***

| | 1 (fully disagree) | 2 (somewhat disagree) | 3 (neutral) | 4 (somewhat agree) | 5 (fully agree) | Don't know - No opinion - Not applicable |
|---|---|---|---|---|---|---|
| creating internal market for AIFs | ☐ | ☐ | ☐ | ☒ | ☐ | ☐ |
| enabling monitoring risks to the financial stability | ☐ | ☐ | ☐ | ☐ | ☒ | ☐ |
| providing high level investor protection | ☐ | ☐ | ☐ | ☐ | ☒ | ☐ |

[1] Please refer to ESMA's press release of 9 November 2020 on Fund's Marketing Communications.

[2] IOSCO's Recommendations for Liquidity Risk Management for Collective Investment Schemes, released on February 2018, available at the following link.

***Other statements:***

| | 1 (fully disagree) | 2 (somewhat disagree) | 3 (neutral) | 4 (somewhat agree) | 5 (fully agree) | Don't know - No opinion - Not applicable |
|---|---|---|---|---|---|---|
| The scope of the AIFM license is clear and appropriate | ☐ | ☐ | ☐ | ☐ | ☒ | ☐ |
| The AIFMD costs and benefits are balanced (in particular regarding the regulatory and administrative burden) | ☐ | ☐ | ☐ | ☐ | ☒ | ☐ |
| The different components of the AIFMD legal framework operate well together to achieve the AIFMD Objectives | ☐ | ☐ | ☐ | ☐ | ☒ | ☐ |
| The AIFMD objectives correspond to the needs and problems in EU asset management and financial markets | ☐ | ☐ | ☐ | ☐ | ☒ | ☐ |
| The AIFMD has provided EU AIFs and AIFMs added Value | ☐ | ☐ | ☐ | ☐ | ☒ | ☐ |

***Question 3.1 Please explain your answer to question 3, providing quantitative and qualitative reasons to substantiate it:***

Overall, EFAMA considers that the framework has been successful in achieving the objectives it was intended for. It has allowed a high level of harmonisation in many areas, notably the conditions required to be authorised as an AIFM in the EU and the corresponding requirements in terms of organisation, risk management policies and relationships with other stakeholders (as depositaries and external valuers). It has contributed to increase investor protection and has facilitated the cross-border distribution of EU AIFs across the EU (even if not totally satisfactory as mentioned below).

The risk management framework has also permitted to put in place a comprehensive set of rules. This framework is working well and has represented a significant progress in achieving the objective of financial stability. The market stress experienced during the pandemic constituted a "real life" stress test for the investment management industry and demonstrated the robustness of the current framework, including the effectiveness of ESMA's recent Liquidity Stress Testing Guidelines[3].

The initial costs for the effective implementation of those measures were quite significant, especially for the development of new reporting requirements which were totally new and imposed the use of a common format. The AIFMD regulatory framework has now been fully integrated in the running of management companies and both AIFMs and investors have adapted to its requirements. Further legislative and regulatory changes at this stage should be avoided as they could be disruptive to the necessary legal certainty and stability, and divert resources from the post Covid-19 recovery.

As noted below there are a number of opportunities for European supervisory authorities to address their own data architecture to allow more efficient sharing and cross-referencing of data already provided by AIFMs. We believe this approach would allow authorities to address many of the supervisory comments raised in recent years without imposing additional burdens on the industry.

***Question 4. Is the coverage of the AIFM license appropriate?***

☒ yes

☐ no

☐ Don't know / no opinion / not relevant

***Question 5. Should AIFMs be permitted to invest on own account?***

☐ yes

☒ no

☐ Don't know / no opinion / not relevant

***Question 5.1 Please explain your answer to question 5:***

Investment on own account – in the meaning of MiFID service – should not be allowed under AIFMD in order to avoid taking any proprietary investment risks or create conflicts of interest. Asset managers act as trustees for the investors of the funds they manage. Dealing on own account means trading against proprietary capital resulting in the conclusion of transactions in one or more financial instruments (Article 4(1) (6) MiFID II). In other words, dealing on own account takes place when a firm puts its own books at risks. Allowing asset managers to deal on own accounts would change their entire

[3] ESMA's Guidelines on liquidity stress testing in UCITS and AIFs, released on 16 July 2020, available at the following link.

business model and risk taking and present significantly different risks from the firm's perspective (e.g. conflict of interest) and from an NCA's perspective (e.g. financial stability).

For those reasons, we have not seen appetite amongst our members for AIFMs to be provided with the ability to invest on own account. However, it is important to draw a distinction between AIFMs investing on their own account and operations of the AIFM that may result in them holding small positions in their own AIFs, such as for seeding purposes (where a principal model is used for investors buying and selling units in an AIF). These are important functions for the management of AIFs and AIFMs should not be prevented from undertaking these. In our view, such activities do not constitute investment on own account within the meaning of a MiFID service.

***Question 6. Are securitisation vehicles effectively excluded from the scope of the AIFMD?***

☒ yes

☐ no

☐ Don't know / no opinion / not relevant

**Reasoning:**

EFAMA members are not aware of any issue of regulatory arbitrage possibilities regarding securitisation vehicles.

***Question 7. Is the AIFMD provision providing that it does not apply to employee participation schemes or employee savings schemes effective?***

☒ yes

☐ no

☐ Don't know / no opinion / not relevant

***Reasoning:***

Employee participation or savings schemes have always been an important aspect of organisation and management in companies based on national, labour, social and tax law. Various European governments have traditionally developed their own legislative arrangements to promote the involvement of employees. The exemption of these participation or savings schemes from the scope of the AIFMD ensures precise alignment to the local conditions in national markets – further clarifications in terms of ensuring alignment might however be needed.

***Question 8. Should the AIFM capital requirements be made more risk- sensitive and proportionate to the risk-profile of the managed AIFs?***

☐ yes

☒ no

☐ Don’t know / no opinion / not relevant

**Reasoning:**

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|---|
| Existing capital requirements already include this risk-dimension in both UCITS and AIFMD. We consider that the approach for asset management and banking institutions cannot be fully aligned as these entities do not perform the same types of activities. Key objectives for banking activities are to avoid over risk-taking while the mission of an asset manager is to act on behalf of its clients and to manage the right balance between risks taken and performance of the fund. Therefore there is no direct link between the risk exposure of the managed assets and the solvency of the manager’s balance sheet as they do not trade on the own books of the management company. The AIFM does not hold the assets of its clients and act only on their behalf. Capital requirements of the AIFM should therefore not be assessed by reference to the clients’ money. |

***Question 9. Are the own funds requirements of the AIFMD appropriate given the existing initial capital limit of EUR 10 million although not less than one quarter of the preceding year's fixed overheads?***

☒ yes

☐ no

☐ Don’t know / no opinion / not relevant

***Question 10. Would the AIFMD benefit from further clarification or harmonisation of the requirements concerning AIFM authorisation to provide ancillary services under Article 6 of the AIFMD?***

☐ Fully agree

☐ Somewhat agree

☐ Neutral

☒ Somewhat disagree

☐ Fully disagree

☐ Don’t know / no opinion / not relevant

***Question 10.1 Please explain your answer to question 10, presenting benefits and disadvantages of the entertained options as well as costs:***

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|---|
| The majority of EFAMA members believe that the UCITS and AIFM Directives are very clear as regards the scope of permitted activities. There is no need for any further legislative action. We are aware of diverging interpretations between NCAs concerning the scope of permissible business activities listed |

in Article 6(4) of the AIFMD and Article 6(3) of the UCITS Directive. However, as such, these provisions set out without ambiguity which activities AIFMs and UCITS management companies are authorised to perform. While greater harmonisation and a level playing field are worthwhile goals, we believe that these goals can be achieved without amending the AIFMD. Further convergence could be achieved at the level of NCAs with the support of ESMA.

***Question 11. Should the capital requirements for AIFMs authorised to carry out ancillary services under Article 6 of the AIFMD be calculated in a more risk-sensitive manner?***

☐ yes

☒ no

☐ Don’t know / no opinion / not relevant

**Reasoning**

In line with our responses above, we do not see any need to amend the current well-functioning regime. The current capital requirements applicable to asset management companies cover in a very strict way those risks that could occur in providing asset management activities. Changing calculation methods would not bring any added value and it would only create additional complexity. We are not aware that neither higher nor lower own capital requirements are needed to cover potential risks of ancillary services in a more risk sensitive manner.

***Question 12. Should the capital requirements established for AIFMs carrying out ancillary services under Article 6 of the AIFMD correspond to the capital requirements applicable to the investment firms carrying out identical services?***

☐ yes

☒ no

☐ Don’t know / no opinion / not relevant

***Question 12.1 Please explain your answer to question 12, presenting benefits and disadvantages of your suggested approach as well as potential costs of the change, where possible:***

There is no need to change a well-running system. The core services that MiFID firms provide are activities such as individual portfolio management, investment advice and reception and transmission of orders. Therefore, the capital requirements for MiFID firms need to reflect that engaging in these activities is the business purpose for these firms. It is quite different for AIFMs which perform collective portfolio management activities as their core services and only provide MiFID services as ancillary services.

The new K-factor approach developed under the investment firm framework is not yet tested in practice and will lead to an administrative burden in view of changing the calculation method, internal processes for calculation and monitoring. Moreover, the investment firm framework does not consider risk mitigating measures such as capital commitments given within a group by the parent company or coverage of risks through insurances and is still focusing on any risk-driving factors.

We do not believe there are any compelling reasons on which to base the need to change the capital requirements for asset managers.

***Question 13. What are the changes to the AIFMD legal framework needed to ensure a level playing field between investment firms and AIFMs providing competing services?***

***Please present benefits and disadvantages of your suggested approach as well as potential costs of the change, where possible:***

There is no need to make changes on this specific point, separate regimes should be maintained for the reasons mentioned previously. Being able to provide investment services with an AIFM license (as authorised today under AIFMD) should be maintained as the core activities of an AIFM relate to portfolio management and risk management. Adopting such an approach would result in much more constraining rules that would over-regulate AIFMs in view of the risks they generate and in the nature of their activities.

AIFMs and UCITS management companies are already subject to requirements very similar to MiFID in terms of governance, process, etc. We do not see any benefit in submitting AIFMs/UCITS management companies and MiFID firms to identical requirements. AIFMs/UCITS management companies authorised to perform the additional but limited number of MiFID functions must perform those activities on an ancillary basis, and this is the key difference with the performance of those activities by MiFID firms as core and unique business.

It is important to consider the different core businesses and services of investment firms and those of management companies, where the latter cannot execute orders on behalf of clients, nor dealing on own account.

***Question 14. Would you see value in introducing in the AIFMD a Supervisory Review and Evaluation Process (SREP) similar to that applicable to the credit institutions?***

☐ yes

☒ no

☐ Don’t know / no opinion / not relevant

***Question 14.1 Please explain your answer to question 14, presenting benefits and disadvantages of your suggested approach as well as potential costs of the change, where possible:***

Introducing a complex supervisory and assessment framework such as the SREP would only be justified in the event of clearly established failures in the governance and management of risk by AIFMs. Continued regulatory focus on ensuring a consistent approach to substance in management companies already requires their detailed focus on risk management and controls, including ongoing operational risk. In practice, management companies regularly provide detailed information to their NCAs on governance and controls framework as part of existing ongoing supervisory review processes under the AIFMD. As such the AIFMD already provides a comprehensive governance and supervisory framework suited for the agency business model of AIFMs. We are not aware of failures in the AIFMD supervisory oversight regime which warrant significant change.

Furthermore, the SREP is essentially designed to assess the risks arising on a group consolidated basis rather than on a solo firm basis and as such is ill suited to the make-up of many firms. Those AIFMs which are part of a wider group are likely to be already subject to some form of consolidated oversight under CRDV, Solvency II or IFD/IFR. Hence the incremental regulatory benefits of extending the SREP to AIFMs would be minimal compared to the cost of implementation.

It is important to understand that firms cannot isolate the SREP from a series of other detailed requirements which need to be in place before a SREP can commence. The typical steps leading to a SREP, drawing from members' experience in applying the CRD process, include:

- Pillar 1 required capital assessments

- Pillar 2 internal assessment of the firm's market risk, credit risk, operational risk and other risks (for which it may not hold capital), based on the firm's own risk methods for modelling risk (with guidance on the methods from the NCA and ongoing review of industry standards). This is achieved through an Internal Capital Adequacy Assessment Process ('ICAAP'). This process, which is required to be fully documented sets out how the firm intends to mitigate identified risks and how much current and future capital is necessary having considered other mitigating factors. Under CRD, this is generally produced on an annual basis. The ICAAP is a time-consuming process taking many months and several hundred hours of FTE time to produce.

- Still under Pillar 2, the SREP is then the process by which the relevant NCA reviews the firm's internal methods. A typical SREP process will require several hundred hours of FTE commitment, including by senior staff, to produce and complete, as well as significant time commitment by NCAs to review and assess, including follow up testing of the assumptions put forward in the SREP and review of internal procedures.

- This process is accompanied by detailed Pillar 3 disclosures which also require several hundred hours of FTE commitment to produce disclosures to the required standard.

Taken together these steps will be extremely burdensome, particularly in terms of time commitment and need for additional headcount, by both AIFMs and NCAs alike to run such a process.

***Question 15. Is a professional indemnity insurance option available under the AIFMD useful?***

☒ yes

☐ no

☐ Don't know / no opinion / not relevant

***Question 15.1 Please explain your answer to question 15, presenting benefits and disadvantages of your suggested approach as well as potential costs of the change, where possible:***

| |
|---|
| Provided that the professional indemnity insurance option is clear and transparent, we believe it should be kept as it is used by a number of specialist AIFMs. Multiline AIFMs, on the other hand, tend to have additional own funds to cover potential liability risks given the underwriting procedure is more complex for their activities.<br><br>Professional indemnity insurances are an effective tool in their management of risks and a recognised instrument for reducing risk-based contributions to the investor compensation scheme. |

***Question 16. Are the assets under management thresholds laid down in Article 3 of the AIFMD appropriate?***

☒ yes

☐ no

☐ Don’t know / no opinion / not relevant

***Question 17. Does the lack of an EU passport for the sub-threshold AIFMs impede capital raising in other Member States?***

☐ yes

☒ no

☐ Don’t know / no opinion / not relevant

***Question 17.1 Please further detail your answer to question 17, substantiating it, also with examples of the alleged barriers:***

| |
|---|
| The fact that the EU passport is not available to sub-threshold AIFMs means that the marketing options available to these types of AIFMs are more restricted.<br><br>However, sub-threshold self-managed AIFs can opt into the AIFMD regime or, for example, appoint a third party AIFM, which may ensure compliance with the AIFMD in a professional way, hence helping smaller AIFs to develop best practices and have access to the EU passport. It is important to note that National Private Placement Regimes (NPPRs) need to remain in place until a valid alternative solution to access cross-border markets is found. |

***Question 18. Is it necessary to provide an EU level passport for sub- threshold AIFMs?***

☐ yes

☒ no

☐ Don't know / no opinion / not relevant

***Question 18.1 Please explain your answer to question 18:***

It would be difficult to strike the right balance between a regime that would allow sub-threshold AIFMs to have access to a EU-wide passport and a regime that would guarantee sufficient investor protection. Notwithstanding this, the introduction of a passport would certainly mean a higher level of regulation, which would rather be a burden for sub-threshold AIFMs than an opportunity.

It is therefore our belief that most sub-threshold AIFMs would opt out from such a passport regime, where possible.

***Question 19. What are the reasons for EuVECA managers to opt in the AIFMD regime instead of accessing investors across the EU with the EuVECA label?***

Please explain your answer:

We outline some of the possible reasons below:

- The EuVECA manager expects to exceed the relevant thresholds in the near future, and rather than submitting itself to two application and approval processes, (s)he opts immediately for the AIFMD regime;

- The EuVECA manager wants to manage funds with the EuVECA label in an EU jurisdiction different to its home Member State;

- The EuVECA manager wants to offer its investors products that fall outside the parameters of the EuVECA label (e.g. funds that invest more than 30% of their capital in non-qualifying investments): a EuVECA manager can only market EuVECA funds, but a fully authorised AIFM can market other types of AIFs;

- Funds marketed by a fully authorised AIFM could be more appealing to certain investors as there could be a perception that they are more stringently supervised.

## SECTION II: INVESTOR PROTECTION

The AIFMD aims to protect investors by requiring AIFMs to act with the requisite transparency before and after investors commit capital to a particular AIF. Conflicts of interest must be managed in the best interest of the investors in the AIF. AIFMs must also ensure that the AIF's assets are valued in accordance with appropriate and consistent valuation procedures established for an each AIF. The AIF assets are then placed in safekeeping with an appointed depositary that also oversees AIF's cash flows and ensures regulatory compliance.

Questions in this section cover the topic of investor categorisation referencing to MiFID II, stopping short of repeating the same questions that have been raised in its recent public consultation on MiFID II, rather inviting comments on the most appropriate way forward. Views are also sought on the conditions that would make it possible to open up the AIF universe to a larger pool of investors while considering their varying degrees of financial literacy and risk awareness. Examples of redundant or insufficient investor disclosures are invited.

Greater clarity on stakeholders' views of the AIFMD rules on depositaries is sought in particular where such rules may require clarification or amending. The introduction of the depositary passport is desirable from an internal market point of view, but stakeholders are invited to propose other potential legal solutions, if any, that could address the issue of the short supply and concentration of depository services in smaller markets.

**Question 20. Can the AIFM passport be improved to enhance cross-border marketing and investor access?**

☐ Yes

☒ No

☐ Don't know / no opinion / not relevant

**Question 20.1 If so, what specific measures would you suggest? Please explain your suggestions, presenting benefits and disadvantages as well as potential costs thereof, where possible:**

**Question 20.1 Please explain your answer to question 20:**

At present, we see no need for the cross-border marketing and investor access rules for AIFs (as well as for UCITS) to be reviewed through further legislative actions, pending the application of the most recent amendments to both UCITS and AIFM Directives published in June 2020. We note in particular that the amending Directive 2019/1160 is currently undergoing Member State transposition and will only apply as from 2 August 2021. Once transposed and fully effective, it is imperative for such requirements (as well as those of the accompanying Regulation 2019/1156) to be interpreted consistently by NCAs.

EFAMA has welcomed the resulting amendments to both the AIFM and UCITS Directives, in particular, the definition of a pre-marketing regime for AIFs, the clarification of de-notification requirements for both AIF/UCITS funds, the creation of enabling facilities for retail investors, alongside the removal of local agent requirements, completed by greater transparency for management companies on each jurisdiction's marketing requirements. We believe it is largely premature for the Commission to consider additional amendments to the AIFMD (and possibly even to UCITS Directive) until the provisions emerging from the latest amendment round have been adequately transposed and applied.

However, there remain a few challenges to the marketing passport which can be met through a series of targeted clarifications by ESMA. For instance, there is no clarity in relation to Article 30a(2) of the recent amending Directive 2019/1160 concerning the start of the 18-month period for the pre-marketing of AIFs, within which any subscription shall be considered to be the result of marketing and trigger the relevant notification requirements.

### a) Investor classification and investor access

***Question 21. Do you agree that the AIFMD should cross-refer to the client categories as defined in the MIFID II (Article 4(1)(ag) of the AIFMD)?***

☒ Yes

☐ No

☐ Don’t know / no opinion / not relevant

***Question 21.1 Please explain your answer to question 21:***

Client categories should be the same throughout all EU financial services legislations to create much needed alignment and avoid additional red tape. Instead of envisaged changes in AIFMD, MiFID II should be the basis for the client categorisation and AIFMD should only cross-reference the relevant MiFID articles.

This is important, as the current MiFID categories lack granularity in order to account for the different needs of different investor groups. This ‘one size fits all’ approach and missing granularity are especially detrimental for AIFs which cover a large variety of fund structures with very different risk profiles (ranging from genuine hedge funds employing high amounts of leverage or short selling to (nationally) regulated long-only bond funds adapted to the prudential needs of regulated investors such as insurance companies or banks).

Please also see our respond to Question 22 below.

***Question 22. How AIFM access to retail investors can be improved? Please give examples where possible and present benefits and disadvantages of your suggested approach as well as potential costs of the change:***

We do not see an outright issue with access for retail investors to AIFs, but rather an issue within MiFID which has ‘cordoned off’ more sophisticated retail investors (HNWIs, family offices, etc.) from being considered as professional under certain predefined conditions, thus making it harder for these types of investors to access AIFs which may be more suitable to their particular investment needs.

To allow these investors easier access to AIFs, we see a distinctive need for more flexibility within the existing MiFID client categories. If the Commission believes that AIFMD should cross-refer to the client categories as defined in the MIFID II, it is necessary to revise the current conditions for investors to be opted up to professional status in the upcoming MiFID II/MiFIR review. Of essential importance for AIFs is that the number of transactions to be undertaken in each calendar year must be lowered for investors in well-diversified and/or illiquid AIFs, as it is highly unlikely that they will undertake 10 transactions per quarter/40 transactions per year.

In our reply to the recent MiFID consultation, we have therefore advocated for increasing the current number of conditions to be classified as professional investor from three to four. Two (or more) would have to be met before a retail client could be considered eligible to opt-up to professional status. The four conditions EFAMA proposes are:

- Amend the current ‘10 transactions per quarter and 40 transactions per year’ criterion to 20 transactions over the previous year. In addition, a lower threshold should be considered for diversified funds and for illiquid instruments (e.g. two illiquid transactions in the previous year).
- Reduce the threshold of the client’s portfolio from currently EUR 500,000 to EUR 200,000.
- The wording of the “sufficient financial knowledge and/or experience” criterion should also refer to “a master-level diploma (or higher) in economics or finance, or has managed a portfolio of more

than EUR 500,000 over the last five years, or has worked in fields that involve financial expertise for at least one year, or has gained other similar experience".

- Add a fourth criterion that the client has or wishes to undertake a transaction in a financial instrument of over EUR 100,000.

In addition, improvements to the current ELTIF framework could also make these AIFs more attractive for retail investors (as well as AIFMs). In particular, the eligible asset classes and investment strategies should be reviewed and expanded to e.g. allow fund of fund structures or clarify the eligibility of investments outside Europe. Also, it should be considered whether the ELTIF framework covers all desirable strategies.

***Question 23. Is there a need to structure an AIF under the EU law that could be marketed to retail investors with a passport?***

☐ Yes

☒ No

☐ Don't know / no opinion / not relevant

***Question 23.1 Please explain your answer to question 23:***

ELTIFs, EuVECAs and EuSEFs can already be marketed to certain retail investors (i.e. with a passport under certain conditions). For the time being, we do not see a need to expand this to other types of AIFs under the existing EU frameworks. In line with our comments on the ELTIF framework in our response to Q22, we could see the following improvements to ELTIFs that could make them more accessible to retail investors:

- Remove the minimum subscription amount of 10,000 euros or the 10% investment limit of a portfolio of financial instruments in ELTIF funds for a retail investor whose portfolio of financial instruments does not exceed 500,000 euros.

- Allow management companies to decide whether an ELTIF fund can be set up as an open fund (with subscription/redemption windows during its lifetime, but less frequent than for UCITS: e.g. weekly, bi-monthly or monthly).

- Reduce the proportion of long-term assets to allow the fund to be more liquid: long-term assets must represent at least 50% of the fund's assets;

- Remove the threshold preventing the ELTIF from investing more than 10% of its capital in the same company, the same physical assets or the same fund in order to facilitate progressive investments if the fund is an open-ended fund.

- Set up liquidity risk management mechanisms (e.g. by setting up gates, side pockets, swing pricing mechanisms, adjustable entry and exit fees);

- Remove the possibility of cancelling the subscription within a period of two weeks which does not correspond to an open distribution mode of the funds.

- Of course, an ELTF fund open to non-professional investors could only be marketed within the framework of existing MiFID investment advice.

Creating dedicated AIFs for retail investors would necessitate subsequent product regulation which is currently not envisaged by AIFMD. The current approach which allows Member States to decide on allowing non-national funds to be marketed in their jurisdiction is working well. This allows national authorities to decide on a case-by-case basis whether a particular AIF should be distributed to retail investors or not. This works well, as some types of AIFs can be more complex than UCITS, we believe it is right to leave the decision on distribution with the national authorities.

EFAMA believes that a passporting regime for retail AIFs would not be justified. Despite the existence of a retail AIF distribution regime in a few EU jurisdictions domestically, cross-border retail demand for AIF products remains low compared to other fund products (i.e. UCITS). The latter in fact already offers retail investors a very wide range of different investment opportunities, supported by a recognised brand that third-party intermediaries and fund distributors are familiar with when explaining its product features to investors.

As the AIF product is on average far less standardised than UCITS and requires a higher degree of financial literacy (where financial literacy in the EU remains on average still too low), demand in certain Member States has been limited to high net-worth individuals, bordering the professional investor category. Absent In the absence of sufficient EU-wide demand, considerations around a retail AIF passport and the consequent conversion of the existing AIFMD regime into a product one on par with UCITS are in our view unwarranted. Instead, as a more viable mean of offering EU retail investors access to alternative, less-liquid and longer-term asset classes, we believe that a fundamentally revised ELTIF – already built around a "product" regulation and promising to become more accessible to retail investors – has a role to play.

In other terms, we view product regulation as a necessary precondition for the establishment of a passport. To function, the latter must count on an even landscape that the required flexibility of the AIFMD for alternative asset managers should not allow by design. Moreover, we favour the current approach which allows Member States to decide on allowing foreign funds to be marketed in their jurisdiction. This allows NCAs to decide on a case-by-case basis whether a particular AIF should be distributed to retail investors or not. This approach is working well, with the decision on an AIF's distribution remaining with the NCA.

### b) Depositary regime

**Question 24. What difficulties, if any, the depositaries face in exercising their functions in accordance with the AIFMD? Please provide your answer by giving concrete examples identifying any barriers and associated costs.**

EFAMA would prefer to let depositaries and their representative bodies answer this question in greater detail.

***Question 25. Is it necessary and appropriate to explicitly define in the AIFMD tri-party collateral management services?***

☐ Yes

☒ No

☐ Don’t know / no opinion / not relevant

***Question 25.1 Please explain your answer to question 25:***

We do not see a need for a more precise definition, especially as tri-party collateral management services are not used broadly across the asset management industry.

When they use tri-party services, asset managers managing EU regulated funds (including AIFs) frequently seek to improve fund returns throughout securities financing transactions. The associated transactions create a credit exposure for the lender (also referred as the “Collateral Receiver”) to the borrower (also referred as the “Collateral Provider”) and triparty collateral administration supports the efficient collateralisation to mitigate such credit exposure.

Besides mitigating such credit exposures, we welcome the entry into force of the AIFMD Delegated Regulation of 12 July 2018, applicable since April 2020 that introduces the obligation for the depositary to perform a reconciliation as often as is necessary between its internal accounts and registers and those of a third party to whom the depositary has delegated the custody function.

However, we consider that the reconciliation process should be refined, as the existing regime leaves ample room for interpretation. For example, we consider that reconciliation duties would not affect the ability of the depositary to perform its oversight and cash monitoring duties, as the depositary is already able to perform these obligations whatever the safekeeping regime applicable to assets. However, we believe the Commission could task ESMA to develop Level 3 guidelines to clarify reconciliation practices between counterparties, as these diverge between tri-party service providers and custodians.

***Question 26. Should there be more specific rules for the delegation process, where the assets are in the custody of tri-party collateral managers?***

☐ Yes

☒ No

☐ Don’t know / no opinion / not relevant

***Question 26.1 Please explain your answer to question 26, presenting benefits and disadvantages of your suggested approach as well as potential costs of the change, where possible:***

We think that the existing framework provides sufficient clarity and flexibility when defining roles and responsibilities between the various stakeholders. The implementation of the Commission Delegated Regulation 2018/1618 was a good opportunity to set a number of key principles and clarify a few practical points. Should there be a willingness to specify the delegation mechanism, we consider that the delegation process should be detailed in level 3 guidance, knowing that the responsibility and the obligation of return remain on the head of the depositary, and could not be transferred to the collateral manager in spite of such process.

Such guidance should provide details regarding certain aspects mentioned in question 27: (i) the flow of information between the tri-party collateral manager and the depositary the frequency at which the tri-party collateral manager should transmit and (ii) the positions on a fund-by-fund basis to the depositary in order to enable it to record the movements in the financial instruments accounts opened in its books.

***Question 27. Where AIFMs use tri-party collateral managers' services, which of the aspects should be explicitly regulated by the AIFMD?***

☐ obligation for the asset manager to provide the depositary with the contract it has concluded with the tri-party collateral manager

☐ the flow of information between the tri-party collateral manager and the depositary

☐ the frequency at which the tri-party collateral manager should transmit the positions on a fund-by-fund basis to the depositary in order to enable it to record the movements in the financial instruments accounts opened in its books

☒ **no additional rules are necessary, the current regulation is appropriate other**

☐ None of these topics should be tackled – it works well currently

***Please explain why you think the obligation for the asset manager to provide the depositary with the contract it has concluded with the tri-party collateral Manager should be explicitly regulated by the AIFMD.***

Article 83(g) AIFMR – Commission Delegated Regulation 2018/1618 as amended states that the "AIFM or the AIF transmits all relevant information or ensures the depositary has access to all the information it needs to fulfil its duties". We deem this sufficient for triparty services to not be explicitly regulated.

**Question 28. Are the AIFMD rules on the prime brokers clear?**

☐ Yes

☐ No

☒ Don't know / no opinion / not relevant

**Question 28.1 Please explain your answer to question 28, providing concrete examples of ambiguities and where available suggesting improvements:**

We refer the Commission to our answer to question 25 above.

**Question 29. Where applicable, are there any difficulties faced by depositaries in obtaining the required reporting from prime brokers?**

☐ Yes

☐ No

☒ Don't know / no opinion / not relevant

**Question 29.1 Please explain your answer to question 29, providing concrete examples and suggesting improvements to the current rules and presenting benefits and disadvantages of the potential changes as well as costs:**

| |
|---|
| We would defer to depositaries and their representative bodies answer this question in greater detail. |

**Question 30. What additional measures are necessary at EU level to address the difficulties identified in the response to the preceding question? Please explain your answer providing concrete examples:**

| |
|---|
| Please refer to our answer to the question above. |

**Question 31. Does the lack of the depositary passport inhibit efficient functioning of the EU AIF market?**

☐ Yes

☒ No

☐ Don't know / no opinion / not relevant

**Question 31.1 Please explain your answer to question 31:**

| |
|---|
| EFAMA does not see a need for the introduction of a depositary passport and believes that its continued absence will not affect the marketing of AIFs across the EU. We believe there is a reasonable equilibrium between having sufficient operators of scale and having a competitive choice of providers. Consequently we do not see the introduction of a depositary passport as a priority. |

**Question 32. What would be the potential benefits and risks associated with the introduction of the depositary passport? Please explain your position, presenting benefits and disadvantages of your suggested approach as well as potential costs of the change, where possible:**

| |
|---|
| The key risk we see in the introduction of a depositary passport is that of increased complexity in the supervision of European fund structures, with a potential negative fallout for investors. For instance, if introduced and implemented, a fund domiciled in jurisdiction A, may have depositary in jurisdiction B (using a global custody network) and a manager in jurisdiction C. In the event of a loss of assets, or any investor harm provoked by the depositary's negligence or misconduct, legal certainty in the interest of investors may not be guaranteed, as their means of redress through litigation and ultimately |

compensation or restitution will be substantially hampered by needing to file claims and other requests between three jurisdictions.

Having the depositary in a jurisdiction other than that of the fund's domicile would additionally complicate the effective supervision by the fund's NCA, as well as the depositary's oversight over the fund and its management company. The geographical proximity of the depositary to the fund's NCA facilitates the exercise of the latter's supervisory mandate, for instance, in the ease of access to the fund's representatives, as well as through ready opportunities to conduct inspections, examinations or investigate any possible misconduct *in loco*.

Moreover, we observe that a depositary located in a particular country may not be familiar with the fund domicile's legislative framework, and where present, additional costs are implied from having a foreign depositary developing such a presence and competency. Against the background of a non-harmonised custody, insolvency and securities legislation across EU Member States, a depositary passport would achieve contrasting results. In particular, investors in AIFs (but potentially also in UCITS as well) would stand to face uncertain regulatory outcomes, if not uneven treatments.

In relation to costs, those associated with the depositary's oversight of administration, transfer agency and management activities will increase, especially where the discharging of depositary services will occur cross border, not least due to tax complications depending on where the legal vs. beneficial ownership is located. Problems are deemed to arise also in light of differences between common law and civil law systems, adding to the difficulties of recognising cross border contractual agreements and their legal basis.

**Question 33. What barriers are precluding introducing the depositary passport? Please explain your position providing concrete examples and evidence, where available, of the existing impediments:**

The reasons cited in our response to Question 32 would count as "barriers" precluding the introduction of a depositary passport. To these, we add the consideration of varying national requirements for entities applying to be expressly authorised under a separate approval process as AIF depositories by different NCAs. These approval processes, and their relevant requirements beyond the few listed under Article 21(3) of the AIFMD, are currently not harmonised, with a potential to fundamentally complicate cross-border interactions between NCAs, depositories and AIFMs/AIFs.

The prospect of a depositary passport finally leads us to consider the quality of the interaction between the AIF, the AIFM and the appointed depositary. In light of the latter's fiduciary role in safe-keeping assets, monitoring cash-flows and overseeing the AIFM, interactions between the depositary and the AIFM/AIFs may suffer. To obviate such challenges, considerable expenditures to enhance communication and other system requirements will be necessary to ensure comparable outcomes in relation to what is presently available.

In conclusion, one should bear in mind that the depositary is ultimately an independent entity entrusted with the safekeeping over a fund's assets. In doing so, it offers independent governance and oversight over decisions made by the asset management company in the interest of a fund's investors. As mentioned, there is additionally a distinct advantage for local NCAs to have a depositary bank domiciled in the same jurisdiction as the fund. Any dilution of such safeguards through the introduction of a depositary passport could have a detrimental effect in the eyes of investors, while possibly also tarnishing the success of the AIFM/UCITS passports as a whole.

**Question 34. Are there other options that could address the lack of supply of depositary services in smaller markets? Please explain your position presenting benefits and disadvantages of your suggested approach as well as potential costs of the change:**

| |
|---|
| In our view, one option could consist in making use of the AIFMD passport by allowing an AIFM to establish a presence (e.g. through a branch) in the Member State where the appointed depositary is located and then launch locally-authorised AIFs. These could be marketed and sold back into the AIFM's "home" market through the product passport. This should be realised *pari passu* with reforms to simplify the opening of branches for UCITS/AIFMD/MiFID portfolio management services in "host" jurisdictions, especially in the leading European centres for depositary and fund administration services. In smaller centres, nothing would prevent smaller market players from building-up their expertise by specialising in asset classes and services to be discharged on a delegated basis (i.e. as sub-custodians).<br><br>Nevertheless, we fear that attempts to "push" a depositary passport away from the more developed and closely-regulated traditional fund domiciles will have important implications for investors themselves, in the form of less oversight over funds and their management companies by the appointed depositary, as well as by the fund's NCA over the latter. |

**Question 35. Should the investor CSDs be treated as delegates of the depositary?**

☒ Yes

☐ No

☐ Don't know / no opinion / not relevant

**Question 35.1 Please explain your answer to question 35, providing concrete examples and suggesting improvements to the current rules and presenting benefits and disadvantages as well as costs:**

| |
|---|
| With regard to the treatment of CSDs as "delegates" under the UCITS/AIFMD regimes, EFAMA is in favour of a clear recognition of the dual role CSDs can play as either "issuer" or "investor" CSDs.<br><br>Our views are consistent with our response to ESMA's 2016 Call for Evidence on asset segregation and custody services4. Only after the finalisation of the AIFMD, did it become apparent that certain CSDs (namely those offering ancillary services under a banking license) are competing with UCITS/AIF depositaries and their third party delegates by offering identical services, albeit on unequal terms. Such inequality stems from the fact that such CSDs are exempted under EU regulation from the strict liability requirements UCITS/AIF depositaries are intended to comply with under their respective Directives. In fact, there are currently no provisions in the CSDR that introduce a comparable and harmonised liability regime for CSDs, only national laws and regulations apply to a large degree .<br><br>Such "liability gap" becomes more clear when considering that certain CSDs become interposed as third-party agents in the custody holding chain by providing custody in relation to securities that are initially issued in another CSD, while offering a range of ancillary services in direct competition with |

[4] We refer to the EFAMA's Response to the ESMA's call for evidence on asset segregation and custody services, published on 23 September 2016, available at the following link.

those offered by UCITS/AIF funds' depositaries. Such "investor CSDs" are domiciled in local jurisdictions where they operate an Securities Settlement System (SSS), but only for a limited number of securities (either local securities or Eurobonds) and for which they also provide notary and/or central maintenance services (respectively points 1 and/or 2 of Section A of the Annex to the CSDR). In this capacity, they qualify as an "issuer" CSD, but for these few securities only.

Were UCITS/AIF securities to be lost at the level of an appointed CSD agent and where the latter is not clearly recognised as a "delegate" under the current UCITS/AIFM framework given that it is also considered as an "issuer" CSD for securities other than those belonging to the UCITS/AIF, the fund depositary may avail itself of the opportunity to prove that such loss has resulted from "an external event beyond its reasonable control, the consequences of which would have been unavoidable despite all reasonable efforts to the contrary". Where such test is convincingly proven and absent any further guarantees (e.g. in the form of privately negotiated general terms and conditions), a regulatory loophole would exist, implying fund end-investors would potentially not be able to claim any liability against the depositary. Such outcome would contravene the spirit and the EU Legislators' original rationale behind the depositary requirements under both UCITS and AIFM frameworks.

In light of these considerations, EFAMA would observe that certain CSDs are able to act in a dual capacity, i.e. as (i) an "issuer" CSD for a limited number of issues, while (ii) discharging competing services (i.e. as an "investor" CSD) in commercial competition with depositaries and their delegates (i.e. global custodians). In the absence of a comparable and harmonised liability regime for CSDs, the latter CSD types should therefore to be treated as "delegates" under UCITS/AIFM rules in a number of very clear and prescribed circumstances.

## c) Transparency and conflicts of interest

***Question 36. Are the mandatory disclosures under the AIFMD sufficient for investors to make informed investment decisions?***

☒ Yes

☐ No

☐ Don't know / no opinion / not relevant

***Question 37. What elements of mandatory disclosure requirements, if any, should differ depending on the type of investor? Please explain your position, presenting benefits and disadvantages of the potential changes as well as costs:***

As stated above, we are confident that the existing disclosures are sufficient for investors to make informed investment decisions.

This is especially true for the varied nature of AIFs and their investor base. Flexibility must be given to AIFMs to provide relevant and meaningful information to their investors. We must avoid a situation, as is currently the case with MiFID, where retail investor-type disclosures are mandated for all types of clients. This leads to a situation where non-relevant information is disclosed to professional investors and eligible counterparties without taking into account that bilaterally agreed and more targeted information is already being provided.

Professional investors, in particular those who are subject to prudential regulation (such as banks, insurance undertakings or pension funds), usually have very specific information needs vis-à-vis their asset managers. Given that they negotiate at 'eye level' with their AIFMs, they have the power to make sure that the AIFM provides tailored data matching their demand. For them, the generic information requirements according to Article 23 of the AIFMD have hardly any added value for investors but create administrative costs for the AIFMs. In general, the quality of disclosure has improved: the information document under Article 23 is generally of no value for professional investors who are interested in very specific type of information and often able to obtain it in the pee-launch phase of the fund. Hence, we believe that the obligation to provide the information under Article 23 to professional investors should be materially reduced. At least professional investors should be given the possibility to waive their information rights under this Article.

In addition, problems with competing EU rules occur: publicly offered closed-ended funds must not only produce investor information under Article 23 of the AIFMD but are, in addition, subject to the Prospectus regime. This results in duplication of information that creates unnecessary costs which ultimately need to be borne by investors. In order to safeguard equal standards for all AIFs, we believe that closed-ended funds should be excluded from the scope of the prospectus regime. Such exclusion would warrant application of a consistent set of rules for all investment funds of the same type.

For AIFMs wishing to access the retail market, we recommend using an improved ELTIF framework rather than creating a new framework. The ELTIF regulation already contains additional disclosure requirements that apply in case of retail distribution.

Any additional inconsistencies can be remedied by amending the respective disclosure rules in the AIFMD Level 2 Regulation.

***Question 38. Are there any additional disclosures that AIFMs could be obliged to make on an interim basis to the investors other than those required in the annual report?***

☐ Yes

☒ No

☐ Don't know / no opinion / not relevant

***Question 38.1 Please explain your answer to question 38, presenting benefits and disadvantages of the potential changes as well as costs:***

In our view, the current annual AIFMD disclosure requirements adequately satisfy investor needs. The current information required by Article 23 of the AIFMD and presented in the annual report is sufficient. We also do not consider it necessary to increase the frequency or scope of such disclosures.

In particular for professional investors, standardised additional information requirements are superfluous. Due to their nature, the relationship between management company and professional investors is open with an ongoing communication. Moreover, as long as these professional investors are subject to supervisory requirements themselves (such as banks, insurance undertakings), the management company provides these investors with additional information (investor reporting) so that they can fulfil their own reporting obligations based on their supervisory reporting requirements.

However, we take the opportunity to recommend some improvements to the current disclosures:

- Level 1 Regulation – Article 22(e) / Level 2 Regulation – Article 107: Whenever this type of remuneration is disclosed at the AIFM level, we recommend that AIFMs should not be mandated to disclose this information in each AIF's annual report, it rather should be sufficient, and is more appropriate, to indicate in the AIF's annual report where such information can be found, for example, by indicating the AIFM's website address. A similar approach is allowed under Article 434 of CRR, which states that institutions may determine the appropriate medium, location and means of verification to comply effectively with the disclosure requirements.

- Level 2 Regulation – Article 104(2): The requirements under this article for classification of 'realised gains on investments' and 'unrealised gains on investments' within 'Income' and 'realised loss on investments' and 'unrealised loss on investments' within 'Expense', conflicts with both the requirements of IFRS and general accepted accounting principles in Ireland and the UK, as realised losses and unrealised losses are considered to investment income in nature rather than an operational expense. There is also no accounting guidance on how to separately calculate unrealised gains and unrealised losses for the purposes of Article 104 of the AIFMR. This has resulted in divergent practices amongst industry participants and it could be argued that the inclusion of the disaggregation of gains and losses is of limited use to readers of financial statements. We would recommend such conflict and divergent practices are resolved by the presentation of gains/losses on investments in accordance with the requirements of the relevant AIF's accounting framework.

***Question 39. Are the AIFMD rules on conflicts of interest appropriate and proportionate?***

☒ yes

☐ no

☐ Don't know / no opinion / not relevant

## d) Valuation rules

***Question 40. Are the AIFMD rules on valuation appropriate?***

☒ yes

☐ no

☐ Don't know / no opinion / not relevant

**Reasoning:**

The AIFMD rules on valuation provide a robust framework to ensure that AIF assets are fairly valued and that subscriptions and redemptions are at a price that fairly reflects the value of the assets. Importantly, these rules also provide some flexibility in how the valuation is determined, recognising that valuation practices will vary for different asset types, while ensuring in each case there is strong governance on this process. AIFMs invest indeed in very different types of assets (listed and non-listed securities, liquid and illiquid, etc.) which obey to different valuation rules - it would not make sense to build a “one size fits all approach” for instance on valuation between a CTA Hedge Fund and Real Estate funds.

The requirements introduced by AIFMD involved some changes to internal procedures for AIFMs, in particular the establishment of an independent valuation function within the AIFM, typically overseen by a valuation committee to provide oversight of the valuation of the AIF, including where a valuation has been provided by an external valuer. This has provided additional robustness around the governance of the valuation process, ensuring greater protection for investors. With the industry having successfully adapted to the AIFMD valuation requirements, EFAMA does not believe there is any requirement to change the AIFMD valuation rules.

***Question 41. Should the AIFMD legal framework be improved further given the experience with asset valuation during the recent pandemic?***

☐ yes

☒ no

☐ Don’t know / no opinion / not relevant

**Reasoning:**

We do not believe that the AIFMD legal framework needs to be improved specifically further to the Covid-19 pandemic experience.

Overall, the governance of the valuation process proved robust during this period. Importantly, fair value processes were implemented when concerns arose around the accuracy of published price feeds, and ensured that other information sources were properly taken into account when determining valuations, ensuring that these represented the circumstances in the market as fairly as possible. Few funds chose to suspend dealing due to material uncertainty in the valuation of their assets, ensuring investors were protected from any disadvantage due to subscriptions and redemptions being processed at inaccurate prices.

As such, the recent pandemic has highlighted the robustness of the existing valuation requirements, and we do not believe that any changes are needed.

***Question 42. Are the AIFMD rules on valuation clear?***

☒ yes

☐ no

☐ Don’t know / no opinion / not relevant

**Reasoning:**

We believe that the AIFMD rules on valuation are overall clear. If anything, we would ask for Level 3 guidance if divergent interpretation across Member States have emerged.

***Question 43. Are the AIFMD rules on valuation sufficient?***

☒ yes

☐ no

☐ Don’t know / no opinion / not relevant

***Question 44. Do you consider that it should be possible in the asset valuation process to combine input from internal and external valuers?***

☒ yes

☐ no

☐ Don’t know / no opinion / not relevant

***Question 44.1 Please substantiate your answer to question 44, also in terms of benefits, disadvantages and costs:***

This is already the case under current rules. External valuers are helpful to perform the valuation of specific assets – e.g. real estate and infrastructure investments, which require experience from the local market. However, the use of external valuers should remain optional and at the discretion of the management company, and the ultimate responsibility for valuation should always remain with the management company.

***Question 45. In your experience, which specific aspect(s) trigger liability of a valuer?***

***Please provide concrete examples, presenting costs linked to the described occurrence:***

N/A

***Question 46. In your experience, what measures are taken to mitigate/offset the liability of valuers in the jurisdiction of your choice?***

***Please provide concrete examples, presenting benefits and disadvantages as well as costs of the described approach:***

Our members have different experience on this point. While in some jurisdictions, the AIFM takes responsibility for the overall valuation, through establishing a separate Valuation Committee which is independent of the portfolio function, in others, the AIFMs manage liability risks by performing extensive due diligence before appointing an external valuer to ensure that the proposed appointee is suitably qualified and meets regulatory requirements; monitoring the performance of the external valuer through close oversight on a day-to-day basis; or ensuring that the external valuer has professional indemnity insurance or a parental guarantee or similar in place to cover professional liability risks arising.

The adoption of Level 2 or Level 3 measures to help a common understanding of 'negligence' has to be interpreted as serious error of the external valuer.

## SECTION III. INTERNATIONAL RELATIONS

Considering the global nature of financial services, the AIFMD interacts with the third country regulatory regimes. By adopting the AIFMD the EU co-legislators sought to put in place a legal framework for tackling risks emanating from AIF activities that may impact the EU financial stability, market integrity and investor protection. The questions below are seeking views on where to strike the balance of having a functioning, efficient AIF market and ensuring that it operates under the conditions of a fair competition without undermining financial stability. Besides posing general questions on the competitiveness of the EU AIF market, this section seeks views on how the EU market could interact with international partners in the area governed by the AIFMD. The focus is on the appropriateness of the AIFMD third country passport regime and delegation rules.

***Question 47. Which elements of the AIFMD regulatory framework support the competitiveness of the EU AIF industry?***

Looking at the international landscape, it is worth noting that in other jurisdictions such as in the US and China, regulators have defined competitiveness as one of the key objectives to be achieved through fund regulation (beyond investor protection and financial stability), although it does not appear to be the case in Europe (at least not in such an explicit manner).

We have identified the following elements in the current AIFMD framework which support the competitiveness of the EU AIF industry:

- **Passporting -** The passporting mechanism for EU AIFMs sets the foundation for a level playing field within the internal market regarding distribution of EU AIFs (fund passport) as well as economies of scale in asset management (management company passport), and which contribute to promote the Single Market. It has become difficult for Member States to protect their local industry from competition from AIFMs domiciled in other Member States, at least as far as products for professional clients are concerned. The passporting rules require non-EU AIFMs wanting to access the EU market to adhere to regulatory standards similar to those for EU AIFMs and thus protect the latter from unfair third country competition.

- **Delegation -** The strength of the EU AIF industry is that a fund can be registered in one Member State while simultaneously being managed from several other Member States, or even from third countries, as AIFMs can have their portfolio management and risk management teams in different jurisdictions.

- **The "brand awareness" for AIFMD** - the coherent set of rules for alternative investment funds is increasing on a global level, creating the potential to evolve into a quality standard in the fund sector for regulators worldwide, along the lines of the UCITS brand.

- **Flexibility -** This has allowed NCAs to take into consideration the specificities of each type of AIF, contributing to the success of the AIFMD. Instead of imposing a too restrictive one-size-fit-all approach to all AIFs, it enables to maintain a wide of range of investment funds adapted to the various needs of end-investors.

***Question 48. Which elements of the AIFMD regulatory framework could be altered to enhance competitiveness of the EU AIF industry?***

***Please explain providing concrete examples and referring to data where available:***

On a global level, the European asset management industry is operating in an extremely competitive environment. EU AIFMs are competing with their peers from non-EU jurisdictions for investment opportunities as well as for investors.

The biggest threat to competitiveness of EU AIFs at this stage would consist in making significant changes to the existing AIFMD framework, which would divert resources, and disrupt the current balance.

Better harmonisation of supervisory requirements for cross-border activities could certainly help, removing the current bias by some NCAs which tend to impose more stringent substance requirement to cross border activities where entities belong to the same group. To this effect, it is also key that improvements to any supervisory reporting are designed in a way as not to impose more costs on the industry.

We would also welcome improvements to the ELTIFs regime to create a long-term sustainable label accessible to retail investors across the whole Single Market.

***Question 49. Do you believe that national private placement regimes create an uneven playing field between EU and non-EU AIFMs?***

☐ Yes

☒ No

☐ Don't know / no opinion / not relevant

***Question 49.1 If you believe there is an uneven playing field between EU and non-EU AIFMs, which action would you suggest to address the issue?***

***Please explain your choice, presenting benefits and disadvantages of the potential changes to the AIFMD as well as potential costs associated with your preferred option:***

At present, pending the entry into effect of the AIFMD "third-country passport" regime, we do not believe that national private placement regimes (NPPRs) create an uneven playing field.

By allowing third-country investors to invest in one or more EU Member States, these regimes can be beneficial to the domestic investor community as well, offering co-investment opportunities in the same structures. Moreover, NPPRs allow third-country AIFMs to market their AIFs to professional investors in a Member State, thereby competing against EU AIF products distributed in that same Member State. Non-EU AIFMs are however not subject to the same rules as EU AIFMs, although such potential advantage is in practice levelled by the fact that third-country AIFMs do not have access to a pan-EU passport, as well as by the fact that NPPR regimes may impose additional requirements on third-country AIFs when registered under a Member State's NPPR. We also observe that some Member States do not have NPPRs at all.

Despite these "playing field" considerations, EFAMA's view is that the Commission should not – in the interest of investors – amend NPPRs until the AIFMD's third-country access regime is effectively implemented.

***Question 50. Are the delegation rules sufficiently clear to prevent creation of letter-box entities in the EU?***

☒ Yes

☐ No

☐ Don't know / no opinion / not relevant

***Question 50.1 Please explain your answer to question 50:***

EFAMA believes the AIFMD establishes a very clear framework, as further specified by its delegated Regulation 2013/231 (AIFMR). Article 82 thereof establishes a series of clear parameters against which a management company could be considered to be a "letter-box" entity. Such parameters are in our view exhaustive enough, striking an optimal balance between the twin objectives of investor protection and the preservation of a management company's need to structure its business as most appropriate when serving its investors.

As a preamble to this and to the following delegation-specific questions, our concern is that ESMA has too often interpreted the legitimate practice of delegating investment management functions as a delegation of the management company's responsibilities. We find it important to observe from the outset of our delegation-specific responses to the questions below that such possibility is denied by the provisions under the AIFMD and would be contrary to our industry's best practices.

In its letter addressed to Commission vice-President Valdis Dombrovskis in August 2020, ESMA highlights instances where some management companies delegate a substantial part of their activities

– including their entire portfolio management and/or parts of their risk management ones – to third-party entities and questions, as a result, whether these management companies can still effectively monitor such third-party delegates and consequently calls for a series of far-reaching legal clarifications in the AIFMD[5].

The AIFMD already provides, however, an extensive set of general principles that prevent asset managers from becoming "letter-box" entities. Management companies have to notify their NCA before entering into a delegation agreement (Article 20 AIFMD). They cannot delegate their responsibilities or liabilities (Article 75(a) AIFMR). They can only delegate for "objective reasons" as defined by Article 76 of the AIFMR. They have to be able to effectively supervise the third parties to which they delegate (Article 75, letters (e) and (f), AIFMR). Last but not least, they cannot delegate to such an extent that they become "letter-box" entities as defined by Article 82 of the AIFMR. NCAs have therefore the powers to oppose delegation arrangements that would be contradictory to the letter of the AIFMD framework.

These EU-level provisions have been further elaborated by NCAs to provide extensive guidance to asset management companies operating in their jurisdictions in relation to the supervisory expectations delegating firms will be held accountable for when delegating investment management and/or other functions to third parties. For instance, such guidance is to ensure that management companies have sufficient resources, clear governance, and management and oversight arrangements to guarantee they retain the capacity to effectively supervise their delegates[6].

Delegation should not, in any case, be construed as a mean to create a "letter-box entity", nor used as a mean for management companies to circumvent their responsibilities under the Directive. Rather, delegation is performed bearing investors interests in mind, in line with their desired allocation preferences and risk/reward profiles, while realising all the operational efficiencies that inevitably ultimately translate into lower costs for investors. As such, delegation is indeed inherent to many business models, and management companies operating in several Member States rely on it to avoid cost and resource duplications while serving investors. Besides the critical need for an asset management company to source the best skills and leverage local investment expertise, efficiencies matter to an asset management company in many ways. For instance, one needs to consider the need of portfolio managers to execute numerous and often very large trades on behalf of investors by accessing deep pools of liquidity, where transactions costs – for the purpose of ensuring "best execution" in the interest of their clients – can be better managed and minimised by local delegates. Another example where delegates enhance the performance quality of a management company can be found in Article 3(g) of the Shareholder Rights Directive II[7] that requires asset managers to engage with, and exercise their voting rights attached to the shares of the companies in which they invest in order to maintain and enhance long-term value, with the aim of preserving or adding value to the clients' assets. EU management companies are not always in a position to engage with US or APAC companies to the same extent as appointed delegates in that region can.

We note that, while the claims in the ESMA's letter stem from ESMA's 2017 Opinion to support supervisory convergence in the area of investment management in the context of the United Kingdom

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[5] Please refer to ESMA's letter to Commission vice-President Valdis Dombrovskis, and more precisely to the section on the "Extent of delegation", page 5.

[6] As an example of NCAs' guidance in further specifying the AIFMD/AIFMR delegation rules (including substance requirements) and related supervisory expectations, please refer to the German BaFin's Circular 01/2017 (WA), the Central Bank of Ireland's Fund Management Company Effectiveness Guidance (CP 86) of 2016, or the Luxembourg CSSF's Circular 18/698.

[7] Directive (EC) 2007/36 of the European Parliament and of the Council of 11 July 2007 on the exercise of certain rights of shareholders in listed companies amended by Directive (EU) 2017/828 of the European Parliament and of the Council of 17 May 2017 as regards the encouragement of long-term shareholder engagement (text with EEA relevance) (Shareholder Rights Directive II – SRD II).

withdrawing from the European Union, they remain to be substantiated and confirmed[8]. ESMA does not refer in these two communications to specific cases or evidence suggesting that some management companies would be taking advantage of the current delegation framework to circumvent its requirements and spirit. We are also cognisant of the fact that, since May 2017, the ESMA's Supervisory Coordination Network (SCN) has discussed hundreds of "live" delegation and relocation cases submitted before it by member NCAs, with none, or potentially only very few, being challenged to the best of our knowledge. We logically conclude, therefore, that delegation has not been identified as an area of particular concern by the SCN[9].

The ESMA's letter therefore implies that a review of the AIFMD/AIFMR is required, without considering or explaining why the perceived shortcomings of the current delegation framework cannot alternatively be addressed by NCAs through better enforcement, accompanied by possible reviews of existing cooperation agreements between EU NCAs and their non-EU counterparts (including MoUs negotiated under the *aegis* of ESMA), or by promoting further convergence between NCAs relying on ESMA's existing toolkit. We note that the latter was only recently revised through amendments to its founding Regulation (EU) No 1095/2010, which came into effect in January 2020.

Proportionality, as described in Article 5(3) of the TEU, requires the EU to choose the measures that do not exceed what is necessary to achieve the pursued objective. It would therefore be incompatible with EU law to introduce legislative changes where supervisory convergence would result in an equivalent outcome. It is therefore crucial, under the EU Better Regulation Strategy, for the Commission to consider more accurate facts around delegation (both intra- and extra-EU) before introducing changes to the current delegation regime to ensure that the policy debate will be evidence-based.

***Question 51. Are the delegation rules under the AIFMD/AIFMR appropriate to ensure effective risk management?***

☒ Yes
☐ No
☐ Don't know / no opinion / not relevant

***Question 51.1 Please explain your answer to question 51, presenting benefits and disadvantages of the current rules and where available providing concrete examples substantiating your answer:***

AIFMD rules are appropriate to ensure effective risk management in the context of a delegation. The AIFMD not only introduces strong risk management rules requiring asset managers to put in place an extensive risk management system, but it also introduces delegation-specific rules to ensure that risk management remains effective following a delegation.

The risk management function under the AIFMD has undergone a significant transformation as it is no longer only a "control function" – contrary to what ESMA stated in its letter to the Commission – but a function fully integrated into the investment process itself (Recital 51 – AIFMR). In practice, the risk management function is involved in setting an AIF's risk profile and investment strategy; and these, in turn, inform investment decisions made by the portfolio management team and require the latter to

[8] We refer to ESMA's Opinion to support supervisory convergence in the area of investment management in the context of the United Kingdom withdrawing from the European Union, in particular paragraph 56 thereof.
[9] Please refer to ESMA's related press release of 29 May 2020, communicating the conclusion of the SCN's work by the end of 2020.

involve the risk management team in decisions that will have a significant impact on the risk profile of the AIF.

AIFMD rules on delegation complement risk management rules to ensure that delegation does not reduce the risk-management oversight over the portfolio management function. Article 75(b) of the AIFMR states that obligations towards the AIF and its investor remain unchanged, which implies that delegating asset managers have to maintain the same level of risk management oversight over their delegates than they would have over their own internal investment team. This notion is further reinforced by Article 75, letters (e) and (i), that require delegating management companies to maintain sufficient substance to supervise on an ongoing basis their delegates and to assess whether these delegates comply with their investment strategies (and thus to their risk-management policies).

Unsurprisingly, in the vast majority of cases, when asset managers delegate portfolio management functions, the risk management functions remain generally with the management companies. It entails that delegating management companies establish their own risk management policies, set their own risk limits, and take their own decisions regarding the minimisation and/or control of risk limits. Delegates can only be involved in ongoing risk measurement by, for instance, compiling statistics or providing other relevant information needed for risk measurement.

When delegating risk management functions, asset managers also face delegation-specific requirements to ensure that the delegates are competent and that the management companies retain part of their risk management functions. The delegating parties can only delegate to third parties authorised or registered for the purpose of asset management and subject to supervision (Article 78(2) AIFMR) which have the capacities and experience to conduct risk management activities (Article 77 AIFMR). Lastly, they have to keep sufficient substance to manage the risks associated with delegation (Article 75(f) AIFMR).

From these observations, we therefore find that there is a synergy between risk-management rules and delegation rules: Both sets of rules ensure (a) that the risk management function remains independent from the portfolio management function (Articles 44, 75(f), 82 AIFMR) and (b) that the risk management function has the capacity to supervise on a regular basis the portfolio management function (Articles 22, 39(a), 75, letters (e) and (f) AIFMR).

As NCAs have translated the contents of the AIFMD/AIFMR provisions into their own domestic regulatory requirements in greater detail, it is ultimately against such more granular risk, operational and conduct requirements that management companies will be held accountable by their NCA in the way they choose to delegate and oversee investment management functions. ESMA's considerations around diverging national requirements are legitimate, but these can be addressed more efficiently and proportionately by making full use of its existing powers, including common supervisory actions (CSAs) *inter alia*, to ensure that the existing AIFMD/AIFMR requirements are interpreted evenly by NCAs.

ESMA does not provide sufficient evidence to demonstrate that delegation, as it is currently regulated under the AIFMD/AIFMR framework, leads to improper oversight by the management company over its delegates. Absent further evidence or signs of clear market failures under the present AIFMD/AIFMR delegation framework, we believe existing rules are already adequate to realise a balanced outcome between preserving a management company's freedom to organise its agency business in the most advantageous and cost effective way, while exercising adequate oversight over its delegates for which it is ultimately responsible for.

***Question 52. Should the AIFMD/AIFMR delegation rules, and in particular Article 82 of the Commission Delegated Regulation (EU) No 231/2013, be complemented?***

☐ Yes
☒ No
☐ Don't know / no opinion / not relevant

***Question 52.1 Should the delegation rules be complemented with:***
*Please select as many answers as you like:*

☐ quantitative criteria
☐ a list of core or critical functions that would be always performed internally and may not be delegated to third parties
☐ other requirements

*Please explain why you think the AIFMD/AIFMR delegation rules should be complemented with* ***quantitative criteria****, presenting benefits and disadvantages of the potential changes as well as costs:*

EFAMA strongly opposes the insertion of quantitative criteria into Article 82 of the AIFMR.

Such requirements should remain strictly qualitative so as to not remove the AIFMR's flexibility to adapt to various delegation arrangements, reflecting the diversity of management companies, both in terms of size and operational complexity.

In its August 2020 letter addressed to the Commission, ESMA advocates for the introduction of quantitative criteria – we assume for instance a minimum number of full-time employees (FTEs) – or alternatively a list of critical/core functions for the delegating management company to abide by. We believe such criteria or minimum list of critical/core functions do not provide the sought after "clarifications" ESMA believes are required as a mean to curb "excessive" forms of delegation. Instead, they introduce additional requirements that are not justified in the absence of convincing proof.

In relation to strict quantitative criteria, we note these would inevitably fail to account for the diversity of the investment management industry, as characterised by a diversity of size, corporate structures, business models, investment strategies, etc. More specifically, they would disrupt certain managers' operations quite significantly by artificially duplicating resources away from where they are most needed, and typically, in global financial centres. For instance, introducing in the AIFMR a new rule according to which every delegating management company should at least keep three FTEs (based on the recommendation enclosed in ESMA's aforementioned 2017 Opinion) on their payroll could potentially force asset management companies (especially smaller ones) to employ more staff than their business model would otherwise require. Moreover, such rule would necessarily overlook key qualitative criteria, like a staff member's seniority and experience. There would be no distinction made between employees in terms of their qualifications, experience and skills. Employees with more seniority are likely to be better prepared to adequately supervise and challenge a delegate than a junior employee whose access to the delegate and experience is likely to be more limited. As a result, in such a situation, it can be argued that a better outcome for the delegating management company would be to have two senior employees, rather than one senior and two junior ones.

Lastly, the current framework should be preserved as it also gives NCAs the flexibility they need to tailor their substance requirements to each delegating management company, depending on their respective specificities.

*Please explain why you think the AIFMD/AIFMR delegation rules should be complemented with **a list of core or critical functions**, presenting benefits and disadvantages of the potential changes as well as costs:*

As for quantitative criteria, we strongly object to the inclusion of a list of core or critical functions that, in ESMA's view, would deserve to be always performed internally and not be delegated to third parties. From ESMA's abovementioned letter, we understand the justification remains the same, i.e. to seek legal "clarifications" to prevent management companies from delegating too many of their functions (thus becoming "letter-box" entities).

Firstly, this list could undermine the internal market by limiting intra-EU delegation across borders. Management companies in the EU rely extensively on delegation, especially firms who have operations in two or more countries and which want to avoid the costs of replicating services country by country in relying on one or two centres of excellence. This might no longer be possible in some cases following the introduction of a minimum list of functions which should always be performed internally.

Secondly, from a competitive perspective, we believe that a closed list of core or critical functions would favour the "super management company" model, where both collective portfolio and individual portfolio management sit within a same large, consolidated legal entity. In addition, it would render more burdensome the operation of other alternative organisational models, which exist in the European market such as those where member firms consolidate management of individual segregated accounts and accounts on behalf of AIFs in a single entity such as another management company or in a MiFID investment firm to provide economies of scale. Lastly, it would also most likely prevent "white labelling" as an important service for the European investment management industry, especially for smaller asset managers/investment boutique firms choosing the services of a third-party management company to free-up resources and focus on capital raising and portfolio management. This legislative change would therefore sensibly further consolidate the internal market, reduce competition, as well as investor choice in national markets to the advantage of large and well-established incumbents.

Thirdly, asset management is by its very nature a global business. To meet investor demands in terms of offering them access to a broader set of investment strategies, asset classes, and exposures, as well as to best manage investment risks through greater portfolio diversification and offer products at lower costs, the continued delegation of portfolio management and related functions is of critical importance. A minimum list could undermine the possibility for management companies to have access to the expertise in third-country financial centres such as London, Hong Kong, or New York, to name only a few.

Delegation also allows management companies to better diversify their portfolio, allowing certain portions (or "sleeves" of it) to be managed by delegating portfolio management functions to foreign group subsidiaries or third-party entities. Portfolio managers generally need to be close to the markets and in the same time-zone where they directly invest on behalf of their investors. Hence, EU management companies often need to delegate portfolio management to third-country financial centres, ensuring their investors' access to the local expertise. Absent delegation, or with access to third-country portfolio managers significantly restricted, EU management companies would either no longer be able to access certain asset classes for their investors altogether, or offer an approximation of the required exposure at a far higher cost, given several inefficiencies (e.g. less engagement with investee companies, information gaps, shallower liquidity and resulting higher trading costs, etc.).

As a result, and for EU AIFs in particular, these would become less attractive investments for European (and non-European) investors alike and ultimately also less competitive worldwide. With limited exposures to non-EU assets, EU AIFs are expected to provide poorer diversification and future returns to investors. With less funds on offer allowing investors to access foreign markets, European investors are likely to have to invest solely in AIFs managed out of the EU on less efficient terms, or authorised non-EU AIFs sold under national private placement regimes. Foreign investors, on the other hand, may have to consider disinvesting from EU AIFs were these to be no longer managed as efficiently as before.

Moreover, we note that many EU management companies have subsidiaries or parent entities in third-country jurisdictions that provide portfolio management to both their subsidiaries/parent entities and local clients. Management companies in this situation will have to relocate their activities in the EU in order to comply with a potentially new AIFMD delegation framework, thereby potentially forfeiting some of their business in third countries. As an example, a European management company through its Tokyo offices manages Japanese equity portfolios for EU-based investors, as well as for large local clients (i.e. Japanese pension funds), whose assets are booked in that same jurisdiction. Were this large European firm to relocate its affiliated Tokyo portfolio managers to Luxembourg on the back of critical/core function requirements as ESMA has recommended, the results would be at least two-fold: a) investors in EU-domiciled Japanese equity funds will likely face higher costs and sub-optimal returns through Japanese equities being managed out of Paris or Frankfurt instead; and b) the management company's subsidiary will have to forcefully sever its investment mandate with its large Japanese pension fund clients. We therefore care to note in this respect that non-EU financial hubs also serve other clients, not only EU-based investors.

These consequences for the investment management industry would be further exacerbated by the fact that some third-country jurisdictions might either try to replace the EU as a domicile for funds or emulate the EU by adopting similarly restrictive measures. It is possible that jurisdictions such as China will tighten EU funds' access to their jurisdictions by adopting restrictive measures. One can also refer to the regulatory projects in place in Switzerland and the UK to attract assets managers and/or funds domiciled in the EU[10].

Non-EU management companies might also decide to end their operations in the EU should their EU AIFMs no longer be able to delegate to their foreign headquarters to avoid a duplication of costs. Many non-EU asset managers have group entities established as AIFMs and ranges of EU-domiciled funds taking advantage of several other EU hubs providing leading administrative, depositary, and legal services. With stricter delegation rules, they would have to reconsider whether they should continue to operate in the EU as AIFMs and domicile their funds in the EU. This would reduce competition in the EU investment management industry and undermine the European fund products, notably also UCITS.

In conclusion, the current framework should not be reviewed to introduce a list of core or critical functions that would be always performed internally and may not be delegated to third parties. Such list does not provide the sufficient flexibility to take into account the important diversity characterising the EU asset management industry and would imply negative consequences for all parties with a stake in our industry.

[10] Please refer to the initiative to introduce a new fund category in Switzerland, the Limited Qualified Investor Fund (L-QIF), and the initiative by the United Kingdom to review its tax treatment of asset holding companies in alternative fund structures.

*Please explain with what **other requirements** the AIFMD/AIFMR delegation rules should be complemented, presenting benefits and disadvantages of the potential changes as well as costs:*

Introducing new delegation rules in the AIFMD framework, such as extending the delegation regime to "supporting tasks" or introducing restrictions on "seconded staff" proposed by ESMA, stands to also damage the good functioning of the investment management industry.

Firstly, interpreting Article 82(d) of the AIFMR as an interdiction for assets managers to delegate "a substantial margin" of their entire portfolio management and/or risk management functions, as per ESMA's 2017 Opinion, would upend management company business models significantly. As outlined in our response to Question 50, extensive delegation is required for certain funds such as those seeking unique exposures, or in the case of white-label funds relying on the expertise of a third-party management company. Any prohibitions or restrictions in this regard would inevitably reduce investment opportunities for EU investors and play to the advantage of the largest market incumbents from a competitive viewpoint.

Secondly, extending the delegation regime's requirements to "supporting tasks" when they are closely associated with collective portfolio management should also be resisted. There are myriads of ancillary functions across a management company's value chain that are associated with portfolio management: risk models & analytics, order management and trade execution systems, cash & position reconciliation systems, fund accounting & administration, performance calculation, fund reporting, transfer agency services, even depositary services. These are currently considered as "administrative functions" under Annex I AIFMD. Management companies are allowed to outsource these functions as they see fit while bearing the primary responsibility for selecting and overseeing these delegates/third party vendors. Moreover, we note that recital (82) of the AIFMR expressly states that "supporting tasks like administrative or technical functions assisting the management tasks" should not be deemed to constitute delegation of AIFM functions. An attempt to re-locate such functions to adhere to the delegation requirements intended for investment management functions – as the August 2020 ESMA letter to the Commission appears to suggest – would thus cause massive disruptions to say the least, let alone for those services that are offered by providers forming natural oligopolies (like ICT).

Thirdly, introducing restrictions on "seconded staff" would also deserve a clearer justification. Secondment is a critical element in the way management companies structure their operations. Although only a temporary feature of how management companies structure themselves, secondment provides firms with vital experience for key projects and initiatives, such as transitions and implementation of regulatory changes. Management companies should remain free to second key staff/specialist staff as they see fit. Any restriction placed on secondments, including the location of where a secondee works, would not be welcomed as it is after all a temporary appointment, related to a project or the replacement of an approved person with another approved person.

Fourthly, introducing strict requirements on "white labelling" would also be counterproductive. White labelling is important for the investment management industry because it allows small asset managers/investment boutiques firms to focus on developing innovative investment products, while relying on a third-party management company for administrative tasks, regulatory compliance, and risk management. Allegedly, the need to regulate "white-labelling" practices stem from the fact there is a potential conflict of interest between the third-party management company and its client (e.g. a small investment boutique firm) when the latter would be deemed too important (for instance, by contributing significantly to the delegating company's bottom line). While recognising the potential for conflicts of interest to arise between these actors, the third-party management company is already required to address such (potential) conflicts of interests in the best interest of the investors, in line with Article 14 of the AIFMD and Articles 30 to 37 and Article 80 of the AIFMR. Therefore, offering a "white label" service is more a question of adhering to the existing delegation requirements of the AIFMD, instead of a matter related to one or more clients' relative importance for the third-party management company.

***Question 53. Should the AIFMD standards apply regardless of the location of a third party, to which AIFM has delegated the collective portfolio management functions, in order to ensure investor protection and to prevent regulatory arbitrage?***

☒ Yes
☐ No
☐ Don't know / no opinion / not relevant

***Question 53.1 Please explain your answer to question 53:***

The current delegation regime strikes the right balance between being too permissive and imposing a fully-fledged extra-territorial application of the AIFMD regime by ensuring that non-EU delegates comply with a comparable level of regulation, while allowing EU management companies to delegate to non-EU jurisdictions. We therefore believe that the current standards are appropriate, regardless of the location of a third party delegate and notwithstanding whether the latter is part or not of the management company's group.

There are indeed sufficient guarantees under the current AIFMR framework to ensure that non-EU delegates comply with the AIFMD standards. The relevant requirements are those included between Articles 75 and 82 of the AIFMR. Effectively, these offer two levels of control over the delegate; i.e. at the level of the delegating management company, and at the level of the authorising NCA. Delegating asset managers unequivocally retain the responsibility for the activities delegated and contractual obligations are included and specified in the delegation arrangements to ensure that the delegate comply with the relevant AIFMD standards (i.e. ensuring thereby an indirect compliance with the AIFMD framework). Indeed, Article 20(3) of the AIFMD clearly provides that "the AIFM's liability towards the AIF and its investors shall not be affected by the fact that the AIFM has delegated functions to a third party", so that an EU management company will not delegate (e.g. the collective portfolio management function) to a third party when it may expose him to such liability risks, and will therefore carefully consider the quality and effectiveness of the delegate's regulatory framework. Moreover, the delegating party is required to regularly supervise and monitor the delegate, for example through Service Level Agreements (SLAs) and/or Key Performance Indicators (KPIs), to ensure that the delegate complies with these standards. Finally, NCAs, when assessing delegation arrangements, scrutinise the existence of an "objective reason" behind the delegation and that the delegating entity has the capacity to effectively monitor the delegate, against a backdrop of exchange of multilateral information and cooperation agreements being in place between EU NCAs and their foreign counterparts.

We do not believe that an extra-territorial application can be implied from the above question as it refers to AIFMD "standards" and not to more specific requirements. However, we would like to stress that we would be opposed to any extra-territorial application of the AIFMD and wish to elaborate on some of the inevitable implications of requiring non-EU delegates to comply with the letter of the AIFMD framework. In this case, EU management companies would struggle to find delegates in third countries as the pool of potential delegates would undoubtedly shrink. Eligible delegates would have to operate in accordance with AIFMD requirements either by fully complying with the AIFMD for all their activities, including local ones, or setting up a specific entity to provide services to EU management companies. Fewer potential delegates would increase operational costs for EU management companies and their clients, while undermining AIFMs' access to financial expertise in foreign financial centres, as well as their ability to effectively meet their clients' exposure and diversification specifications by investing in non-EU assets. Moreover, EU AIFs' competitiveness worldwide would also suffer, since managing these funds will become less cost-efficient and no longer offer the same level of diversification *vis-à-vis* non-EU funds.

Lastly, we would like to highlight that it is not because a third-country service provider does not comply with the letter of the AIFMD that the rules it must comply with are of a lesser quality or inconsistent with those applied in the EU. Where compliant with global standards (as those of IOSCO[11]), it is important to not assume that because rules are different they do not achieve the same outcome.

It is therefore believed that the AIFMD framework should provide sufficient flexibility to allow EU management companies to delegate to third-country entities, while expecting the former to effectively monitor the activities of the delegates. This flexibility could be ensured by leaving NCAs the power, when they review a delegation authorisation request, to assess whether the delegates can comply with rules comparable to the AIFMD ones, while making full use of the mechanisms and procedures foreseen under their respective cooperation arrangements with their third-country peers. Presently, there does not appear to be concerns around access to supervisory data between supervisors based on existing multilateral memorandums of understanding between non-EU and EU NCAs, leading us once more to question the need for such potentially far-reaching changes to existing "Level 1" or "Level 2" requirements in the manner outlined by ESMA[12].

***Question 54. Do you consider that a consistent enforcement of the delegation rules throughout the EU should be improved?***

☐ Yes

☒ No

☐ Don't know / no opinion / not relevant

***Question 54.1 Please explain your answer to question 54, presenting benefits and disadvantages of the current rules and where available providing concrete examples substantiating your answer:***

Effective and consistent enforcement is key to ensure that the delegation regime functions properly since NCAs are given leeway when deciding whether delegation arrangements comply with the AIFMD framework.

In line with our response to the questions above, we argue that there is no sufficient evidence at our disposal to suggest that, at present, NCA enforcement actions have found management companies to be in breach of delegation requirements. Indeed, according to the ESMA report on sanctions, there were only two enforcement cases in 2019 related to a breach to the AIFMD delegation framework[13]. This report, interpreted together with the findings from the ESMA SCN, indicates a high-level of compliance from the asset management industry with the AIFMD delegation rules. We encourage nonetheless NCAs to maintain high-levels of enforcement in their respective Member States as enforcement has a critical role to play in ensuring that delegation rules are respected.

When it comes to improving the AIFMD delegation framework, we believe that the focus should rather be put on supervisory convergence as, according to ESMA in its letter to the Commission, there are instances where delegation has been interpreted differently by NCAs. To achieve greater convergence around these interpretations, we wish to reiterate that ESMA should firstly make full use of the tools at its disposal, including guidelines, to ensure a consistent assessment of delegation structures across the Union. Alternatively, it could set up a "peer review committee" or a "coordination group" based on

[11] IOSCO's Principles Regarding Cross-border Supervisory Cooperation, released in May 2010, available at the following link.

[12] In this regard, EFAMA welcomes the recent publication of the Multilateral Memorandum of Understanding concerning consultation, cooperation and the exchange of information between each of the EEA competent authorities and the UK Financial Conduct Authority, on 4 January 2021, available at the following link.

[13] We refer to ESMA's first annual report on the use by National Competent Authorities (NCAs) of sanctions under the Alternative Investment Fund Managers Directive (AIFMD), released on 12 November 2020, and particularly to section 5.3.

its amended founding Regulation (in force as from January 2020) to foster greater supervisory convergence in the way NCAs go about implementing the AIFMD/AIFMD's delegation requirements in their respective markets.

ESMA could, for instance, start by ensuring greater supervisory convergence on delegation-specific topics related to white labelling, marketing, and procedures and controls in place in individual AIFMs as regards due diligence process, skills and expertise of staff, and governance aspects.

***Question 55. Which elements of the AIFMR delegation rules could be applied to UCITS?***

*Please explain your position, presenting benefits and disadvantages of the potential changes as well as costs:*

We do not believe that the AIFMR delegation rules should be applied to UCITS at this stage, especially in light of the potential wide-ranging changes that the AIFMD Review might introduce. Furthermore, we reiterate that, to the best of our knowledge, the ESMA's SCN did not identify material problems with the current delegation regime even though it reviewed hundreds of 'live' cases, including ones related to UCITS.

Moreover, we also note that changes advocated for by ESMA, namely introducing quantitative criteria or a list of core functions that could not be delegated, would, for the reasons outlined in our previous responses, not only deprive UCITS investors of important diversification opportunities, but it would also undermine the UCITS global brand. We therefore conclude that it is too early for a revamp of the UCITS delegation rules; the Commission should rather focus on more urgent matters, as outlined in the rest of our response.

## SECTION IV: FINANCIAL STABILITY

One of the main objectives of the AIFMD is to enable supervisors to appreciate and mitigate systemic risks building up in financial markets from different sources. To this end, AIFMs are subject to periodic reporting obligations and supervisors are equipped with certain market intervention powers to mitigate negative effects to the financial stability that may arise from the activities on the AIF market.

The section below invites opinions whether the intervention powers and a tool-kit available to the relevant supervisors are sufficient in times of severe market disruptions. Shared views on the adequacy of the AIFMR supervisory reporting template will be important in rethinking the AIFM supervisory reporting obligations. According to the FSB report, markets for leveraged loans and CLOs have grown significantly in recent years exceeding pre-crisis levels (FSB, Vulnerabilities associated with leveraged loans and collateralised loan obligations (CLOs), PLEN/2019/91-REV, 22 November 2019). While most leveraged loans are originated and held by banks, investment funds are also exposed to the leveraged loan and CLO markets. In order to assess risks to the financial stability and regulatory implications associated with leveraged loans and CLOs it would be commendable to continue collecting the relevant data and monitoring the market. The stakeholders are invited to cast their views on the matter. With particular regard to the loan originating AIFs, suggestions on the optimal harmonisation of the rules that could apply to these collective investment vehicles are welcome. Finally, questions are raised whether leverage calculation methods could benefit from further standardisation of metrics across the AIF market and potentially also across the UCITS for the supervisors to have a complete picture of the level of leverage engaged by the collective investment funds.

## a. Macroprudential tools

***Question 56. Should the AIFMD framework be further enhanced for more effectively addressing macroprudential concerns?***

☐ Yes

☒ No

☐ Don't know / no opinion / not relevant

**Question 56.1 Please explain your answer to question 56:**

EFAMA believes that the AIFMD provides a strong framework for effectively addressing macroprudential concerns, as this has been demonstrated by the Covid-19 outbreak. At the first peak of the pandemic, the EU investment fund industry has faced a significant deterioration in liquidity in particular in some market segments (funds that were invested in less liquid assets, such as corporate HY bonds and EM bonds, property funds and Money Market Funds (MMFs)) along with large-scale investment outflows. Despite these market pressures – mostly driven by the overall stressed market liquidity conditions and not the underlying credit-quality or structure of the funds – the vast majority of funds were able to maintain their portfolio structure when meeting redemptions with no direct public support implemented or directed to investment funds. Funds redemptions were not met by cash holdings but vertical slices of portfolio, providing a proof point that there was available liquidity across the assets.

In this real-life stress test the sector operating under the currently liquidity and risk management regime has proven its overall resilience.

In the limited cases of suspensions (0.4% of funds according to an ESMA Report[14]) it is important to note the relevant challenges (i.e. valuation) and the link to the overall market turmoil prior to drawing conclusions and identifying causes solely linked to the liquidity profile and mismatches at the level of these funds.

We note from the ESMA Report mentioned above that there are still some funds which have not updated their redemption policy with their liquidity profiles and as an industry we look forward to engaging with our members and policy makers on how to address this behaviour. We also point out that in March 2020 the industry was half way through the process of implementing the recommendations of ESMA LST Guidelines[15] and EFAMA is aware that a lot of work has gone in EFAMA's members to fully operationalise ESMA Guidelines, and include lessons from the crisis in the stress scenarios.

This does not mean being complacent: we are keen in drawing the right lessons from the crisis which need to be considered in an appropriate manner, i.e. focusing on those types of funds that have experienced pressures, and taking a holistic approach, i.e. understanding that the pressures were linked not to idiosyncratic characteristics of the funds' sector but rather to the overall extreme market

[14] ESMA's Report – Recommendation of the European Systemic Risk Board (ESRB) on liquidity risk in investment funds, released on 12 November 2020, available at the following link.
[15] ESMA's Guidelines on liquidity stress testing in UCITS and AIFs, released on 16 July 2020, available at the following link.

volatility. A holistic approach also means collecting and assessing data across the non-bank sector, not just the investment fund sector where there is already extensive data provision.

We fully acknowledge the need of regulators to further assess the conditions and circumstances of the market turmoil and have access to appropriate and sufficient data to analyse those and where necessary update supervisory mechanisms. One area to explore further is coordination amongst NCAs in their data request to management companies. The feedback received from members is that management companies have often to send same data sets to different public authorities (NCAs, NCBs, ESRB, ECB). During the COVID-19 outbreak, those operating open-ended funds on a cross-border basis had to provide to multiple public authorities financial flow data following ad hoc and uncoordinated requests, putting additional pressure on those teams handling the crisis.

A better data sharing between Central Banks and Securities Regulators, could be improved at national and EU levels and changes in this regard should take place, at the Level 2 or Level 3 with the consequence of reducing supervisory burden on management companies and, as a result, reducing costs for investors.

The recent crisis has contributed to accelerating the adoption of LMT tools in jurisdictions where they were not yet available. This has been one of the longstanding EFAMA's position to make sure the IOSCO toolkit is available in all EU jurisdictions both to minimise systemic risks and assist in the fair treatment of investors[16]. Some national supervisors have encouraged and facilitated the use of LMTs, which proved again to be very helpful to tackle redemption shocks.

We would caution however against any restrictive definitions or rules on the deployment of LMTs in the AIFMD framework. The ongoing development of industry standards reflect changes in market and technology that appear to be more effective than rigid rules on how to apply these tools in a stress market conditions. It must be at the discretion of the manager of the funds which tools they want to use because of very different fund types and structures.

Finally, we would call for caution against new macro-prudential policies that are not adequate for the asset management business model. It should be kept in mind that requiring the use of similar tools triggered under the same circumstances or centralising the decision over LMTs would end up enhancing pro-cyclicality risks instead of promoting effective risk management. It would also become an important constraint for market finance which in turn would lead to further market pressures and impact financial stability.

***Question 57. Is there a need to clarify in the AIFMD that the NCAs' right to require the suspension of the issue, repurchase or redemption of units in the public interest includes financial stability reasons?***

☐ Yes

☒ No

☐ Don't know / no opinion / not relevant

[16] Please refer to the Joint EFAMA/AMIC Report on liquidity stress testes in investment funds, published on 6 January 2019, available at the following link.

***Question 57.1 Please explain your answer to question 57, presenting benefits and disadvantages of the potential changes to the existing rules and processes as well as costs:***

EFAMA believes that there is no need for clarification as under the current framework. Article 46(2)(j) of the AIFMD provides that NCAs shall have the power to “require the suspension of the issue, repurchase or redemption of units in the interest of the unit-holders or of the public”. The notion of public interest is intended to include the concept of “financial stability”.

On the other hand, we would stress that risk management is a function that is directly linked to specific investment strategies and therefore cannot fit either into a one-size fits-all approach nor be based on a prescriptive approach from the regulator. It requires discretion at the asset manager’s level along with adequate transparency as to the tools used and effective supervision from the regulators.

The macroprudential tools provided for in Articles 25 and 46 of the AIFMD should be reserved by NCAs only for conditions of extreme market stress. These should not be deployed on a “business as usual” (BAU) basis as it is likely to both constrain and undermine European AIFs.

In terms of transparency, we fully agree that NCAs need to be informed and notified of any suspensions of redemption by the asset management companies (as it is the current practice), while the decision to suspend redemption in an AIF is most appropriately undertaken by the Board of the AIFM or the AIF, after having taken all considerations into account. By definition, suspension is only used in exceptional and unpredictable circumstances, where either the volume of redemption requests has been significantly higher than anticipated or liquidity of the portfolio assets has been significantly lower than expected.

Suspension by NCAs is already known under Article 84(2)b) of the UCITS Directive where a Member State may allow the competent authorities to require the suspension of repurchase or redemption of units if this is necessary in the interests of unit-holders or the public, even if the UCITS has not itself contemplated any suspension. For instance, the competent authorities could require a suspension in the event of severe political, economic or social disruption likely to have a distorting effect on the transferable securities market. However, the aim of supervision of financial stability is already addressed by Article 25 of the AIFMD where competent authorities are required to act for reasons of financial stability after consulting with ESMA.

***Question 58. Which data fields should be included in a template for NCAs to report relevant and timely data to ESMA during the period of the stressed market conditions?***

***Please provide your suggestions, presenting benefits and disadvantages of the potential changes as well as costs:***

Stressed conditions are by nature different. Hence any template drafted *ex ante* would defeat the purpose of reporting ‘relevant’ data as their relevance can change according to the specific market conditions. The risk is to transform such data gathering into a regular exercise, of little use during real stressed situation.

During the March/April disruptions, NCAs have asked for additional data mostly in relation to significant extraordinary events and very large redemptions. This mechanism has proved to work well and does not require any changes to the AIFMD reporting. Standard reporting would bring less value than a reporting that is tailored to the actual event.

NCAs as well as European securities regulators and banking supervisors should develop tools both to better exchange information among themselves, and to better exploit all the sources of data which are accessible and already reported (AIFMD Reporting, EMIR, etc. as well as fund inventories, fund prospectuses, fund annual reports and semi-annual reports).

***Question 59. Should AIFMs be required to report to the relevant supervisory authorities when they activate liquidity risk management tools?***

☐ Yes

☒ No

☐ Don't know / no opinion / not relevant

***Question 59.1 Please explain your answer to question 59, providing costs, benefits and disadvantages of the advocated approach:***

We welcome increased transparency in the use and availability of LMTs and in particular during times of stressed market conditions and we acknowledge this can substantially help regulators reach timely decisions. Management companies already inform their NCAs when they activate LMTs to ensure that NCAs remain updated in real time about market developments (this is also well covered by ESMA LST Guidelines requiring AIFMs to notify NCAs of material risks and actions taken to meet redemption requests in normal and stressed conditions). A distinction should, however, be made on the basis of the LMTs. There are a number of LMTs which are used on a regular basis (i.e. swing pricing) and requiring notification every time they are activated would put an important, and ultimately unnecessary, supervisory burden on the investment management industry. Only those LMTs – such as redemption suspensions – used to face adverse market conditions, should be notified to the competent supervisory authority. No ex ante notification for the use of ordinary LMTs foreseen in the funds' documentation/rules should be required.

***Question 60. Should the AIFMD rules on remuneration be adjusted to provide for the de minimis thresholds?***

☐ Yes

☒ No

☐ Don't know / no opinion / not relevant

**Reasoning:**

Proportionality allows smaller and simpler management companies to disapply quantitative remuneration thresholds and certain pay-out structures that would otherwise be burdensome at the same time as offering no systemic or investor risk mitigation.

The Commission's intention seems to be to harmonise AIFMD and UCITS proportionality requirements with banking rules enshrined in CRD/R V, and soon the IFD/R, that grant smaller banks and investment firms an exemption on a 'de minimis' (small) balance-sheet basis.

The banking approach is not designed to properly consider the specificities of the different business model of asset managers and the characteristic risks associated to their categories of staff and pay structures. Other than banks, management companies commonly have different risk profiles, based on differing investor bases, risk appetites and risk horizons. Similarly, business models and structures typically vary from those in banks, and correspondingly management companies can have different pay structures.

Particularly since the management company is not dealing on its own balance sheet, the criteria must be formulated differently and be based on the already applied principle-based requirements of the AIFMD and UCITS Directive specified by ESMA in its remuneration guidelines for asset managers. Moreover, such sector-specific remuneration requirements are already recognised by the banking government rules in the context of group consolidation (cf. Article 109(2), (4) and (5) CRD V). In particular, CRD V states that the banking remuneration requirements (including de minimis thresholds) set out in Directive 2013/36/EU (CRD) should not apply on a consolidated basis to subsidiaries which are not institutions (such as asset managers).

We would like to highlight that it is crucial to maintain a distinction between remuneration rules for fund management companies (under AIFMD and UCITS) and those for other financial services firms (e.g. under CRD/R V, IFD/R and Solvency II).

The current rules are already well-suited to management companies and AIFMs, and work well.

The Commission should not simply import rules relating to the size of bank, investment firm and insurer balance-sheet across into the non-balance-sheet / agency world of fund management in the way this consultation seems to be doing.

## b. Supervisory reporting requirements

***Question 61. Are the supervisory reporting requirements as provided in the AIFMD and AIFMR's Annex IV appropriate?***

☐ Fully agree

☒ Somewhat agree

☐ Neutral

☐ Somewhat disagree

☐ Fully disagree

☐ Don't know / no opinion / not relevant

***Question 61.1 Please explain your answer to question 61:***

The supervisory reporting requirements as provided in the AIFMD and AIFMR's Annex IV are mostly appropriate. Changes to the Annex IV Reporting template would have significant costs implications - including data sourcing, aggregation, editing XML for both the managers, and the NCAs consuming the data. Those costs and adaptations should not be underestimated due to the interconnection of the various IT systems.

Resources (notably in IT and development teams) should not be mobilised on limited added-value developments whereas the current economic context requires the effective contribution of the whole financial industry on projects that will foster economic recovery and access of market participants to effective financing and/or investment solutions.

It is worth reiterating that management companies provide further information on their activities in individual fund inventories which are transmitted to several Central Banks and in fund annual and semi-annual reports. NCAs should use these reports and make sure that they have access to the data collected by Central Banks.

We acknowledge that further consistency in reporting requirements across Member States would be welcomed, and we encourage the European Commission – together with technical experts from the industry and NCAs – to undertake a gap analysis on the basis of current European and national reporting obligations management companies are subject to, before introducing any changes at this stage.

***Question 62. Should the AIFMR supervisory reporting template provide a more comprehensive portfolio breakdown?***

☐ Yes

☒ No

☐ Don't know / no opinion / not relevant

**Question 63. Should the identification of an AIF with a LEI identifier be mandatory?**

☒ yes

☐ no

☐ Don't know / no opinion / not relevant

**Question 63.1 Please explain your answer to question 63, presenting benefits and disadvantages as well as costs associated with introducing such a requirement:**

Funds and asset managers already provide LEIs for all their AIFs since 2012. It does not generate any issue, and it facilitates the overall tracking for regulators, except for firms managing several LEIs that could face higher costs on a cumulative basis.

We also consider that, in case of delegation of management, the LEI identifying the management company should remain the one of the company identified in the prospectus and which is legally responsible for the constitution and operation of the fund.

The LEI facilitates the harmonisation and automation of reporting, risk and portfolio management hence helping cost reduction and increasing data quality and security.

Therefore, we support the use of LEI for:

- Delegated Third Parties, including Asset managers, Investment Managers and Investment Advisors,

- Umbrella funds; and

- Master fund and Feeder(s) funds.

In situations where a fund related party is not legally required to obtain an LEI, this should not limit the ability of the LEI fund entity to fulfil its legal obligations, for example the missing LEI on a fund related entity should not impede regulatory reporting and should not create reporting mismatches due to a sole lack of a LEI on a related fund entity. LEIs on all fund related entities should only be mandatory in local (regulatory reporting) regulation after the use of LEI is mandated worldwide.

**Question 64. Should the identification of an AIFM with a LEI identifier be mandatory?**

☐ yes

☒ no

☐ Don’t know / no opinion / not relevant

**Question 64.1 Please explain your answer to question 64, presenting benefits and disadvantages as well as costs associated with introducing such a requirement:**

Funds already provide LEIs for all its national AIFMs : it does not generate any issue, and it facilitates the overall tracking for regulators.

However, lack of LEIs should not always lead to a fail report in situations where a LEI is not yet allocated (similar to the grey situation between the finalisation of an IPO and the issuance of the ISINs of a new issue) and where the reporting is rejected because the LEI of the asset manager is wrong despite the fact that the fund is properly identified.

***Question 65. Should the use of an LEI identifier for the purposes of identifying the counterparties and issuers of securities in an AIF's portfolio be mandatory for the Annex IV reporting of AIFMR?***

☒ Yes

☐ No

☐ Don't know / no opinion / not relevant

***Question 65.1 Please explain your answer to question 65, presenting benefits and disadvantages as well as costs associated with introducing such a requirement:***

***5000 character(s) maximum***

***including spaces and line breaks, i.e. stricter than the MS Word characters counting method.***

Most EFAMA's members already provide LEIs for all their counterparties and issuers of securities.

However, for OTC derivatives the management of LEIs may be complex and generate burdens, due to their decentralised nature.

***Question 66. Does the reporting data adequately cover activities of loan originating AIFs?***

☒ Yes

☐ No

☐ Don't know / no opinion / not relevant

***Question 66.1 Please explain your answer to question 66:***

There is currently no market failure for data reporting covering activities of loan originating AIFs which justifies changes to current practice, and current reporting data provides supervisors with sufficient information regarding the activities of loan originating AIFs.

In its 2020 annual statistical report on EU AIFs, ESMA concludes that AIFs' exposures to leveraged loans and CLOs have increased, but exposures remain limited and most AIFs investing in leveraged loans and CLOs make limited use of leverage and do not face significant liquidity mismatch. However, ESMA sees the need to actively monitor AIF exposures in the context of deterioration of underwriting standards and lower credit quality of leveraged loans[17]. This can be achieved by the current reporting requirements because the structure of the AIFMD reporting is in general suitable to cover the principal

[17] We refer to ESMA Annual Statistical Report: EU Alternative Investment Funds, published on 10 January 2020, available at the following link.

information of a loan (e. g. issuer, notional, yield, price, maturity). ESMA is already able to use two main sources of data under the AIFMD to assess AIFs' exposures to specific asset classes:

- Under Article 24(2) of the AIFMD, AIFs must report detailed data on their exposures (long and short), including specifically on some asset classes. AIFs report exposures on leveraged loans and on CDO/CLOs, where both securitised products are grouped together.

- Under Article 3(3)(d) of the AIFMD, funds must report at security-level the top five instruments in which they are trading.

Adding further data fields would only add operational burdens and cost to such funds without any commensurate benefits. This would also have an impact on the appetite of loan funds to provide credit to European businesses at a time when alternative sources of finance should be encouraged to support the economic recovery from the COVID-19 pandemic.

***Question 67. Should the supervisory reporting by AIFMs be submitted to a single central authority?***

☐ Yes

☒ No

☐ Don't know / no opinion / not relevant

***Question 67.1 Please explain your answer to question 67:***

There is no need for ESMA, or any other entity, to become a central authority for supervisory reporting. NCAs should remain competent for gathering data from the investment management industry, then share them with ESMA.

ESMA should also use its supervisory convergence powers' tools to minimise difference of interpretation of reporting data amongst NCAs.

***Question 68. Should access to the AIFMD supervisory reporting data be granted to other relevant national and/or EU institutions with responsibilities in the area of financial stability?***

☒ Yes

☐ No

☐ Don't know / no opinion / not relevant

***Question 68.1 If yes, please specify which one:***

☐ ESRB

☐ ECB

☐ NCBs

☐ National macro-prudential authorities

☒ Other

*Please specify to which other relevant national and/or EU institutions the access to the AIFMD supervisory reporting data should be granted:*

All of the above.

***Question 68.2 Please explain your answer to question 68.1:***

From an EFAMA perspective, access to AIFMD supervisory reporting data should be granted to all EU institutions which deal with supervision of financial risks such as ESRB, National Central Banks, national macro prudential authorities, and the ECB.

This exchange of data should not, however, be unidirectional: Central Banks should also share their data on the investment management industry (e.g. fund inventories) with securities supervisors at both the national and European levels. Data exchange should be a two-way street.

Rules on full exchangeability of granular instrument master file, transaction, portfolio holdings and associated risk/return data between the relevant supervisory, regulatory and Central Bank bodies within the EU are a prerequisite to avoid duplicative and non-harmonised regulatory reporting going forward. The use of available technology to exploit all the data would largely optimise such a use, on an ongoing basis, to obtain a permanent view on financial markets.

***Question 69. Does the AIFMR template effectively capture links between financial institutions?***

☒ Yes

☐ No

☐ Don’t know / no opinion / not relevant

***Question 69.1 Please explain your answer to question 69:***

The AIFMR template effectively captures links between financial institutions because asset managers are required to disclose their top 10 exposures/counterparties (Reporting Templates: AIF – data field n°13), top five portfolio concentration/counterparties (Reporting Templates: AIF – data field n°14), their top five beneficial owners (Reporting Templates: AIF – data field n°17) and, for substantially leverage funds, their top five lenders (AIF-specific information to be made available to the competent authorities under Article 24(4) AIFMD – data field n°2). This allows NCAs to identify funds that have extensive ties to other financial institutions and, as a result, could represent a systemic risk.

***Question 70. Should the fund classification under the AIFMR supervisory reporting template be improved to better identify the type of AIF?***

☐ Yes

☒ No

☐ Don't know / no opinion / not relevant

***Question 70.1 Please explain your answer to question 70:***

The AIFMD reporting template currently includes five AIF categories and no less than 35 investment strategy categories (see Annex IV – AIF-specific information to be provided – data field n°10, pp. 72-74). It is therefore unclear whether further granularity would indeed increase the quality of the data reported to NCAs.

Moreover, most AIFs under the "other AIFs" category are de facto UCITS-like AIFs that invest in securities with no leverage. Although it is true that a subset of the "other AIFs" category could pose greater systemic risks as they are more leveraged, tend to have their investments concentrated in fewer assets, and may sometimes have liquidity mismatches, these only account for 7% of the "other AIFs" category and 4% of the total AIF universe.

Furthermore, ESMA does not provide any evidence that these funds are substantially leveraged (i.e. having a leverage above the 300% threshold) nor that they face important liquidity mismatches. As regards leverage, ESMA does not provide the average leverage for these "other" AIFs. We note, nonetheless that that the average leverage for the whole "other AIFs" category is 162%. This figure is much lower than the 5514% average for Hedge Funds, for instance. Similarly, as regards liquidity mismatch, ESMA does not provide any evidence that these funds have important liquidity mismatches either. It only provides that there is a very slight liquidity mismatch across the "other AIFs" category and that some of these AIFs have high levels of unencumbered cash.

It is crucial to keep in mind that the AIMFD supervisory reporting has for purpose to give NCAs the tools necessary to monitor the AIF market and prevent the build-up of systemic risk. A more granular fund classification would only be warranted where there is evidence that some funds under the "other AIFs" category would represent greater financial stability risks and, even in that case, it is far from certain that a more granular classification would improve the supervisory outcome as leverage and liquidity mismatch might cut across investment strategies.

***Question 71. What additional data fields should be added to the AIFMR supervisory reporting template to improve capturing risks to financial stability:***

☐ value at Risk (VaR)

☐ additional details used for calculating leverage

☐ additional details on the liquidity profile of the fund's portfolio

☐ details on initial margin and variation margin

☐ the geographical focus expressed in monetary values

☐ the extent of hedging through long/short positions by an AIFM/AIF expressed as a percentage

☐ liquidity risk management tools that are available to AIFMs

☐ data on non-EU master AIFs that are not marketed into the EU, but which have an EU feeder AIF or a non-EU feeder marketed into the EU if managed by the same AIFM

☐ the role of external credit ratings in investment mandates

☐ LEIs of all counterparties to provide detail on exposures sustainability-related data, in particular on exposure to climate and environmental risks, including physical and transition risks (e.g. shares of assets for which sustainability risks are assessed; types and magnitudes of risks; forward-looking, scenario-based data)

☒ other

***Please explain what other data fields should be added to the AIFMR supervisory reporting template, providing as much detail as possible and relevant examples as well as the costs, benefits and disadvantages of this option:***

Members believe that Value at Risk (VaR) should be an optional metric. VaR is already part of the AIFMD reporting, and included in the AIFMD template (ID302) as additional information that NCAs could require AIFMs to report on a periodic basis pursuant to the Opinion published by ESMA on 'Collection of information for the effective monitoring of systemic risk under Article 24(5), first sub-paragraph, of the AIFMD'[18]. If included in the AIFMD template, the field should clearly indicate: VaR (leave blank if the metric is not calculated). In no case VaR should be imposed on all AIFs, this would be ineffective for a majority of low to none leverage UCITS-like funds.

In essence, VaR information could be useful as an additional measure in the risk assessment, where relevant for the AIF, meaning that this information should not be mandatory for all strategies implemented by AIFs. It would also be useful to recommend using for the reported figure the same settings as the UCITS Directive so that the analysis is meaningful (either calculated with the UCITS settings or converted in a common format).

***Question 72. What additional data fields should be added to the AIFMR supervisory reporting template to better capture AIF's exposure to leveraged loans and CLO market?***

*Please explain your answer providing as much detail as possible and relevant examples as well as the costs, benefits and disadvantages:*

No additional data fields should be added to the AIFMR supervisory reporting template to better capture AIFs exposures to leveraged loans and the CLO market.

[18] ESMA's Opinion on Collection of information for the effective monitoring of systemic risk under Article 24(5), first sub-paragraph, of the AIFMD, released on 1 October 2013, available at the following link.

An AIF's principal exposures and portfolio concentration levels are already reported under existing requirements (see Annex IV – AIF-specific information to be provided to competent authorities under Article 24(2) AIFMD – data field n°8, p.80). It is unclear why any exposure to leveraged loans and CLO market would merit additional disclosure through new data fields beyond what it already required.

Further evidence would be needed from NCAs and ESMA on the reasons why they cannot perform this analysis based on the reporting that they currently receive.

Please also refer to our response to Question 66.

***Question 73. Should any data fields be deleted from the AIFMR supervisory reporting template?***

☐ Yes

☒ No

☐ Don't know / no opinion / not relevant

***Question 74. Is the reporting frequency of the data required under Annex IV of the AIFMR appropriate?***

☒ Yes

☐ No

☐ Don't know / no opinion / not relevant

**Question 74.1 Please explain your answer to question 74, presenting the costs, benefits and disadvantages for a suggested change, if any:**

The AIFMD reporting frequency is well understood and established within AIFMs at this stage and AIFMs have developed processes and solutions and engaged resources to ensure that they can comply with the current reporting frequency.

***Question 75. Which data fields should be included in a template requiring AIFMs to provide ad hoc information in accordance with Article 24(5) of the AIFMD during the period of the stressed market in a harmonised and proportionate way?***

*Please explain your answer presenting the costs, benefits and disadvantages of implementing the suggestions:*

Please refer to our response to Q. 58. Each crisis has its own characteristics. It is thus impossible to say which data fields would be necessary in future stressed market conditions.

As mentioned before, the critical point is to ensure proper information sharing between National Central Banks receiving fund inventories, NCAs, ESMA and ESRB. And during stressed situations, such preestablished improved connections among securities regulators and central banks would facilitate the efficient and immediate exchanges of data if needed. NCAs need to stay in regular contact with firms through regular reporting. Firms would have little time to provide for additional exceptional reporting when dealing with crisis situation (from this perspective, it is important to note that the EU and US Authorities have decided on their own to postpone a series of regular reporting duties in the midst of the March volatility period).

***Question 76. Should supervisory reporting for UCITS funds be introduced?***

☐ Yes

☒ No

☐ Don't know / no opinion / not relevant

***Question 76.1 Please explain your answer to question 78, also in terms of costs, benefits and disadvantages:***

EFAMA advocates for the European Commission to focus on the AIFMD Review before considering any change to the UCITS framework as national regimes are already in place in many Member States and reviewing the two frameworks at the same time would introduce unnecessary complexity into the policy debate.

Similar reporting requirements should only be introduced for UCITS if it could be proven that this reporting was necessary in order to monitor whether UCITS are contributing to a build-up of systemic risk. We should also not lose sight of the purpose of this exercise, which for AIFMD was to assist NCAs and ESMA in monitoring whether there is a build-up of systemic risk.

We would encourage the European Commission to start discussions in the context of an expert group involving ESMA, National Competent Authorities as well as the industry, in order to consider pros and cons of the current approach.

***Question 77. Should the supervisory reporting requirements for UCITS and AIFs be harmonised?***

☐ Yes

☒ No

☐ Don't know / no opinion / not relevant

***Question 77.1 Please explain your answer to question 79, also in terms of costs, benefits and disadvantages:***

It is important to recognise that UCITS and AIFs are very different products in the design and application of rules. UCITS do not present the same level of risk from a financial stability perspective because of strict exposure limits and borrowing rules, and more restrictive rules on eligible assets. Any potential UCITS reporting regime should take into account the fundamental differences between both Directives (retail investor protection from a UCITS perspective and financial stability considerations from an AIFMD perspective).

We would encourage the European Commission to start discussions in the context of an expert group involving ESMA, National Competent Authorities as well as the industry, in order to consider pros and cons of the current approach, look at possible solutions and to ensure greater convergence between reporting regimes, reduce unnecessary duplications of reporting obligations, as well as facilitate a better exchange of information.

***Question 78. Should the formats and definitions be harmonised with other reporting regimes (e.g. for derivates and repos, that the AIF could report using a straightforward transformation of the data that they already have to report under EMIR or SFTR)?***

☐ Yes

☒ No

☐ Don’t know / no opinion / not relevant

***Reasoning:***

Whereas we agree that consistent approaches among different regulatory frameworks should apply to transaction reporting (such as in EMIR or MiFIR) and supervisory requirements deriving from other regulatory frameworks (like the provisions applicable to funds in the SFTR ), we oppose to any fundamental short term changes to existing funds reporting. Fundamental changes to these requirements are not necessary as the current reporting requirements are detailed, well-targeted and function well.

We also urge the European Commission to:

- Mandate the use of ISIN codes for all financial instruments,
- Support the international adoption of ISO20022 in as much domains as possible (e.g. corporate actions, collateral, etc.),
- Consider our proposed hybrid reporting mechanism , created for EMIR Refit that can by nature be extended to other reporting.

## c. leverage

***Question 79. Are the leverage calculation methods – gross and commitment – as provided in AIFMR appropriate?***

☒ Fully agree

☐ Somewhat agree

☐ Neutral

☐ Somewhat disagree

☐ Fully disagree

☐ Don't know / no opinion / not relevant

***Question 79.1 Please explain your answer to question 79 in terms of the costs, benefits and disadvantages:***

| |
|---|
| In general, the leverage calculation methods (gross and commitment) as provided in AIFMR work very well and are appropriate in practice. In this context, we do not agree with the ESRB statement in its letter on considerations regarding the AIFMD[19] that NCAs cannot readily reconstruct a fund manager's computation of leverage based on the current reporting of the leverage figures. Comparison of figures across funds and data quality assessments should be possible precisely because there are concrete specifications for the calculation of leverage based on the two methods, and this allows for exact overview of the degree of leverage of an AIF.<br><br>Any policy consideration on leverage should take into account that because of the current low levels of leverage in the European investment funds sector (see latest ESMA's RTV Report[20]), the use of leverage mainly for risk-hedging purposes and the already comprehensive current EU regulatory framework, the majority of investment funds employing leverage in Europe do not pose financial stability risks. |

***Question 80. Should the leverage calculation methods for UCITS and AIFs be harmonised?***

☐ Yes

☒ No

☐ Don't know / no opinion / not relevant

***Question 80.1 Please explain your answer to question 80:***

| |
|---|
| The current EU regulatory framework offers a set of methods addressing in a comprehensive way the use of leverage in investment funds. It consists of the AIFMD framework, with detailed requirements for the calculation of leverage in the AIFM Regulation, and the UCITS Directive with requirements in the Delegated Directive to calculate the global exposure and additional explanations in the CESR Guidelines on Risk Measurement and the Calculation of Global Exposure and Counterparty Risk for UCITS[21]. These requirements foresee a matrix of calculation methods, namely the gross method, the commitment method, and the VaR metrics. |

[19] ESRB considerations regarding the AIFMD, published on 3 February 2020, available at the following link.
[20] Please refer to the ESMA Report on Trends, Risks, and Vulnerabilities, released on 2 September 2020, available at the following link.
[21] CESR Guidelines on Risk Measurement and the Calculation of Global Exposure and Counterparty Risk for UCITS, published on 14 April 2020, available at the following link.

We believe that such a matrix of different measures allows for a better representation of a fund's economic exposure on micro-level in order for regulators to draw the right conclusions for financial stability purposes. It helps meet the challenges of calculating leverage across such a wide range of portfolios with different investment strategies and significantly different risks in size, nature and characteristics associated to their underlying assets. EFAMA firmly supports the measures foreseen in the European regulatory framework, which has proven its risk-resilience and value through the diverse market events since the global financial crisis and is among the more advanced ones at the global level.

AIFs and UCITS can differ in the methods used to increase the market exposure of a fund. In particular, UCITS are limited in the use of derivatives and may borrow cash only on a temporary basis with a limit of 10 per cent of the value of the fund. Another difference between AIFs and UCITS is that AIFs are required to calculate a gross leverage in any case. UCITS are only required to calculate and to disclose a gross leverage if they use the VaR approach (cf. Box 24(2) of the CESR guidelines). That approach should remain unchanged. It does not make sense to have different measures of leverage for UCITS and AIF funds that are, regarding all constituents of the funds, identically composed.

If harmonisation or changes are envisaged, EFAMA is in favor of using the UCITS Commitment approach and diversity of measures (crafted with a view to using a cap). We want to highlight that the current UCITS regime works well, both for fund managers and for investors.

Furthermore, if changes are envisaged by the regulators/legislators – following a gap analysis from IOSCO – EFAMA would be happy to discuss all questions regarding different definitions, interpretations and practical implications of leverage figures in a group of experienced practitioners together with the regulators.

***Question 81. What is your assessment of the two-step approach as suggested by International Organisation of Securities Commissions ('IOSCO') in the Framework Assessing Leverage in Investment Funds published in December 2019 to collect data on the asset by asset class to assess leverage in AIFs?***

***Please provide it, presenting costs, benefits and disadvantages of implementing the IOSCO approach:***

We are supportive of the international regulators' efforts to assess the robustness of the existing regulatory frameworks that monitor the use of leverage in investment funds and enhance consistency at the global level via common measures.

In terms of the suggested approach by IOSCO, we agree in principle with the proposal to establish a framework for the calculation and analysis of leverage in funds in two steps (the "2-step approach"), with the aim to identify first which funds may pose risk to financial stability on the basis of the use of leverage (step 1) and then further analyse this particular subset of funds (step 2). We do not consider that every fund using leverage is a source of risk to financial stability and as the majority of the European funds industry is not substantially leveraged it should be filtered out at step1.

Only a small subset of investment funds merits further analysis at step-2 and the right criteria need to be in place at step-1 to appropriately identify those funds. Even then, it is important to stress that funds identified for further assessment at step-2 are not to be automatically considered as posing financial stability risks, as there is further assessment to take place on the basis of the investment strategy, the risk profile, the level of interconnectedness and the specific characteristics of the asset management business model.

Concerning the measures proposed for step-1, we firmly support the measures foreseen in the current European regulatory framework, i.e. the gross method and the commitment approach, whereas in relation to measures foreseen for step-2, we welcome IOSCO's suggestion to perform risk-based analyses to better understand leverage-related risks potentially posed by funds identified in step-1.

In this respect, and as highlighted above, the existing EU framework – the AIFMD, UCITS Directive and the CESR Guidelines on Risk Measurement and the Calculation of Global Exposure and Counterparty Risk for UCITS - already foresees a matrix of calculation methods (the gross method, the commitment method, and the VaR metrics).

Regarding the analysis of metrics by asset class discussed by IOSCO, we would like to stress that there are extensive reporting requirements at the EU level covering a wide range of data, but this type of analysis by asset class is not required. Instead, many EFAMA members are already providing for a line-by-line report ("inventories") to their prudential authorities. Going further and adding a different reporting layer would bring important burden and costs, which should be avoided, given that the level of existing reporting is already granular and detailed.

Moreover, this type of aggregation by asset class cannot be relevant when reporting net notional exposures. The best way to aggregate by asset class is to gather similar funds/strategies.

***Question 82. Should the leverage calculation metrics be harmonised at EU level?***

☐ Yes

☒ No

☐ Don't know / no opinion / not relevant

We have addressed the response to this question under our response to question 80.

***Question 83. What additional measures may be required given the reported increase in CLO and leveraged loans in the financial system and the risks those may present to macro-prudential stability?***

| |
|---|
| It is unclear what measures might be appropriate within the AIFMD framework to address potential concerns arising from the reported increase in CLO and leveraged loans and any risks these may present to the financial system. CLOs and leverage loans do not create additional leverage at fund level, therefore, it is not necessary to create additional requirements within AIFMD. |

***Question 84. Are the current AIFMD rules permitting NCAs to cap the use of leverage appropriate?***

☒ Yes

☐ No

☐ Don't know / no opinion / not relevant

***Question 85. Should the requirements for loan originating AIFs be harmonised at EU level?***

☐ Yes

☒ No

☐ Don't know / no opinion / not relevant

***Question 85.1 Please explain your answer to question 85:***

| |
|---|
| There is currently a public consultation on the effectiveness of the ELTIFs framework which provides a pan-European framework for some types of loan origination by AIFs, reform of which has been identified as a core part of the EU's capital markets union project. We would strongly recommend that there is no further consideration of additional requirements for AIFs until the ELTIF review and any necessary reforms are implemented.<br><br>The establishment of a specific framework for loan origination within the AIFMD would represent a significant departure from the existing AIFMD framework. Recital 10 of the AIFMD explicitly states that the Directive does not regulate AIFs and that it would be "disproportionate to regulate the structure or composition of the portfolios of AIFs managed by AIFMs at Union level and it would be difficult to provide for such extensive harmonisation due to the very diverse types of AIFs managed by AIFMs".<br><br>We agree with this approach which ensures there is a consistent approach for different types of alternative investment strategies (e.g., hedge funds, private credit, private equity, real estate or infrastructure) and to limit the potential for nominal distinctions between these strategies within the AIFMD to affect investment decisions. In addition, as of today, there are no comprehensive statistics concerning EU AIFMs investing in loan origination which would allow authorities to assess whether such AIFs would create a systemic risk, which would justify specific requirements and limitations to this specific asset class. |

Hence, the existing AIFMD framework provides NCAs with the necessary tools to authorise and supervise loan origination.

# SECTION V. INVESTING IN PRIVATE COMPANIES

## BACKGROUND:

*The AIFMD rules regulating investing in private companies aim to increase transparency and accountability of collective investment funds holding controlling stakes in non-listed companies. This section seeks insights whether these provisions are delivering on the stated objectives and whether there are other ways to achieve those objectives more efficiently and effectively. Private equity industry has been growing for years from a few boutique firms to € 3,7 T global industry. The questions are raised therefore whether the AIFMD contains all the relevant regulatory elements that are fit for purpose.*

***Question 86. Are the rules provided in Section 2 of Chapter 5 of the AIFMD laying down the obligations for AIFMs managing AIFs, which acquire control of non-listed companies and issuers, adequate, proportionate and effective in enhancing transparency regarding the employees of the portfolio company and the AIF investors?***

***Please choose between:***

☒ Fully agree

☐ Somewhat agree

☐ Neutral

☐ Somewhat disagree

☐ Fully disagree

☐ Don't know / no opinion / not relevant

***Question 86.1. Please explain your answer to Question 86, providing concrete examples and data, where available.***

We believe the current rules are appropriate. AIFMD have certainly formalised the flow of information and the collaborative process between the proposed controller and the company and its senior managers.

***Question 87. Are the AIFMD rules provided in Section 2 of Chapter 5 of the AIFMD whereby the AIFM of an AIF, which acquires control over a non-listed company, is required to provide the NCA of its home Member State with information on the financing of the acquisition necessary, adequate and proportionate?***

***Please choose between:***

☒ Fully agree

☐ Somewhat agree

☐ Neutral

☐ Somewhat disagree

☐ Fully disagree

☐ Don’t know / no opinion / not relevant

***Question 87.1. Please explain your answer to Question 87, providing concrete examples and data, where available.***

While we would question the use NCAs make of information provided, the requirements have not proved overly burdensome and no changes are needed.

***Question 88. Are the AIFMD provisions against asset stripping in the case of an acquired control over a non-listed company or an issuer necessary, effective and proportionate?***

***Please choose between:***

☒ Fully agree

☐ Somewhat agree

☐ Neutral

☐ Somewhat disagree

☐ Fully disagree

☐ Don’t know / no opinion / not relevant

***Question 88.1. Please explain your answer to Question 88, providing concrete examples and data, where available.***

Current provisions on asset stripping are broadly effective and we do not believe changes are needed. There are limited activities in Europe on asset stripping and considerable time has been invested by the industry in understanding the current requirements and even minor changes to the regime would require firms to incur significant time and expense in refreshing legal advice across multiple jurisdictions.

***Question 89. How can the AIFMD provisions against asset stripping in the case of an acquired control over a non-listed company or an issuer be improved?***

***Please provide your suggestion(s) including information, where available, on the costs and benefits, advantages and disadvantages of the proposed measures.***

The current regime achieves the desired regulatory objectives and no changes to those provisions are necessary or desirable.

## SECTION VI. SUSTAINABILITY / ESG

Integrating sustainability factors in the portfolio selection and management has a double materiality perspective, in line with the non-financial reporting directive (2014/95) and the European Commission's 2017 non-binding guidelines on non-financial. Financial materiality refers in a broad sense to the financial value and performance of an investment. In this context, sustainability risks refer to potential environmental, social or governance events or conditions that if occurring could cause a negative material impact on the value of the investment. For example, physical risks from the consequences of climate change may concern a single investment/company, e.g. due to potential supply chain disruptions or scarcity of raw materials, and may concern welfare losses for the economy as a whole. Non-financial materiality, also known as environmental and social materiality, refers to the impacts of an investment/corporate activity on the environment and society (i.e. negative externalities). Still, there is also a financial dimension to non-financial materiality. Notably, so-called transition risks arise from an insufficient consideration for environmental materiality, for instance due to potential policy changes for mitigating climate change (e.g. to regulatory frameworks, incentive structures, carbon pricing), shifts of supply chains and end-demand, as well as stakeholder actions for mitigating climate change.

The disclosure regulation 2019/2088 requires a significant part of the financial services market, including AIFMs, to integrate in their processes, including in their due diligence processes, assessment of all relevant sustainability risks that might have a material negative impact on the financial return of an investment or advice. However, at the moment AIFMs are not required to integrate the quantification of sustainability risks. Regulatory technical standards under the disclosure regulation 2019/2088 will specify principal adverse impacts to be quantified or described. This section seeks to gather input permitting better understand and assess the appropriateness of the AIFMD rules in assessing the sustainability risks.

***Question 90. The disclosure regulation 2019/2088 defines sustainability risks, and allows their disclosures either in quantitative or qualitative terms.***

***Should AIFMs only quantify such risks?***

☐ Yes

☒ No

☐ Don’t know / no opinion / not relevant

***Question 90.1 Please substantiate your answer to question 90, also in terms of benefits, disadvantages and costs as well as in terms of available data:***

EFAMA fully supports the integration of sustainability risks as part of risk management policy at fund level, but we believe that from a risk management perspective there is no reason to single out sustainability risks vis a vis all the other types of risks by requiring specific quantification and introducing an artificial ranking amongst those different risks. As already recognised by a number of public authorities, such as the ECB, sustainability risks can be assessed on a both qualitative and quantitative basis.

Disclosing sustainability risks only in quantitative terms would increase costs without proving benefits to end-investors. Although there may be benefits with quantitative assessments, in terms of risk management it is important to understand how risk integration is done rather than constraining this assessment in particular areas where sustainability risks are easier to quantify. Therefore, a qualitative approach should remain possible and is often desirable. As highlighted by the challenges of implementing the disclosure regulation, we currently observe significant limitations as regards quantitative methodologies to identify and assess sustainability risks and their impact. In addition, qualitative information must be backed by solid data to be meaningful and reliable. Given the lack of data for some categories of underlying assets , or sufficiently sophisticated data, we will need a flexible approach in relation to risk assessment which therefore will need to include disclosures based on estimations and projections. This is particularly true for information provided on actively managed funds, whose composition may change over the investment’s lifetime, and for pre-contractual disclosures, when the AIFM may not be able to provide -and commit to- specific metrics. For these reasons, we believe that the requirement to only quantify sustainability risks would introduce both costs and constraints to the types and extent of risks covered, as end-investors would be provided with potentially misleading information, and bear the additional costs of retrieving and processing the information needed to elaborate qualitative disclosures. While methodologies evolve, and until the availability of non-financial information has improved, AIFMs should continue to provide qualitative disclosures.

The Commission is set to publish the Delegated Acts on the integration of sustainability risks in UCITS and AIFMD and should look at the assessment and implementation of the L2 measures instead of triggering changes at the Level of the AIFMD Review.

***Question 91. Should investment decision processes of any AIFM integrate the assessment of non-financial materiality, i.e. potential principal adverse sustainability impacts?***

☐ Yes

☒ No

☐ Don’t know / no opinion / not relevant

***Question 91.1 Please substantiate your answer to question 91, also in terms of benefits, disadvantages and costs. Please make a distinction between adverse impacts and principal adverse impacts and consider those types of adverse impacts for which data and methodologies are available as well as those where the competence is nascent or evolving:***

AIFMs' investment decision processes integrate non-financial considerations when these are relevant, material to financial performance, consistent with the objectives of the investments and aligned with the preferences expressed by the client. In this process, there is cross-over between adverse impact and sustainability risks. Some adverse impacts also result in a potential financial risk to the portfolio and as such constitute sustainability risks. Broadening the scope of this assessment, requiring *any* AIFM to integrate non-financial materiality independently from the investment's features, may cause the manager to act against its fiduciary duties towards the investor.

Until there is more clarity on how to identify, measure and disclose adverse sustainability impacts under SFDR, AIFMs would benefit from the flexibility to consider sustainability impacts in their investment decision processes on the basis of a materiality assessment, therefore those relevant for underlying assets and investment strategies they use. When doing so and in order to allow integration of those adverse impacts that are truly relevant and material it is important for asset managers to have discretion as to the type of adverse impacts they consider and the methods they use to assess them. Avoiding an overly prescriptive approach, applicable to *any* AIFM, would ensure more proportional requirements and more relevant disclosures for end-investors, that are well-aligned with the fund's composition and characteristics.

***Question 92. Should the adverse impacts on sustainability factors be integrated in the quantification of sustainability risks (see the example in the introduction)?***

☐ Fully agree

☐ Somewhat agree

☐ Neutral

☐ Somewhat disagree

☒ Fully disagree

☐ Don't know / no opinion / not relevant

***Question 92.1 Please explain your answer to question 92:***

For asset managers, there is a link between adverse impacts and sustainability risks, only to the extent the ESG factors linked to adverse impact also have a material impact for the product's returns to investors.

It is crucial for the asset manager to take into account all the (sustainability-related) factors that will affect the performance and risk profile of the product. To that extent, the adverse impact on sustainability factors is integrated in investment decisions – and across AIFM's operations, as in the objectives to mainstream sustainability in the financial sector.

To the contrary, adverse impacts that do not affect the performance of the product, do not entail material risks, aren't financially material and in that sense cannot be considered in the same context as sustainability risks.

It is also important to ensure legal clarity and consistency. Therefore, we strongly recommend alignment with SFDR and the relevant definitions regarding sustainability risks and principal adverse impact. In this context, sustainability risks relate to any ESG factor that is financially material, i.e. that has an impact on the financial returns of the product. Principal adverse impacts, on the other hand, relate to ESG factors that include non-financial materiality.

In these terms, any sustainability factor of financial materiality is already under SFDR and in the level AIFMD and UCITS Delegated Regulation related to ESG risks management. To the contrary, ESG factors with no financial materiality are to be reported as PAI and according to the SFDR requirements for disclosure.

Both PAI and sustainability risks are already covered under disclosures and integration requirements and we see no reason to address this further. To the contrary, mixing the two notions and including non-financially material PAIs to be included into sustainability risks contradicts the fundamentals of risk management policies (that is, to focus on materiality for financial returns) and the definitions under SFDR.

***Question 93. Should AIFMs, when considering investment decisions, be required to take account of sustainability-related impacts beyond what is currently required by the EU law (such as environmental pollution and degradation, climate change, social impacts, human rights violations) alongside the interests and preferences of investors?***

☐ Yes

☒ No

☐ No, ESMA's current competences and powers are sufficient

☐ Don't know / no opinion / not relevant

***Question 93.2 Please explain your answer to question 93:***

AIFMs cannot, and should not, be required to take into account interests and preferences other than those expressed by investors. Asset managers are subject to fiduciary obligations and must build an investment strategy according to these investor preferences, which increasingly consider the impact of investment decisions on sustainability. When this is not in line with investors' preferences, asset managers cannot breach their fiduciary duty by forcing sustainability considerations upon their clients. We therefore believe that the consideration of adverse impacts of investment decisions on sustainability should not be required for all investments but only when this is in line with end-investors preferences.

Upstream in the investment process, financial advisers should take appropriate steps to ensure that retail investors are asked about their sustainability preferences in a simple and adequate way. However, the Commission should avoid prescriptive measures or duplication with the integration of sustainability considerations in MiFID II, or with the definitions and transparency requirements specified under SFDR. At the same time, retail investors' preferences encompass a broader range of considerations than sustainability alone, such as risk tolerance or time horizon.

Appropriate diversification is also essential to ensure investors' protection. In a market where the availability of sustainable investment products is still insufficient, and critical pieces of regulation remain to be finalised or implemented, we would advise against the integration of sustainability considerations *alongside*, and irrespectively of, the interests and preferences of investors. This would also place disproportionate requirements on AIFMs, beyond the requirements imposed on other financial market participants, and add compliance costs to those introduced by SFDR. We believe, instead, that any requirement to consider the sustainability-related impacts of investment decisions would be more relevant in company law, to be introduced as part of the upcoming initiative on sustainable corporate governance. This would enable AIFMs and their clients to make more informed decisions.

***Question 94. The EU Taxonomy Regulation 2020/852 provides a framework for identifying economic activities that are in fact sustainable in order to establish a common understanding for market participants and prevent green-washing. To qualify as sustainable, an activity needs to make a substantial contribution to one of six environmental objectives, do no significant harm to any of the other five, and meet certain social minimum standards.***

**In your view, should the EU Taxonomy play a role when AIFMs are making investment decisions, in particular regarding sustainability factors?**

☐ Yes

☒ No

☐ Don't know / no opinion / not relevant

***Question 94.1 Please explain your answer to question 94:***

If, and only if, there is a sustainability preference of a client, it is justified to include sustainability related requirements laid down in Regulation 2020/852 to AIFMs investment decisions for a specific product or mandate. However, their ex-ante inclusion for every investment decision would in our opinion go too far and fail to align with due diligence of investment managers. It may severely restrict asset managers' investment universe, to the point of funds not being viable. It also entails important risks for asset misallocation and therefore market distortions.

The Taxonomy Regulation serves the purpose of facilitating the reporting on standards under Article 8 and 9 SFRD funds and is therefore not relevant for all funds. The impact of its application to AIFMs would be to add costs and restrict asset managers in making their investment decisions and thereby interfere in the general investment process. For example, it would be very difficult for an actively managed non-Article 8 & 9 AIF, where investments change significantly over time, to meet ex-ante ESG disclosure requirements.

Furthermore, such linkage seems premature given that final technical screening criteria on all environmental objectives, as well as the breadth and quality of reporting by listed and non-listed companies on their level of Taxonomy compliance, remains unclear. The Taxonomy has been introduced to serve the purpose of reporting under an EU Ecolabel, SFDR article 8 & 9 funds and EU Green Bond Standard.

We also find it important to note that, in the absence of data and sufficient sophistication of taxonomy-analysis, such a link would mean over-reliance on third party data; therefore if such a requirement would be in place we see high risks of that becoming a box-ticking exercise.

***Question 95. Should other sustainability-related requirements or international principles beyond those laid down in Regulation (EU) 2020/852 be considered by AIFMs when making investment decisions?***

☐ Yes

☒ No

☐ Don't know / no opinion / not relevant

***Question 95.1 Please explain your answer to question 95, describing sustainability-related requirements or international principles that you would propose to consider.***

***Please indicate, where possible, costs, advantages and disadvantages associated therewith:***

If there is a sustainability preference of a client, it is justified to include sustainability related requirements laid down in Regulation 2020/852. But we do not see the reason or practical merit in introducing further requirements at a time when Taxonomy and NFRD review are only awaiting their implementation. We believe it is too premature to introduce further extensions and that such extensions would undermine the approach and principles of SFRD. In our view, requirements of AIFMD should be consistent with the scope and requirements introduced under SFRD. Adoption of other sustainability requirements could be detrimental to the ultimate policy objective, as this would introduce unnecessary complexity and increase compliance costs.

## SECTION VII. MISCELLANEOUS

This section contains a few questions on the competences and powers of supervisory authorities. It also opens up the floor for any other comments of the stakeholders on the AIFMD related regulatory issues that are raised in the preceding sections. Respondents are invited to provide relevant data to support their remarks/proposals.

***Q96 – Should ESMA be granted additional competences and powers beyond those already granted to them under the AIFMD?***

☐ entrusting ESMA with authorisation and supervision of all AIFMs

☐ entrusting ESMA with authorisation and supervision of non-EU AIFMs and AIFs

☐ enhancing ESMA's powers in taking action against individual AIMFs and AIFs where their activities threaten integrity of the EU financial market or stability the financial system

☐ enhance ESMA's powers in getting information about national supervisory practices, including in relation to individual AIMF and AIFs

☒ no, there is no need to change competences and powers of ESMA

☐ other

EFAMA reiterates its firm opposition to attributing additional competences and powers to ESMA via the present review of the AIFMD/UCITS frameworks.

With the very recent finalisation of the ESFS review concluded in December 2019 and with the amendments to ESMA's founding Regulation (EU) No. 1095/2010 only coming into force as from 1 January 2020, we believe it is far too premature for the Commission to consider additional competences or changes to ESMA's recently revised powers. This is true in particular with regard to those aimed at realising greater convergence among NCAs when it comes to interpret, apply, and enforce common rules. Besides the already well-established "Level 3 measures" (including Guidelines, Opinions, Recommendations and Q&As), this recently-enhanced set of convergence tools, includes:

- The power to initiate in-depth thematic reviews [Article 9(1)(aa)];
- The power to temporarily prohibit or restrict the marketing, distribution or sale of certain financial products, instruments, or activities that have the potential to cause significant financial damage to customers or consumers, or threaten the orderly functioning and integrity of financial markets or the financial stability of the EU [Article 9(5)];
- The power to issue "supervisory briefings", accompanied by possible "common supervisory actions" (CSAs), in line with ESMA's powers to develop new practical instruments and convergence tools to promote common supervisory approaches and practices [Article 29(2)];
- The power to initiate peer reviews to further strengthen consistency and effectiveness in supervisory outcomes [Article 30]; and
- The creation of cooperation groups (at the request of five members of the ESMA Board of Supervisors) on defined topics on which there is need to coordinate and as part of ESMA's mandate to promote supervisory convergence and identify best practices [Article 45b].

As an example of ESMA's greater use of its regulatory convergence powers in ways to bring about common supervisory solutions, we also wish to evoke the valuable creation of an *ad hoc* Supervisory Coordination Network (SCN) to consider multiple authorisation requests brought before NCAs by asset management companies looking to delegate/relocate their functions or activities outside the EU[22].

Furthermore, and as a last resort, ESMA – in coordination with the European Commission – should not hesitate to make full use of its Level 4 powers as described by the Lamfalussy report[23]. Accordingly, ESMA should ensure that EU law is appropriately enforced by checking whether the AIFMD/UCITS

[22] In this regard, please refer to ESMA's relevant press release of 29 May 2020.
[23] The Final Report of the Committee of Wise Men on the Regulation of European Securities Markets, released on 15 February 2001, available at the following link.

requirements are consistently translated and interpreted throughout the European Union and, where necessary, initiate legal actions against Member States deemed to be in breach of EU law.

Until all these tools have not been activated and tested in the context of “live” cases brought to the attention of ESMA by its Member NCAs, we do not believe further powers in relation to asset management companies, nor funds (whether AIFs or UCITS), are justified. In sum, EFAMA believes that ESMA already disposes of the necessary tools to bring about a single EU rulebook for asset management activities.

***Please explain why you think ESMA should be entrusted with authorization and supervision of all AIFMs. Present costs, advantages and disadvantages associated with the chosen option. Concrete examples substantiating your answer are welcome (max. 5000 characters):***

In line with our response above, EFAMA believes there is presently no convincing case for ESMA to obtain direct supervisory powers over asset managers, be they AIFs (including EuVECAs, EuSEFs or ELTIFs), UCITS or other.

As we have also observed during the works of the Commission’s High Level Forum (HLF) on CMU and subsequent final report released in June 2020, European savers/investors are best served by effective and proportionate supervision by those authorities which have a close understanding of the local market. The asset management sector is, in particular, characterised by the existence of a number of “centres of excellence” where particular expertise, whether in relation to the operation of funds, or the management of assets, has developed. The benefits of this proximity and granular knowledge of local players, market conditions and investors were, once again, clearly demonstrated in the Covid-19 context.

Moreover, as the Commission is aware, beneath the opportunities offered by the system of EU distribution passports, fund distribution within the EU single market inevitably reflects different national approaches, each tied to a Member State population’s attitudes towards saving and investing. Effective and clear communication to investors in their native language is also of no lesser importance. We believe the role of national supervisors also remains critical to adapt EU legislation to local conditions, ensuring proportionality is respected, all while acting as the first point of reference for retail investors.

More practically, besides the broad EU body of norms in the form of “Level 1”, Level 2” and “Level 3” provisions, a management company’s daily operations and fund offerings rely on myriads of necessary national provisions, steeped in either common or civil law traditions (e.g. contract law, insolvency law, tax law etc.), thus falling within the remit of each Member State. The absence of EU law provisions in these very specific domains would inevitably create a sort of legal “dualism”, risking to draw ESMA and NCAs/national authorities (and possibly even national courts) into protracted legal disputes related to ESMA’s supervisory decisions.

If financial stability and investor protection are viewed as motives to justify the attribution of greater supervisory powers to ESMA over asset managers – as the ECB presently has for credit institutions under the SSM – we note that the asset management industry and its clientele, as other forms of non-bank financial intermediation, are far less homogenous compared to credit institutions. Subjecting the former to a centralised supervisory system, will not work in practice (and certainly not with the resources ESMA is likely to have available over the short- to medium-term). As an example of the difficulties implied by the concentration of centralised supervision in ESMA’s hands, we could consider how future investigations and/or on-site inspections would be carried out. This is another area, where an NCA's proximity to its local market is needed.

Lastly, what is often missing in the motivations of those advocating in favour of direct oversight powers to ESMA over asset management companies are considerations around ESMA's own resources. Unless ESMA's yearly budget can be expanded exponentially over the coming years, it appears evident that in the foreseeable short- to medium-term future, ESMA will be unable to substitute itself to the NCAs as the sole supervisor of a universe with tens of thousands of funds whose numbers are set to likely only increase further[24]. We therefore believe that considerations on the further attribution of supervisory powers to ESMA – whether over funds, their managers or other entities – should be postponed until the next review of the ESFS and examined against some very decisive and "hard" facts. Among these, of no lesser importance are the skills required to authorise and supervise very different legal structures which differ between Members States, conduct examinations or carry-out enforcement cases, to only name a few. At present and for the foreseeable future, we do not believe ESMA will be able to attract and retain expertise that is commensurate with these essential tasks, which is why preserving the current role of NCAs is clearly preferable.

Instead and until the next ESFS review, ESMA should more practically focus on areas where greater convergence through the full use of its existing toolkit is needed. For instance and as we have advocated above, by subjecting NCAs to binding reviews (as also recommended in the HLF's June 2020 final report), as well as in areas where centralisation proves beneficial and has a clearly identifiable purpose (e.g. data centralisation, an European Ratings Platform, EU-wide consolidated tape, among others).

***Please explain why you think ESMA should be entrusted with authorization and supervision of non-EU AIFMs and AIFs. Present costs, advantages and disadvantages associated with the chosen option. Concrete examples substantiating your answer are welcome (max. 5000 characters):***

We extend our reasoning above to non-EU AIFMs & AIFs, while cognisant of the fact that the AIFMD third-country passport is still pending, hence further removing any justification as to why the authorisation and supervision of non-EU AIFMs and AIFs should be transferred from NCAs (i.e. those of the future Member State of reference) to ESMA.

***Please explain why you think ESMA's powers should be enhanced in taking action against individual AIMFs and AIFs where their activities threaten integrity of the EU financial market or stability the financial system. Present costs, advantages and disadvantages associated with the chosen option. Concrete examples substantiating your answer are welcome (max. 5000 characters):***

As we believe direct supervisory powers over asset managers (AIFMs) are presently not justified for the reasons explained above, considerations around ESMA's product intervention powers over AIFs or other types of funds lead us to the same conclusion. There is, moreover, the absence of a motive to justify why such powers deserve to be transferred, as NCAs have until today successfully managed to

[24] According to EFAMA's quarterly statistics for the third quarter of 2020, this universe counted 29,398 AIFs and 32,234 UCITS, for a total of over 63,000 entities, each requiring its own specific authorisation procedures and ongoing supervisory monitoring as a minimum to guarantee their effective supervision.

avoid authorising potentially harmful fund products and would have no concern to ban their distribution altogether in a hypothetical scenario.

Consistent with our position for the Commission to recognise the specific role NCAs play in their domestic market, especially in view of their proximity to the end-investor and resulting ability to more accurately assess harmful practices, we believe that any restriction or prohibition to the distribution of fund products should thus naturally remain with the NCAs. This would not prevent an NCA from informing ESMA, as well as other (host) NCA in Member States where the funds are distributed cross-border, for coordinated actions to be taken.

EFAMA's opinion on also attributing hypothetical emergency intervention powers to ESMA for the purpose of coordinating responses in a crisis management situation is consistent with our views expressed above. As confirmed in the context of the recent market events induced by the global pandemic in the first half of 2020, for asset management companies NCAs must remain the single most important reference point. Only the latter can have in-depth discussions with managers in relation to the funds they have authorised, to the controls funds need to have in place, as well as to the specific investor profiles that stand to be impacted by significant market corrections, among other factors.

Naturally, this should not prevent discussions around NCAs' experiences to be shared both with ESMA and within ESMA for approaches to be coordinated. In fact, this has occurred quite successfully since March 2020 when a few types of open-end funds began experiencing liquidity stresses. ESMA was able to assume an important coordination role, organising frequent exchanges with NCAs to discuss market developments and the supervisory risks encountered[25].

***Please explain why you think ESMA's powers should be enhanced in getting information about national supervisory practices, including in relation to individual AIMF and AIFs. Present costs, advantages and disadvantages associated with the chosen option. Concrete examples substantiating your answer are welcome (max. 5000 characters):***

Given its remit and powers already available to gather information from its member NCAs, we do not see substantial barriers for ESMA to obtain information related to national supervisory practices. The work of the ESMA Supervisory Coordination Network as from May 2017 offers a clear example of how ESMA can access case-specific information through an open and cooperative approach with its members. Experience also suggests that information requests and resulting responses are regularly performed even more informally.

EFAMA would also strongly question the reasons behind ESMA obtaining supervisory information from NCAs, including one pertaining to individuals AIFMs/AIFs, with the exception of the limited circumstances (i.e. Articles 25 and 47) currently foreseen under the AIFMD.

[25] In this regard, please refer to the ESMA Chairperson Steven Maijoor's keynote speech delivered at the EFAMA Investment Management Forum on 13 November 2020.

***Please explain with what other additional competences and powers ESMA should be granted. Present costs, advantages and disadvantages associated with the chosen option. Concrete examples substantiating your answer are welcome (max. 5000 characters):***

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|---|
| In line with our responses above, there is presently no convincing motivation to justify the further attribution of powers to ESMA. In the absence of significant weaknesses in the current framework, as well as of evident failures in the present supervisory system over asset management entities – especially in terms of guaranteeing financial stability and market integrity – we do not believe ESMA's existing powers under the AIFMD require enhancements. We also note in this regard how the latter have hardly been used, thus making the case for the overhaul of the present system even less convincing.<br><br>In addition, we would question the Commission's emphasis on this aspect, given the scope of this consultation is the review of the AIFMD. Our views is that considerations around ESMA's future powers and supervisory remit should more appropriately be framed in the context of a future review of its founding regulation instead. We note that the European Commission has already programmed, in its new CMU Action Plan, the next ESAs review for the end of 2021[26]. We therefore do not see the necessity to address ESMA's powers as part of the current AIFMD Review. |

***Q97 – Should NCAs be granted additional powers and competences beyond those already granted to them under the AIFMD?***

☐ Yes

☒ No

☐ Don't know / no opinion / not relevant

***Question 97.1 Please explain your answer to question 97, providing information, where available, on the costs and benefits, advantages and disadvantages of implementing your suggestion (max. 5000 characters):***

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|---|
| Please refer to our response to Question 96 above. |

***Question 98 Are the AIFMD provisions for the supervision of intra-EU cross-border entities effective?***

☒ Fully agree

☐ Somewhat agree

☐ Neutral

☐ Somewhat disagree

[26] We refer, more precisely, to Action 16 of the New CMU Action Plan, released on 24 September 2020.

☐ Fully disagree

☐ Don't know / no opinion / not relevant

***Question 98.1. Please explain your answer to question 98, providing concrete examples (max. 5000 characters):***

| |
|---|
| As we are not aware of any salient problem in the supervision of intra-EU cross-border entities, we do not see any issue with the present rules. It is believed that NCAs are better suited to respond to this question than industry bodies since the industry only has limited insights on how NCAs cooperate in practice to supervise intra-EU cross-border entities. |

***Question 99 – What improvements to intra-EU cross-border supervisory cooperation would you suggest? provide your answer presenting costs, advantages and disadvantages associated with the suggestions (max. 5000 characters):***

| |
|---|
| Although we do not see at the moment how the intra-EU cross-border supervision cooperation could be improved, we would like to note that initiatives, such as the SCN or the recent ESMA's Common Supervisory Actions (CSAs) on UCITS liquidity risk management and MiFID II suitability rules, are not only a way to ensure supervisory convergence, but they are also a way to create closer working relations between NCAs, and thus contributing to a more effective intra-EU cross-border supervisory cooperation. We therefore welcome new initiatives by ESMA in that area such as, for instance, the CSA on undue costs[27]. |

***Question 100. Should the sanctioning regime under the AIFMD be changed?***

☐ Yes

☒ No

☐ Don't know / no opinion / not relevant

***Question 100.1 [Please explain your answer to question 100, substantiating your answer in terms of costs/benefits/advantages, if possible:***

| |
|---|
| The AIFMD sanctioning regime should not be changed as NCAs have all the tools at their disposal to adequately enforce AIFMD provisions.<br><br>EFAMA supports further work from ESMA on enforcement as the recent ESMA's Report on sanctions[28], released in November 2020, seems to point towards different enforcement levels across the European Union. The Report outlines that 14 out of the 31 EEA NCAs – 45% of the NCAs – did not take any enforcement measure, based on Article 48 of the AIFMD, in 2019. While this represents an increase |

[27] Please refer to the ESMA's press release of 30 January 2020 for the CSA on UCITS liquidity risk management, the press release of 5 February 2020 for the CSA on MiFID II suitability rules, and the press release of 6 January 2021 for the CSA on undue costs.

[28] ESMA's Report on penalties and measures imposed under the AIFMD Directive in 2018-2019, published on 12 November 2020, available at the following link.

since 2018, where 55% of the NCAs did not take any such measure, ESMA still notes that 35% of the NCAs did not take any measure either in 2018 nor in 2019. The Report remarks as well that, in many Member States, only a few measures were taken each year and that the amount of sanctions issued at national level remained relatively low. While we call for caution as differences in the use of enforcement tools should not automatically be interpreted as enforcement shortcomings from certain NCAs, we believe that the current AIFMD sanctioning regime is appropriate as it does not prevent NCAs from taking enforcement actions where needed.

***Question 101. Should the UCITS and AIFM regulatory frameworks be merged into a single EU rulebook?***

☐ Yes

☒ No

☐ Don’t know / no opinion / not relevant

***Question 101.1 Please explain your answer to question 101, in terms of costs, benefits and disadvantages:***

EFAMA does not support this proposal and deems that the hypothesis of a potential “merger” between the UCITS and the AIFM Directives must be considered very cautiously.

As the Commission is aware, the existing body of norms for asset management companies is characterised by very different parts (intended for very different product types and investor populations), and notably, by the difference between a “product” vs. a “manager” regulation. Merging these together in the absence of critical parts - such as an AIF product regulation - promises to create significant anomalies within a hypothetical single regime. Caution is also worthwhile if one considers the reputation of the UCITS product brand, both within the EU and beyond. In this regard, the proposed merger would cloud the specificity of UCITS, resulting in substantial harm to the product’s successful distribution worldwide.

We also invite the Commission to consider the sheer complexity of the current EU body of norms for asset management companies, including the interdependent and very specific “Level 2” and “Level 3” measures, let alone with regard to the natural diversity of the asset management industry, that of its investor/client types, as well as the breadth of the product offer. We see a risk these key specificities will be disregarded under a single regime, regardless of the underlying intentions to possibly streamline and simplify the existing frameworks.

Another consideration relates to the perpetual state of flux concerning asset management legislation, likely to make attempts to merge UCITS and AIFMD regimes unfruitful, unless legislative proposals for related amendments, or for new legislation, are paused for a least a decade, allowing EU rules – from the “Level 1” all the way down to transposing national requirements – sufficient time to settle and be consistently applied.

Lastly, it is precisely because of the project’s expected scale, that it will inevitably distract considerable resources from the attainment of more important objectives over the nearer-term for all parties involved, be these the Commission, the EU co-Legislators and myriads of all other public and private stakeholders, including end-investors. Chief among these objectives is the completion of CMU, branching into the many initiatives highlighted in the Commission’s September 2020 Communication on a new CMU Action Plan. Of these, we believe that the Commission’s sustainability agenda, including the gradual integration of ESG parameters into many areas of financial services, represents already a tall order. Another important priority will be Europe’s post-pandemic economic recovery. In light of these considerations and of the more pressing challenges confronting the work of the Commission in the years ahead, we do not believe a merger of the already vast *acquis communautaire* aimed at asset management companies should be given further consideration.

***Question 102. Are there other regulatory issues related to the proportionality, efficiency and effectiveness of the AIFMD legal framework?***

*Please detail your answer, substantiating your answer in terms of costs/benefits/advantages, where possible:*

We believe that particular attention and consideration should be given to the competitiveness of the European market. It is important to avoid additional complexity and regulatory costs for fund managers in order to keep an internationally competitive framework.

***

## About EFAMA

EFAMA, the voice of the European investment management industry, represents 28 Member Associations, 57 Corporate Members and 23 Associate Members. At end Q3 2020, total net assets of European investment funds reached EUR 17.6 trillion. These assets were managed by more than 34,200 UCITS (Undertakings for Collective Investments in Transferable Securities) and almost 29,400 AIFs (Alternative Investment Funds). At the end of Q2 2020, assets managed by European asset managers as investment funds and discretionary mandates amounted to an estimated EUR 24.9 trillion.

More information is available at www.efama.org.

## Contact

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