



Draft EU Directive on Alternative Investment Fund Managers (AIFM)

Comments by BVI Bundesverband Investment und Asset Management e.V.

Frankfurt am Main,
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I. Preliminary Note:

BVI Bundesverband Investment und Asset Management e.V.¹ supports the declared intention of the draft AIFM Directive “to extend appropriate regulation and oversight to all actors and activities that embed significant risks” and for that purpose to “establish a secure and harmonised EU framework for monitoring and supervising the risks that AIFM pose to their investors, counterparties, other financial market participants and to financial stability”². Deficits existing with regard to systemically relevant unregulated investment products and their providers can certainly be best remedied by a coherent set of rules established at EU level.

The draft Directive, however, goes significantly beyond of what is necessary in order to achieve that objective in that it covers all collective investment schemes existing outside the UCITS regime. In comparison to the situation in other EU member states, German fund managers are most severely affected by this broad approach. German fund management companies, “Kapitalanlagegesellschaften”, have some 800 billion euros of assets under management in “Spezialfonds”, open-ended real estate funds and other non-UCITS. All of these funds are exhaustively and in every respect sufficiently regulated by the German Investment Act as of December 28, 2007.

BVI members strongly object to the unreasonable additional burden for comprehensively regulated and supervised fund managers which is going to be imposed by the prospective AIFM Directive. Each and every management company licensed under the Investment Act would be covered by new or modified and in many respects unsuitable new regulation, because all of them manage at least one AIF according to the draft Directive. Even though they are all licensed as management companies according to the standards of the UCITS

¹ BVI Bundesverband Investment und Asset Management e.V. represents the interest of the German investment fund and asset management industry. Its 92 members currently manage assets of EUR 1.5 trillion, both in mutual funds and mandates, for some 16 million investors. For more information, please visit www.bvi.de.

² Cf. Explanatory Memorandum to the draft AIFM Directive, page 2 and 5.

directive, the new requirements would mean huge expenditure which could put individual players or even market segments at risk.

Moreover, we have strong reservations against the mix of regulation for retail funds set up in accordance with the UCITS regime and for hedge funds and private equity vehicles.

Also, limitations of fund investment opportunities for professional investors being an effective consequence of the proposed provisions are likely to trigger asset flows to the unregulated sector and hence, cannot be deemed legitimate purpose of the AIFM regulation.

As a result, the Directive would damage not only the German fund industry, but also the European investment landscape as a whole without generating any perceivable benefits in terms of the Directive's objectives.

Finally, we are highly concerned about the extensive use of the comitology procedure. According to the Commission's draft, regulatory areas of essential relevance such as the regulatory limitation of permissible leverage for hedge funds (Article 25 para. 3) or core questions of access of offshore AIFM to the EU market (Art. 39 para. 2) are supposed to be transferred to the executive, thus reducing legislative participation of the EU Parliament to a right of veto. This calls into question the democratic legitimation of the whole Directive as at the moment of its adoption at level 1 the impact of several provisions cannot be adequately assessed.

In order to avoid highly undesirable effects which would involve significant detriments for the fund industry in terms of costs and competition, we would like to suggest several amendments to the general concept of the AIFM Directive as well as to its specific provisions which are laid down in detail below.

II. Key Issues:

1. The scope of application of the draft Directive should be restricted to areas of the fund market which can increase systemic risks and/or exercise considerable influence on the real economy.

The proposed regulatory approach, the scope of which covers all non-EU harmonised investment funds, is not backed by any substantial argument. The G20 Summit in London has unmistakably called for regulation of the systemically relevant financial institutions, instruments and markets³; the same principles have been endorsed by the EU Commis-

³ Cf. communiqué of the G20 Summit of 2 April 2009, 'The Global Plan for Recovery and Reform', p. 4: 'We agree (...) to extend regulation and oversight to all systemically important financial institutions, instruments and markets. This will include, for the first time, systemically important hedge funds'.

sion's Communication 'Driving European Recovery'⁴. Accordingly, it has been acknowledged that there is no need (1) to expand the regulation beyond the systemically relevant area and (2) to become active where appropriate frameworks already exist at national level.

The draft of the AIFM Directive thus goes beyond its own objectives and violates the principle of proportionality by including nationally regulated investment vehicles, such as Spezialfonds, open-ended real estate funds (OEREFs), balanced funds etc. and their managers in its scope of application. On account of being licensed for public marketing, these forms of investment are already subject to strict regulation and supervision which, in terms of standards, are in keeping with the UCITS regime. The same is true for the respective management companies, all of which are licensed as management companies within the scope of the UCITS directive.

In order to capture the systemically relevant forms of investment, it would be sufficient to limit the scope of application to the 'highly leveraged AIF' which are the subject matter of draft provisions in Chapter V. In this context, criteria have been found in order to dissociate some high-risk forms of investment against other investment funds, irrespective of their formal classification as hedge funds. In order to subject the politically disputed influence of investment funds on the real economy to specific regulations, additional standards for private equity funds can be introduced, which, however, cannot be justified by the objective of combating systemic risks.

2. Should the wide scope of application of the Directive be maintained, sound differentiations of product-related rules were indispensable in order to avoid an unnecessary burden for funds and investors.

The draft Directive puts a uniform regime on a multitude of fund products with clearly distinct characteristics. For example, the mandatory appointment of a valuator (Article 16) for German investment funds is a novelty which makes no sense at least for listed assets such as equity. The appointment of a depositary (Article 17) is required for all funds; however, there is no mention regarding the role of the so-called prime broker which is of paramount importance at least with hedge funds. This is surprising, since the integration of a prime broker presents a considerable challenge for managers and contractors of hedge funds, both from the organisational and the liability points of view. Ultimately, the proposed rules for investor information (Articles 20, 23) are evidently tailored to the needs of retail investors. However, they do not create any added value for professional customers who, in practice, request individual information to satisfy their reporting obligations and internal requirements anyway.

⁴ Communication for the Spring European Council of 4 March 2009, volume 2: Annexes (COM (2009) 114), p. 3: Debates have very much focused on hedge funds and private equity. By the end of April, the Commission will come forward with legislative proposals to ensure appropriate oversight and regulation of these and other systemically important market players.

These inconsistencies are definitely not required for the purpose of appropriate supervision and regulation. On the contrary, they are likely to produce superfluous costs which would be passed on to the investors of the respective investment fund and hence, would reduce the attractiveness of regulated investment products, compared with products in the securities segment that continue to be unaffected by regulation.

3. Should the wide scope of the Directive be maintained, management companies offering funds regulated at national level exclusively in their respective domestic markets would have to be excluded from the AIFM regime.

The draft Directive raises considerable concerns in terms of the principle of subsidiarity stipulated in Article 5 para. 2 of the Treaty Establishing the European Community (EC Treaty). The necessity of an EU-wide regime for better monitoring of systemic risks is limited to specific fund types whose activities potentially generate risks of this type ('highly leveraged AIF'). Another aspect with EU relevance, the introduction of the product and the company passports in Articles 33 and 34, relates solely to cross-border activities of fund managers. On the other hand, no apparent need for EU regulation exists for the purely national management of regulated investment funds without systemic relevance and their marketing in the home market.

Management companies holding a UCITS licence or an equivalent licence under national law must therefore be able on that basis to continue their operations in the regulated non-UCITS segment at national level. This should pertain to the management and marketing of local non-harmonised investment funds in the management company's home Member State.

4. The regulatory scope of the Directive must not be limited to collective investment undertakings. Such an approach would cause serious competitive disadvantages vis-à-vis unregulated products such as certificates. This result would be blatantly contradictory to the declared goal of the draft Directive to create a cohesive framework for high-risk activities in the financial markets.

In its striving for an all-encompassing regulatory approach, the draft Directive appears inconsequent when in recital 5 it excludes all comparable forms of investment in the securities segment (certificates, 'managed futures', index-linked bonds) from the scope of application. Last years' market practice shows that nearly all investment fund strategies can be reproduced in the form of certificates, but at considerably less cost and management expenditure due to the non-existing product regulation.

It is inconceivable that the AIFM regime, in spite of its claim to capture 'all actors and activities that embed significant risks', wants to perpetuate this imbalance between invest-

ment funds and certificates. This would be seriously disadvantageous for investment funds in competition with certificates which as unregulated vehicles would be able to continue to service all customer requests. The consequence would be a decrease of investor protection, because substitute products provide for a much lower level of security. The fund investor, for example, is in general protected against risks deriving from bankruptcy of the manager, which is not the case with certificates.

As a result, the AIFM regime would in all likelihood facilitate the flow of customer funds to the unregulated segment and thus, generate blatantly counterproductive effects.

5. The draft Directive contradicts in many important points the proven and tested business practices of regulated non-UCITS, such as German Spezialfonds or open-ended real estate funds, and may have prohibitive impact on specialised approaches to the institutional fund management.

The proposed provisions for delegation (Article 18) and safe-keeping of assets (Article 17) would radically curtail investment flexibility of German Spezialfonds, open-ended real estate funds and other fund types within the German investment law. Subsequently, it would no longer be possible to delegate the portfolio management function to an asset manager domiciled outside the European Economic Area. Delegation of portfolio management to non-EU managers is common practice in the European fund industry and essential for both providers and investors in order to make use of local expertise. Important investment opportunities outside of the EU, especially in emerging markets, that require local custody of the acquired financial instruments, would be obstructed by the proposed regulation on depositaries (for details, cf. our comments on Articles 17 and 18 below).

As a result, the proven and tested practice to provide products for special groups of investors or focusing on particular market segments on the basis of regulation for UCITS management companies will be thwarted. The draft AIFM Directive does not provide for a workable substitute environment. Especially for the business model of the German “Master KAG”, a management company focusing on the administration of UCITS and Non-UCITS, the proposed requirements will cause insurmountable obstacles. The foreseeable consequence would be that institutional investors would turn to different, largely unregulated products such as certificates.

6. The long-standing request by the German fund industry regarding the EU passport for open-ended real estate funds cannot be satisfied by granting marketing opportunities to professional investors.

The authorisation of AIF for cross-border marketing to professional investors is by no means suitable to replace the EU passport for open-ended real estate funds advocated since a long time by the German fund industry. According to the German model, OEREFs

are designed as retail products and are licensed for public marketing. The work of the EU Expert Group on OEREFs has produced solutions on how the strong demand of retail investors for indirect real estate investments can be met also on EU level.

It is totally inappropriate to assign OEREFs together with hedge funds and other unregulated fund types to the segment of alternative investments. Rather, OEREFs should be subjected to harmonised product regulation throughout the EU in accordance with the UCITS Directive, in correspondence with the proposals of the EU Expert Group, and on this basis, become eligible for an EU passport for public distribution. In the area of OEREFs, there is no regulatory need for the objectives of the draft AIFM Directive.

7. The opening of the EU fund market for offshore products and managers by means of an EU passport is inadequate.

The opening of the European fund market to offshore products and suppliers, as stipulated in Articles 35 and 39, is highly questionable from the political point of view. Investment funds are launched in third-country domiciles in order to avail themselves of less stringent standards in terms of regulation and supervision or of more favourable taxation regimes. Facilitation of this legal and tax arbitrage by granting of EU passport to third-country funds cannot be considered legitimate purpose of internal market regulation. Instead, by restricting the eligibility for cross-border distribution to EU products, stronger incentives should be created for alternative investment funds to settle within the Community in order to be able to benefit from the passporting rights for AIFM.

In this context, we would like to stress that BVI members have no objections against the existing means of trading with offshore products under the applicable national regimes (e.g. for private placement). In particular, professional investors should not be prevented by the draft Directive from taking benefit of the freedom granted by global capital markets, and it cannot be the subject matter of the Directive to limit the investment options for such investors to fund products that conform to the AIFM regime.

III. Comments on specific provisions:

In submitting our comments, we adhere to the composition of the draft Directive, but would like to make clear that **our core requests relate to the provisions on valuator (Article 16), depositary (Article 17) and outsourcing of activities (Article 18) as these proposals are expected to have strong adverse impact on the overall practice of the fund business.**

1. *Recital 5 (exemptions)*

The regulatory approach of the draft Directive foils its very own objectives to exempt certain investment structures (according to Recital 5 pension funds or managers of non-pooled investments such as endowments, sovereign wealth funds or assets held on own account by credit institutions, insurance undertakings) from its scope. As a rule, these undertakings do not themselves engage in the management of their assets. Instead, they avail themselves of Spezialfonds or other special purpose funds which, under the draft Directive, are supposed to qualify as AIFM. Thus, these structures would be either covered by the Directive or forced to switch to the non-regulated sector in order to find proper management solutions for their assets.

2. *Recitals 10 and Article 52 (Classification as complex financial instruments)*

According to recital 10, AIF are generally to be classified as complex financial instruments. This contradicts Article 38 of the MiFID Implementing Directive, according to which shares in open-ended regulated funds are basically not considered to be complex.

3. *Article 2 (Scope)*

a. *General criticism*

Management companies, which (also) manage other funds than UCITS, must obtain an AIFM license irrespective of whether they intend to use the EU passports available under the AIFM regime or not. Even fund managers operating at purely national level are required to apply for the new licence at the latest one year after implementation of the AIFM Directive (Article 51).

As explained above, this approach is disproportionate and incompatible with the principle of subsidiarity endorsed by the EC Treaty. **Therefore, a narrower scope of application must be envisaged which should be limited to fund categories identified as raising systemic risks. By no means the requirement for a double license according to both UCITS and AIFM Directives is acceptable for management companies that pursue purely national business.**

If the Commission deems it appropriate to provide for a *de minimis* exemption for managers with assets under management of no more than 500 million euros, there should be even more room for an exemption for managers whose business model confines them to the national market.

b. *Exchange traded AIF*

Another problem relates to stock exchange trading of investment units or shares. Article 2 para. 2 does not provide any exception applicable to these circumstances. Con-

sequently, investment funds traded on stock exchanges or through other multilateral facilities would need to ensure:

- that parties to the transactions are exclusively professional investors, provided no additional national licence for retail marketing applies,
- that cross-border marketing targets only professional investors.

Due to the trading set-up of multilateral platforms, these requirements can be neither fulfilled nor controlled.

c. Exemption of certain AIFM categories?

Article 2 para. 2 ultimately requires clarification in terms of limitation of scope of the draft Directive. In light of the wording of Article 4 para. 1, according to which the licensing obligation for the management of AIF pertains to ‘*AIFM covered by this Directive*’, the question arises whether there may be AIFM that do not fall in the scope of application and thus, are able to provide management services to AIF without obtaining an AIFM licence. This is particularly relevant in respect of Article 2 para. 2 letter d) which stipulates an exemption for credit institutions.

4. Art. 3 letter l) (Definition of leverage)

The very broad definition of the term 'leverage' should be assigned a more precise meaning and in particular, be aligned with the provisions of the UCITS Directive. Otherwise, German non-UCITS which are also subject to the Derivative Regulation (Derivateverordnung) implementing the global exposure rules of the UCITS Directive run the risk of being qualified as AIF 'employing high levels of leverage on a systematic basis' according to Article 22. In view of the UCITS Directive permitting similar investment strategies in retail-oriented products, this appears to be a major contradiction.

5. Art. 4 para. 2 (requirement of a double licence)

The draft requires a double license for managers of products in both UCITS and AIF universe without providing defined rules for the handling of conflicting provisions. This means a massive additional burden for presumably all fund managers regulated under the German Investment Act. According to BVI statistics, nearly 90 percent of BVI members managing security funds, meaning 40 regulated and supervised management companies, engage in management of UCITS and non-harmonised investment funds likewise. Moreover, German fund managers offering solely non-harmonised products are also authorised in accordance with the UCITS Directive and thus, observe the relevant organisational and operational standards in their business activities. Therefore, in order to avoid impracticable difficulties for the fund business, **the provisions for the AIFM must be adapted to the UCITS Directive representing an internationally recognised standard for fund regulation.**

6. *Art. 5 letter d), Art. 7 (Requirements for licensing the AIFM)*

A general obligation for submission of contractual terms for all funds to the supervisory authority in the context of manager authorisation is not acceptable. The same applies to the duty to report changes in investment strategy and policy or of AIF rules according to Art. 7. For German Spezialfonds, these provisions would clearly have a restrictive effect and would hamper the flexibility of issuance or subsequent modification of the product. Especially for Master KAGs, which rely on flexible handling of delegation mandates, such an authorisation process would be infeasible. Moreover, consideration of these aspects when granting the AIFM licence is superfluous since they are dealt with in a sufficient manner within the notification process of Art. 31.

As a minimum, we think that the second sentence of Article 7 should be deleted as it effectively enables supervisory authorities to intervene into the product set-up.

7. *Art. 12 (Liquidity management)*

The Level 2 measures on liquidity management and redemption frequencies give rise to the fear that these EU provisions, being of particular relevance for open-ended real estate funds, would in certain cases apply to fund types operating solely on national level. This would amount to a further violation of the subsidiarity principle. Moreover, it appears totally disproportionate to require minimum liquidity for all AIF offering more often than half-yearly redemption opportunities. At least in case of funds investing in assets for which functioning markets are in place, static rules on minimum liquidity make definitely no sense.

8. *Art. 13, 53 (Investments in securitisation positions)*

In order to avoid competitive disadvantages for investment funds, at this point, strict congruency with the newly worded Art. 122a of Directive 2006/48/EC must be maintained. As regards the definition of the scope of application in terms of relevant investments, this does not yet appear to be the case.

9. *Art. 14 (Capital requirements)*

The capital requirements exceed the standard of the UCITS Directive without any conceivable benefit. The lack of a fix 10 million euros cap on the AIFM's own funds might result in very high financial burden especially for large fund managers. In addition, specific allowance for 'insourcing' mandates will result in an obligation for both the in- and outsourcing companies to provide capital backing and thus, will prompt an unnecessary double consideration of the fund volumes managed by delegation.

10. *Art. 16 (Valuator)*

The requirement of an independent valuator conflicts with the regulatory approach of the UCITS Directive and is superfluous at least for funds investing in assets for which reliable market prices exist, e.g. German Spezialfonds. Strict functional independence of the valuation function within the management company's organisational set-up should be considered sufficient. Current practice of task-sharing of management company and depositary stands the test of time. In order not unnecessarily to break up the well-established and proven valuation systems, **the management company itself or the depositary with support of the management company must be permitted to carry on acting as valuator in this context.** In this respect, we see a definite need for clarification in the draft Directive.

With regard to open-ended real estate funds, application of Art. 16 para. 1, 2nd sentence could prompt an obligation to value the portfolio assets in each case of unit issue or redemption. This would be blatantly impracticable. According to the German model, open-ended real estate funds do as a rule provide for daily issuance and redemption opportunities. However, **re-evaluation of all holdings in real estate and real estate companies of a fund in a trading day frequency is simply impossible.** Generally speaking, assets that are not regularly traded and hence, valued according to mark-to-market, discounted cash flow or similar models, should therefore not be subject to valuation duty on such frequent terms.

Furthermore, it must be sufficient to re-value only the fund (and not each and every single asset) in the event of issuance or redemption. This is currently the case with OEREFs, taking into account value fluctuations deriving from securities used for temporarily investing liquidity, distributions or realisation of assets, including real estate. In this respect, at least a clarification is required.

Paragraph 3 leads to questionable results in terms of non-EU country funds. Even when taking into consideration the equivalence requirement in Art. 37, it appears to be unjustifiable to transfer the evaluation sovereignty for AIF to off-shore providers.

11. *Art. 17 (Depositary)*

We welcome the requirement of Art. 17 para. 3 that only credit institutions with registered office within the EU shall qualify for the depositary function as this can enhance security standards for assets held in AIF portfolios.

Nevertheless, the limitation laid down in paragraph 4 according to which a depositary may delegate its tasks only to other depositaries must be deleted in order not to interfere with investment freedoms of AIF. The proposed provision has the effect of essentially restricting the depositary activity to EEA countries. However, investments in markets outside the EEA often go along with the requirement for a local custody of assets which under the

AIFM regime would be no longer feasible. In order to avoid this disastrous consequence for investment options of AIF, **depositaries should be allowed at least to outsource performance of their safe-keeping tasks to institutions outside the EU which are subject to comparable standards of regulation and supervision and which from the point of view of the depositary allow for a sufficient level of investor protection.**

Article 17 para. 4 is too restrictive also regarding the fact that tasks of the depositary may only be delegated to other credit institutions. This requirement is not necessary as long as the depositary itself holds the status of a credit institution. In this case, delegation should also be possible to other regulated and supervised financial service providers. Outside Europe, depositaries often do not hold the status of a credit institution.

12. *Art. 18 (Delegation)*

The very restrictive criteria for delegation as compared with Art. 13 of the UCITS Directive are not acceptable at least for Spezialfonds and 'conservative' fund types authorised for marketing to retail public. The UCITS Directive provides a proven and tested set of rules for outsourcing of collective asset management activities which should not be hastily and unduly tightened within the AIFM regime. Otherwise, management companies that manage both UCITS and AIF would be confronted with conflicting requirements for processes which tend to be set up in a uniform manner and hence, would be subjected to considerable burdens in financial and operational terms.

First of all, **the limitation of eligible counterparties to other AIFM in case of delegation of portfolio management or risk management activity does not account for the realities of institutional fund management.** Professional clients often request customised management solutions with investment strategies focusing on specific geographic/industry sectors or certain types of assets. As a consequence, management of AIF often requires specialised knowledge of particular markets which might not be available in the EEA, especially in case of funds with focus on geographic markets outside the Community. Moreover, there is no reason to require EU supervision of the outsourcer since the final responsibility for performance of the portfolio management function remains anyway with the outsourcing AIFM pursuant to Art. 18 para. 2.

In this context, we would like to point out a specific problem relating to the management of open-ended real estate funds. For OEREFs with globally diversified portfolios, it is essential to appoint property managers in the relevant local market in order to perform administrative tasks in relation to maintenance and rental of the real estate ('caretaker'). It remains an open question whether property management shall be deemed part of portfolio management or qualified as an administrative function, with some national supervisors taking the former view. In this case, however, the proposed Art. 18 para. 2 would amount to an effective limitation of OEREFs investment options to the EEA countries which would also significantly curtail diversification opportunities of European investors without any justifiable reason. Therefore, **should the restrictive rules on outsourcing of portfolio man-**

agement be maintained, we deem it absolutely necessary to expressly qualify property management of real estate as administration of assets by means of implementing measures pursuant to Art. 18 para. 5 letter a).

Secondly, **prior authorisation of each delegation, regardless of materiality of the delegated function, is absolutely disproportionate and might in considerable way hinder the processes of fund administration.** If at all, the requirement should be reduced to a pure information duty in accordance with Art. 13 para. 1 letter a) of the UCITS Directive.

Furthermore, **there is no discernible need for the absolute prohibition of delegation to the depositary** (Art. 18 para. 1, 3rd sentence). In case of a depositary providing services to several management companies as subsidiaries, combination of various management activities at the level of the parent company will result in noticeable economies of scale without necessarily creating conflicts of interest.

Lastly, **the prohibition of sub-outsourcing envisaged in paragraph 3 might have adverse effect on efficiency of institutional fund management and even prohibit certain management solutions of AIF.** This pertains in particular to multi-manager funds combining specialised management services in different market sectors within one product. The same applies for the business model of the German “Master KAG” which relies on flexible handling also of multilevel delegation arrangements. Open-ended real estate funds might also face serious difficulties in this respect in case of outsourcing of the property management function ('building management') and its partial relocation in terms of facility management ('caretaker'). A similar problem pertains to OREFs which delegate its portfolio management to a third party who subsequently needs to appoint local property managers for each real estate. As a consequence, management of real estate assets would be seriously impaired, if not impossible, by the proposed standards on delegation.

13. *Art. 20 and 23 (Disclosure to investors)*

The information requirements of the AIFM regime are in many parts similar to the disclosure standard for private customers applicable under the UCITS Directive and MiFID. This contradicts the regulatory objective of the draft Directive which is focused on marketing to professional clients. This group of investors tends to make individual arrangements with the fund manager in terms of the requested information and consequently, does not set any value on obtaining standard information at retail investor level. Therefore, it should be at least possible not to apply the information requirements of Articles 20 and 23 in case of explicit consent by the client.

14. *Art. 26 (AIF with controlling influence – scope)*

The undifferentiated inclusion of all funds with controlling influence on companies in Chapter V, Section 2 of the draft Directive would potentially also lead to open-ended real estate

funds which hold properties via Special Purpose Vehicles being classified as AIF with controlling influence. Investments in real property through holdings in real estate companies represent common practice with OEREFs which is essential in order to access certain real estate markets. With regard to the regulatory purpose of this section, however, inclusion of OEREFs does not appear to be justified. In practical terms, this could be avoided by clarifying that the *de minimis* exemption in Art. 26 para. 2 does always apply if the criterion on employed personnel is not met.

15. *Art. 31 para. 2 d), Art. 33 para. 1 e) (Prevention of marketing to retail investors)*

The arrangements for preventing AIF units from being marketed to retail clients required in Art. 31 para. 2 d) and Art. 33 para. 1 e) must be backed up by more details in order to effectively avoid an uncontrolled spill-over of these purely institutional products into the retail market. In this regard, special attention should be given to AIF subject to trading on secondary markets.

16. *Art. 34 (AIFM company passport)*

Compared with the UCITS IV Directive, the standards for the AIFM company passport are surprisingly liberal. For instance, the supervisor of the AIFM home Member State is granted only 10 working days for examining the submitted documents and transmitting them to the host State authority. Moreover, upon receipt of the transmission notification, the AIFM shall be entitled to start its cross-border operations. In contrast, the UCITS Directive provides for a period of one month for forwarding the information to the host State supervisor. In case of establishment of a branch, scrutiny and preparation on the part of involved supervisors may even take up to four months. The time-to-market of cross-border managed UCITS is further delayed by the requirement of product authorisation for which additional two months must be taken into account.

Authorisation for cross-border management of different non-UCITS types, potentially including also nationally regulated retail products such as open-ended real estate funds or balanced funds, by means of the AIFM company passport appears too extensive, especially in view of Art. 34 para. 5 establishing a ban on more restrictive national requirements in these circumstances.

17. *Art. 35 and 39 (EU passport for third-country AIF and AIFM)*

Art. 33 lays down the requirements for AIFM willing to market self-managed AIF cross-border. The marketing provisions in Art. 35 and 39, on the other hand, do not contain any limitations to 'own' funds. Thus, it appears that the authorised AIFM shall also be able to market products of unregulated third-country fund managers within the EU under the passport rules of Art. 35 and 39 which, in our view, cannot be permitted.

Article 35 imposes no requirements on the regulatory framework for AIF domiciled in third countries. It is therefore possible for EU fund manager authorised as AIFM to market completely unregulated products that are not subject to any supervision under the AIF passport. The reporting obligations of Articles 21, 24 and 31 are no adequate substitute for potentially absent product supervision. This situation will result in a considerable distortion of competition between regulated EU funds and third-country funds and can in case of failure even further undermine investor confidence in fund investments.

As regards the company passport in Article 39, the proposed reciprocity of market access does not create additional value for EU fund managers. In particular, it must be expected that US providers will enter the EU market not directly from the USA, but via production hubs in the Caribbean (Bahamas, Cayman Islands). A comparable access to the Caribbean sales markets is definitely no priority for European management companies.

18. *Art. 51 (Transitional provision)*

Within one year after the expiry of the period for national transposition, already existing AIFM shall be obliged to file applications for re-licensing. Since the application can be approved only if an AIFM fulfils all conditions of the Directive according to Art. 6 para. 1, it must be assumed that as of this point in time, the approval requirements for marketing of AIF (Art. 31) and for delegation of activities (Art. 18) must be in place.

Against this background, it can be expected that within one year after coming into force of national provisions implementing the AIFM regime, applications for the following approvals must be filed with the competent supervisor:

- Licence of the management company as AIFM
- Approval of the modified contractual terms of all existing AIF
- Authorisation of the conditions for delegated activities

Having regard to the applicable time limits for modification of contractual terms, the applications in question would even need to be filed within the first half-year after beginning of the transitional period in order for the application for AIFM licence to be filed in due time. This would result not only in insurmountable operational efforts within the industry, but also present the supervisory authority with an irresolvable task, especially since the number of funds requiring adaptation to the AIFM regime only in Germany should be a middle four-digit figure. In a worst-case scenario, an authorisation bottleneck must be expected which would prevent timely implementation of the Directive.

Should our interpretation of the practical implementation efforts be confirmed and should the draft Directive remain essentially unchanged, a **transitional period of at least three years would be absolutely necessary.**