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European Commission
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BELGIQUE

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CJ/SJ n°2274/Div.

AFG ANSWER TO THE EU COMMISSION CALL FOR EVIDENCE ON PRIVATE PLACEMENT REGIMES IN THE EU

Dear David,

AFG[1] welcomes the initiative taken by the European Commission to launch a call for evidence on private placement at EU level, following the White Paper of November 2006.

The work on this concept will no doubt prove very useful and we hope the Commission will be able to convince Member States to agree on common definitions of eligible financial products and investors for a "private placement" regime.

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1 The Association Française de la Gestion financière (AFG)[1] represents the France-based investment management industry, both for collective and discretionary individual portfolio managements.

Our members include 365 management companies and 772 investment companies. They are entrepreneurial or belong to French or foreign banking or insurance groups.

AFG members are managing more than 2500 billion euros in the field of investment management, making in particular the French industry *the leader in Europe in terms of financial management location* for collective investments (with more than 1500 billion euros managed, i.e. 22% of all EU investment funds assets under management, wherever the funds are domiciled in the EU) *and the second at worldwide level*. In the field of collective investment, our industry includes – beside UCITS – the employee savings schemes funds and products such as regulated hedge funds/funds of hedge funds as well as a significant part of private equity funds. AFG is of course an active member of the European Fund and Asset Management Association (EFAMA) and of the European Federation for Retirement Provision (EFRP). AFG is also an active member of the International Investment Funds Association (IIFA).

We would like, though, to stress that, even if it proves – as we wish – successful, it would only bring a limited progress towards the building up of a fully open and levelled playing field for financial products in Europe. Two main reasons supporting our views:

- first, purely institutional investors are, in the retirement field that will be tomorrow's main market, inevitably on the decline: many defined benefit schemes are being closed while in defined contribution plans, which are growing rapidly, the risk rewards are borne by the "end investors", which will not be eligible for "private placement". The insurance market is also moving towards unit-linked contracts: to make it short, the concept of private placement is not fit for the fast growing "instividual" market.

- Second, one of the main goals of the asset management industry is to make financial innovation accessible to all types of investors, and not only to institutions or high net worth individuals. We think, thus, that the useful action on private placement should not slow down the necessary work on revising the UCITS Directive which should lead to an easier inclusion of innovative financial products within the eligible assets of UCITS and to the setting up of a new "alter UCITS" regime ensuring a full passporting of alternative funds

We should also keep in mind that it would be naive to open up the European markets to offshore products without ensuring that the same move is simultaneously made by the other main world markets.

Having said that, you will find below our detailed answers to the EU Commission's questions.

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1. Problem Definition:

As a general comment, we wish to stress the difficulty of handling the topic since there is no common understanding of what private placement is. To illustrate it, we recall the statement made by EFAMA, the European Association for the industry funds, in its comparative survey for hedge funds[2]: "(…) *there is no regulatory consistency over what constitutes a 'private' placement. This definition is given sometimes by reference to the "institutional" nature of the investor, sometimes on the basis that there is a limited number of subscribers or sometimes by the fact that the client makes a specific request to purchase units in the fund*."

Question 1a: Is private placement a useful concept in national laws? What is the size and structure of the business that developed under the national regimes (geographical and product breakdown, dominant players, etc.)?

In France, there is no real private placement regime as such.

However, a category of qualified investors eligible to buy funds without public offering already exists and has been broadened since the implementation of the Prospectus Directive into French law. These investors have - when their own rules make it possible - access to

[2] Published in November 2005.

simplified investment rules and simplified registration funds, whose market has represented 80 billion euros in 2006.

Question 1b: Does the absence of a common understanding of private placement result in a single market failure? Do differences between national regimes, i.e. the absence of an EU private placement approach prevent or discourage possible cross-border investment transactions? Are any sections particularly affected? How do problems manifest themselves?

A pan-European and workable definition of which investors would be eligible to "private placement" rules would clearly help to strengthen the market.

2. Objectives: Designing a 'showcase':

a) borderline between private placement and public offering:

Question 2: How can the borderline between private placement and public offering best be defined? What should be the legal consequences of leakage of private deals into the public sphere (including any liability for the original issuer/placement agent)?

To define the borderline between private placement and public offering, the European Commission could think over re-using the criteria set up in the Prospectus Directive for the exemption of closed-ended funds from public offering/marketing to the public in order to apply them to UCITS funds, non-harmonised funds and offshore finds.
Though, we foresee a problem regarding the resale to the public of units bought via private placement and the control that the offeror would have on the distributor reselling the units acquired through private placement. Typically the situation would be where an asset management company places a fund to a bank (qualified investor) that would resell the fund to its retail clients. In that situation, what would be the asset management company's responsibility and how to protect the retail investor buying funds that were not dedicated to its intent? In fact, if retail investors are targeted, the registration of the product should be mandatory (e.g. UCITS notification procedure) and funds should obey to the UCITS Directive.

And in any case the original issuer/placement agent should not be deemed liable in case a product sold via private placement is resold to the public.

b) Investment products to be sold in the framework of private placement:

Question 3: Are there some types of investment products which could benefit in particular from private placement; e.g. closed ended funds or non harmonised open ended funds? Does it make sense to develop a private placement regime exclusively for some designated products? Or should we build a framework that is open to any types of security?

If the European Commission succeeds in finding a pan-European definition of which investors would benefit from the desirable private placement regime, it is true that it will still be necessary to define which financial products would be eligible for private placement: if it is not the case, national authorities will still be able to block their "importation" and marketing in their jurisdictions.

It is probably necessary to limit the scope to products and contracts falling under the responsibility of a registered and monitored financial provider entity (bank, insurance company, investment firm, asset manager…).

The product should also be authorised for sale to sophisticated investors in the "providing country". We are conscious that many national regulators will be reluctant to accept such an open clause as it is clear that some European countries have only a very small internal market while they are strong exporters of financial products. The solution to this problem lies clearly in an ambitious strengthening of co-operation between regulators, under the authority of an enhanced CESR, CEIOPS and CEBS, if not in the creation of a truly European financial regulator.

We are aware that the opening to off-shore products would be even more difficult. A possible solution would be to limit it, in a first stage, to products provided by a European regulated entity. A full reciprocity should anyway be sought for, as it would arguably be illogical to open up the European markets while the markets of our world competitors are not open to European products.

c) Eligible investors in private placement:

Question 4: What investors should be eligible counterparties under private placement (i.e. capable of being approached on a private basis with a view to possible investment)? Should eligibility be defined following the definition of "eligible counterparty" or of "professional clients" in MiFID, or following the definition of a "qualified investor" of the Prospectus Directive? Or would you suggest an alternative definition?

The Prospectus Directive could be a possible basis to define the eligible investors in order to be consistent with the closed-ended funds and substitute products' regimes and therefore to ensure a level playing field.

d) Eligible providers in private placement:

Question 5: How should the supply side of a private placement be regulated? Is there a need for additional rules or would the respective prudential requirement for the specific market player suffice? Should financial institutions from some/all third countries be recognised?

The provider should be domiciled, registered and therefore monitored by a national regulator located in the EU.

e) Investor protection:

Question 6: Despite being limited to a (to be defined) set of sophisticated investors, would there still be a need for investor protection rules? Is there a need to include rules regarding the eligibility of certain players the owners/unit holders/participants of which might be more vulnerable (e.g. pension funds)?

Since the funds would be placed to eligible investors who understand the risks of the products, there is no need for European investor protection rules. It must be recalled, though, that national laws and regulations will still apply to investors, thus strongly limiting, in practice, the interest of the private placement regime.

f) Restrictions and requirements:

Question 7: Which kind of restrictions/requirements would need to be deactivated for a private placement regime to deliver significant benefits? Which would be seen as excessive? How much discretion can be left to local authorities in defining these rules without risking a minimum level of harmonisation?

Regulating the provider would be a useful monitoring mechanism. The provider should know what it is providing. As a suggestion, the European Commission could elaborate a list of criteria such as the 13 that AMF put in place for French alternative investments.

In any case, regulators should put in place a strong cooperation between them.

Question 8: What would you consider best practice at national level among the existing private placement regimes: with respect to private placement across borders?

A regime inspired by the Dutch private placement regime (close to the Prospectus Directive regime) and the Swiss private placement regime (possibility to sell funds without prior marketing authorisation to 20 qualified investors, including asset managers) seems to be a good one.

While drafting the regime of private placement, the European Commission should also include provisions regarding the language to use and the authorised advertisement of the funds. See below for more details (answer to question 9).

In addition, the taxation regime should ensure a level playing field between all financial instruments.

g) Other issues:

Question 9: Are there any other relevant issues to be analysed that have not been addressed in this note?

The European Commission has not mentioned the following topics:

- tax issue: it is true that it is a very relevant topic, but it is a tricky one, and the European Commission is right to put it aside and deal with it separately, as there are discrepancies among Member States on this topic.

- language to be used: it should only required to provide documents to eligible investors in a language common in the sphere of international finance.

- advertisement of the funds: it should be authorised but only in specialised wealth management magazines to the intent of the eligible investors for private placement.

3. Assessing the current EU framework

Question 10: a) Is there a risk that the delivering definitions of eligible investors will create problems in their application? If yes, please describe these problems and their impacts.

b) Could the private placement features of the directives with respect to:
- disclosure
- conduct of business
- information requirements
- suitability and appropriateness test for investors

be regarded as sufficient and appropriate for an EU private placement regime? If not, how should these provisions be amended?

c) Are any other elements missing that would be regarded as crucial for an effective EU private placement regime?

a) There is clearly a risk that the definition of eligible investors will create problems since there are several different concepts in the Member states.
b) Yes. The European Commission should have named the directives that were targeted in the question, i.e. the Prospectus Directive as well as the MiFID.
c) Finally, the tax issue is an issue that would require an impact assessment to show the impacts of the tax barriers on the single market.

Question 11: In the event that the provisions for cross-border private placement in the EU needed to be improved: Would this require new rules (e.g. a directive) or could existing EU law be used to shape an EU regime, or would even a light approach, e.g. harmonisation of national rules combined with mutual recognition suffice to establish an effective regime?

Since a Regulation would be directly applicable in the Member States, it is preferred to a Directive. Mutual recognition is not the solution to ensure a sufficient high level of harmonisation among Member States.

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We thank the European Commission for carefully reviewing the comments made by the European industry on the private placement and remain available to discuss further the content of this letter.

Should you have any questions, please contact myself at 01 44 94 94 14 (e-mail: p.bollon@afg.asso.fr); Stéphane Janin, Head of International Affairs Division, at 01 44 94 94 04 (e-mail: s.janin@afg.asso.fr); or Catherine Jasserand, Deputy Head of International Affairs Division, at 01 44 94 96 58 (e-mail: c.jasserand@afg.asso.fr).

Yours sincerely,

(signed)

Pierre Bollon