CD/ SJ – n° 2803/Div.

ESMA
11-13, Avenue de Friedland
75008 Paris

Paris, 17 January 2011

AFG response to CESR's Call for Evidence
Implementing measures on the Alternative Investment Fund Managers Directive

The Association Française de la Gestion financière (AFG)[1] is grateful for the opportunity to comment on CESR's Call for Evidence on the implementing measures on the Alternative Investment Fund Managers Directive (AIFMD).

General comments

First and foremost, we wish to highlight that we agree that matters relating to passports for non-EU AIFM and non-EU AIFs are not as pressing as other matters dealt with in CESR's call for evidence, as the third country provisions will not be implemented before 3 years after the entry into force of the AIFMD.

Regarding cooperation arrangements and exchange of information between competent authorities, we believe that the mechanisms applying to AIFMD should be similar to those applying to the UCITS Directive, unless a differentiation is duly justified by the specific nature of AIFs.

[1] The Association Française de la Gestion financière (AFG) represents the France-based investment management industry, both for collective and discretionary individual portfolio managements. Our members include 413 management companies. They are entrepreneurial or belong to French or foreign banking or insurance groups. AFG members manage 2,600 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 over 1,300 billion euros managed from France, i.e. 20% of all EU assets managed in the form of investment funds), wherever the funds are domiciled in the EU, and second at worldwide level after the US. In the field of collective investment, our industry includes – beside UCITS – employee savings schemes and products such as regulated hedge funds/funds of hedge funds, private equity funds, real estate funds and socially responsible investment. AFG is of course an active member of the European Fund and Investment 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).

More generally, we propose that the rules applying to AIFM are in line with the rules applying to asset management companies managing UCITS, for instance for the European passports, unless a differentiation is duly justified by the specific nature of AIFs. In any case, the requirements of AIFMD Level 2 should not be higher than those of the UCITS Directive, as AIFs are mainly marketed to professional investors (contrary to the marketing of UCITS which relates mainly to retail investors): professional investors are more educated than retail investors, and may take their own assessments in a better way than retail investors.

In addition, AFG believes that the principle of proportionality should be fully followed, depending on the type of AIF considered, for the whole Level 2 exercise, in order to adapt the Level 2 measures to the different types of funds, different underlying assets and different investment strategies (e.g. how to find a one-size-fits-all approach for single hedge funds and real estate funds?). We know that European institutions decided at Level 1 to follow a "*everything but UCITS*" approach, encompassing nearly all non-UCITS funds, but there is a high danger at Level 2 to provide for too detailed provisions – which would probably fit the specificities of some types of AIFs but not the specificities of all types of AIFs.

Please find below AFG detailed comments, shown in bold.

*
**

Detailed comments

Question for the call for evidence

1. Which categories of investment manager and investment fund will fall within the scope of the Alternative Investment Fund Managers in your jurisdiction? Please provide a brief description of the main characteristics of these entities (investment strategies pursued, underlying assets, use of leverage, redemption policy etc).

French investment funds in the scope of the AIFMD
Total AUM = EUR 712 billion

Tailored funds ("fonds contractuels"): EUR 19 Billion

- Subscription : 250,000 € minimum
- NAV : quarterly
- Investment rules defined by bilateral contract
- Mere declaration to AMF

Qualified investor funds - French QIFs ("OPCVM ARIA"): EUR 12.5 Billion

- Subscription : 125,000 € minimum

- NAV : monthly
- Flexible investment rules
- AMF authorised

Funds of hedge funds: EUR 16.6 Billion

- Subscription : 10,000 € minimum
- NAV : monthly
- Investment in underlying funds has to comply with 4 general principles
- AMF authorised

Private equity funds: EUR 34 Billion

- Subscription : depending on fund types (FCPR etc)
- Lock up : 5 years minimum
- 40 % of portfolio invested in non-listed companies
- AMF authorised

Real Estate funds ("OPCI" etc): EUR 8 Billion

- Lock up : possibly three years maximum
- NAV : twice a year
- 60 % minimum in real estate
- AMF authorised

Non coordinated structured funds: EUR 62 Billion

- Subscription : distribution closely monitored
- Formula-based performance
- AMF authorised

Managed future funds ("FCIMT"): EUR 0.3 Billion

- Subscription : 10,000€ minimum
- NAV : daily
- AMF authorised

Nationally regulated "general purpose" funds: EUR 560 Billion

- Most investment rules similar to UCITS (except some ratios, assets may include commodities, etc)

2. Among the topics that will be covered by the implementing measures, which do you consider would be most appropriately adopted in the form of regulations or directives? Please explain your choice.

We believe that Regulations would be the most appropriate instruments to cover most topics:

- Regulations ensure a higher level of European harmonisation as compared to Directives by avoiding divergent national transpositions;

- Regulations allow a faster implementation as they do not require national transposition by the authorities of the different Member States;

- Last but not least, in the new context of setting of an empowered ESMA (as compared to the less empowered previous CESR), adopting Regulations rather than Directives would make sense as they would facilitate the action of ESMA in monitoring and acting upon the right and equal implementation of European provisions across Europe.

3. Can you identify useful sources of data and statistical evidence from which CESR could benefit in the preparation of its advice?

PART I: GENERAL PROVISIONS, AUTHORISATION AND OPERATING CONDITIONS

Issue 1a

1. CESR is requested to advise the Commission on the procedures for AIFM which choose to opt-in under this Directive in accordance with Article 3(4). CESR should consider whether there are specific reasons not to use the same procedure that applies to AIFM that do not benefit from this exemption.

We cannot see any reason to apply different procedures for such beneficiaries; indeed, we believe that a level playing field should be ensured among all players.

2. This advice should include procedures specific to the case of AIFM from third countries seeking to opt in after the phasing-in of the third country regime; in particular the determination of the Member State of reference.

Issue 1b

1. CESR is requested to advise the Commission on how to identify the portfolios of AIF under management by a particular AIFM and the calculation of the value of assets under management by the AIFM on behalf of these AIF.

2. The advice should identify options on how to determine the value of the assets under management by an AIF for a given calendar year. It should indicate the method or methods CESR regards as preferable.

3. CESR is invited to consider how the use of different forms of leverage influences the assets under management by an AIF and how this should best be taken into account in the calculation of assets under management.

4. CESR is requested to advise the Commission on how best to deal with potential cases of cross-holdings among the AIF managed by an AIFM, e.g. funds of AIF with investments in AIF managed by the same AIFM.

5. CESR is requested to advise the Commission on how to treat AIFM whose total assets under management occasionally exceed and/or fall below the relevant threshold in a given calendar year. As part of this work, CESR is requested to specify circumstances under which total assets under management should be considered as having occasionally exceeded and/or fallen below the relevant threshold in a given calendar year.

We agree that circumstances under which total assets under management (AUM) should be considered as having occasionally exceeded the relevant threshold in a given calendar year should be specified. We suggest that, when the total AUM has exceeded the relevant threshold over a given period of time (for example over 3 or 6 months) by a given percentage (for example 10%), the AIFM should be required to comply with the full Directive.

6. CESR is requested to advise the Commission on the content of the obligation to register with national competent authorities for the entities described in Article 3(2).

7. CESR is requested to advise the Commission on suitable mechanisms for national competent authorities in order to gather information from these entities in order to effectively monitor systemic risk as set forth in Article 3(3). To that end, CESR is requested to specify the content, the format, and modalities of the transmission of the information to be provided to competent authorities. CESR is invited to consider the consistency with its advice regarding the Issue 25 (reporting obligations to competent authorities).

8. CESR is requested to advise the Commission on the obligation of AIFM to notify competent authorities in the event they no longer comply with the exemptions granted in Article 3(2).

Issue 2

From a general perspective on this Issue, as for other Issues, we wish ESMA to be as close as possible to the UCITS regime, in order to make it easier for managers to manage different types of assets and to avoid any risk of regulatory arbitrage.

1. CESR is requested to provide the Commission with a description of the potential risks arising from professional negligence to be covered by additional own funds or the professional indemnity insurance referred to in Article 9(7).

2. CESR is requested to advise the Commission on how the appropriateness of additional own funds or the coverage of the professional indemnity insurance to cover appropriately the potential professional liability risks arising from professional negligence referred to in Article 9(7) should be determined, including – to the extent possible and appropriate – the methods to calculate the respective amounts of additional own funds or the coverage of the professional indemnity insurance.

AFG would like to recall that the Directive gives the AIFM the choice between additional own funds and professional indemnity insurance to cover the potential professional liability risks arising from professional negligence. Indeed, we do not fully understand the relevance of the obligation for additional own funds with regards to this objective. The UCITS IV directive does not require management companies to have additional own funds to cover the potential professional liability risks arising from

professional negligence and it would not make sense to impose stricter requirements to management companies managing funds aimed at professional investors.

Moreover, we believe that it would be difficult to quantify the appropriate amount of such additional own funds, as the range of AIFs covered by the Directive is extremely broad: each category of AIF would require tailored requirements.

Besides, it would seem difficult for internally managed funds to comply with such requirement.

Lastly, regarding the choice offered of a professional indemnity insurance cover, we would like to emphasize on the need to keep such cover at a reasonable level. Imposing a high level of professional indemnity insurance cover would generate a heavy burden for managers established in European countries where the insurance market is not as mature as in other countries and make it very difficult for them to find an adequate cover in their home countries.

3. CESR is requested to advise the Commission on the best way to determine ongoing adjustments of the additional own funds or of the coverage of the professional indemnity insurance referred to in Article 9(7).

4. CESR is invited to take account of work done in the context of the Capital Requirements Directive and to liaise as appropriate with CEBS and CEIOPS on this issue.

We would like to note that the work undertaken in the context of the Capital Requirements Directive has not been finalised yet and that it would be very premature at this stage to integrate it in this reflection.

Issue 3

For Issues 3 to 10, we ask CESR again to replicate the UCITS provisions as far as possible, for the reason mentioned above.

1. CESR is requested to advise the Commission on criteria to be used by the relevant competent authorities to assess whether AIFM comply with their obligations under Article 12(1).

AFG believes that the principle of proportionality should be taken into account when assessing whether AIFMs comply or not with their obligations under the directive. Indeed, risk management may be organised differently with respect to a leveraged hedge fund or a plain real estate fund. In other words, proportionality should be applied depending on the type of AIF considered.

Issue 4

1. CESR is requested to provide the Commission with a description of the types of conflicts of interests between the various actors as referred to in Article 14(1).

2. CESR is requested to advise the Commission on the reasonable steps an AIFM should be expected to take in terms of structures and organisational and administrative procedures in order to identify, prevent, manage, monitor and disclose conflicts of interest.

The Commission would encourage CESR to target an appropriate level of consistency with the corresponding provisions of other directives, such as UCITS and MiFID, while taking due account of the differences between the regulated populations.

Issue 5

1. CESR is requested to advise the Commission on the risk management systems to be employed by AIFM as a function of the risks that the AIFM incurs on behalf of the AIF that it manages and on the criteria that competent authorities should take into account when assessing for the AIF managed by the AIFM whether the risk management process employed by the AIFM is adequate in order to identify measure, manage and monitor appropriately all risks relevant to each AIF investment strategy and to which each AIF is or can be exposed.

Following the principle of proportionality, private equity funds do not require the same risk control arrangements than other types of AIFs or even than UCITS and therefore should be treated in an adapted manner.

It is the same issue for real estate funds.

More generally, our members believe that it would not be possible to design a generic one-size-fits-all risk framework for AIFs.

In particular, CESR is requested:

a) to advise on the categories of risk relevant to each AIF investment strategy and to which each AIF is or can be exposed and the methods for identifying the risks that are relevant for the particular AIF investment strategy or strategies so that all risks are adequately identified.

Some of our members are of the opinion that AIFMs should maintain a risk management policy including a mapping of the risks of each AIF they manage and the risk monitoring methods applied. AIFMs should at least consider market risk, liquidity risk, operational risk, credit risk as well as the main risks that are specific to the relevant investment strategy. Such specific risks may be for example sensitivity to long/short equity spread, big cap/small cap spread, credit spread, options greeks, term structure as well as sensitivity to corporate events, country risks, legal risks, regulatory risks, size of the AIF.

b) to advise, to the extent possible, on methods for quantifying and measuring risks including the conditions for the use of different risk measurement methodologies in relation to the identified types of risk so that overall risk exposures as well as contributions to overall risk from each risk factor are properly measured.

Identified risks must be disclosed in the fund documentation. Although many risks of AIFs may be of a qualitative nature, the AIFM could additionally, in some cases and if possible, quantitative measures for each risk identified.

The AIFM should identify the key risks of each investment strategy it manages. The management of the AIFM should set risk limits for such key risks. When possible compliance with such risk limits should be monitored on a systematic basis using quantitative risk measures. Both the risks and the risk measurement methodologies will be specific to each AIFM / AIF. As a part of the Risk Management Policy the AIFM should define the methods used for measuring the key risks of the AIFs it manages.

In addition to monitoring the level of each risk, the AIFM should when possible analyse the probability distribution of each risk parameter as well as the correlation between risks. The risk monitoring methods as well as the implemented risk limits should to the extent possible take into account the specifics of the probability distribution and correlation of each risk. On this point we believe some AIFs will need to go further than UCITS funds as the probability distribution of AIF returns may for certain AIF strategies be more leptokurtic/skewed than that of traditional funds.

Scenario based tools may be useful in order to evaluate the effects of one or a combination of risks playing out in extreme events.

c) to advise on adequate methods for managing and monitoring all such risks so that the AIF risk exposures respect at all times the risk objectives of the AIF.

2. CESR is requested to advise the Commission on the appropriate frequency of review of the risk management system. CESR is invited to consider whether the appropriate frequency of review varies according to the type of AIFM or the investment strategy of the AIF.

3. CESR is requested to advise the Commission on the conditions for the appropriate risk governance structure, infrastructure, reporting and methodology, in particular, on how the risk management function shall be functionally and hierarchically separated from the operating units, including the portfolio management function.

4. CESR is requested:

a) to advise how the principle of proportionality is to be applied by competent authorities in reviewing the functional and hierarchical separation of the functions of risk management in accordance with Article 15(1).

b) to advise on criteria to be used in assessing whether specific safeguards against conflicts of interest allow for the independent performance of risk management activities and that the risk management process satisfies the requirements of Article 15 and is consistently effective. This advice will be particularly relevant in cases where full separation of functions is not considered proportionate. CESR is encouraged to provide the Commission with a non-exhaustive list of specific safeguards AIFM could employ against conflicts of interest referred to in the second subparagraph of Article 15(1).

5. CESR is requested to advise the Commission on the content of the requirements referred to in Article 15(3).

6. This advice should at least address the following issues:

a) the content of an appropriate, documented and regularly updated due diligence process when investing on behalf of the AIF, according to the investment strategy, the objectives and risk profile of the AIF;

b) the criteria to be used by competent authorities when assessing whether the risks associated with each investment position of the AIF and their overall effect on the AIF's portfolio can be properly identified, measured, managed and monitored on an ongoing basis, including through the use of stress testing;

AFG members believe that identifying, measuring, managing the risks associated with *each* investment position of the AIF on an ongoing basis would not be relevant as such to identify activities presenting systemic risk, as positions can be negatively correlated. It would be more adequate to perform this exercise at the level of each investment strategy, as AIFMs might regroup some positions in different categories in order to appropriately and efficiently monitor the global risk of the portfolio, or at the level of the portfolio itself. Moreover, it would be burdensome for competent authorities to due diligence the risk management process at the technical detail.

Furthermore, for some specific investments such as acquisitions of real estate properties in future state of completion, the risk assessment can only be made through the investment strategy of the fund.

c) appropriate stress testing procedures and their frequency pursuant to Article 15(3)(b);

d) the criteria to be used in assessing whether the risk profile of the AIF corresponds to the size, portfolio structure and investment strategies and objectives of the AIF as laid down in the AIF rules or instruments of incorporation, prospectus and offering documents.

Issue 6

1. CESR is invited to advise the Commission on the content of rules that are proportionate and necessary for specifying the general obligations placed on AIFM by Article 16(1) and (2).

AFG believes that disclosing to professional investors that liquidity mechanisms (e.g. "gates") are in place should be a sufficient obligation. Once they are informed, professional investors are able to gauge the liquidity mechanisms attached to an AIF.

We therefore think that there is no further need to regulate the liquidity mechanisms themselves. Keeping flexibility in the area of liquidity mechanisms is crucial as it might be useful for AIFM to be able to resort to new mechanisms, in case of a crisis for instance. In any case, the AIFM should monitor the time period during which each investment can be liquidated as well as the estimated cost for such liquidation, in order to prevent potential liquidity mismatches.

Besides, AFG would like to note that the requirements applying to closed ended real estate funds should be tailored to their specific nature, as by nature their portfolios hold less liquid assets than other types of AIFs.

2. In particular, CESR is invited to advise on:

a) the systems and procedures to be implemented by the AIFM in order to comply with its obligations under Article 16(1), having regard for the appropriateness of these systems and procedures for different types of AIFM and the AIF they manage.

b) the content of the obligation for AIFM to regularly conduct stress tests, under normal and exceptional liquidity conditions, which enable it to assess the liquidity risk of the AIF and monitor the liquidity risk of the AIF accordingly.

c) the circumstances under which the investment strategy, liquidity profile and redemption policy for each AIF managed by an AIFM can be considered to be consistent. In this context, CESR is invited to consider all relevant aspects of the redemption policy, including mechanisms that can be invoked in exceptional circumstances, and assess their consistency with the investment strategy and liquidity profile.

Issue 7

1. CESR is invited to advise the Commission on the content of rules that are necessary and proportionate for an AIFM to fulfil its obligations under Article 17.

AFG members would like to make ESMA aware that, because of the specificities of the securitisation market, they are not able to comply with due diligence obligations relating to securitisation positions on an ongoing basis. In practice, they could only do due diligence at the outset or check that the prospectus includes a commitment by the originator to retain no less than the required 5%. On an ongoing basis, it is the responsibility of regulators to monitor that originators comply with their obligations as it would be extremely difficult for investors (including management companies) to do so.

In addition, as mentioned above, the Capital Requirements Directive has not been finalised yet, and it should provide more detail at Level 2 regarding this retention obligation.

In any case, the article 17 of the AIFM Directive states that "to remove misalignment between the interest of firms that repackage loans into tradable securities and originators and AIFLM that invest in these securities or other financial instruments..." and define the following framework "a) the requirements that need to be met by the originator, the sponsor or the original lender... ". As Credit Default Swaps are not repackaged loans, CSOs are not concerned by the 5% ratio of net economic interest retention. Furthermore, as originator, original lender, sponsors do not exist in n arbitrage CLO actively managed; these transactions are not concerned by this 5%ratio. Our understanding is that the US regulation will follow this route.

So, the approach to be followed by ESMA should be proportionate and realistic.

2. In particular, CESR is invited to advise on:

a) the requirements to be met by the originator, the sponsor or the original lender, in order for an AIFM to be allowed to invest in securities as defined in Article 17.

b) the qualitative requirements to be met by an AIFM in order to comply with their obligations under Article 17.

Issue 8

1. CESR is invited to advise the Commission on the content of rules that are proportionate and necessary for specifying the general obligations placed on an AIFM by Article 18(1).

AFG believes that the requirements applying to AIFM should be in line with those applying to UCITS managers, unless a differentiation is duly justified by the specific nature of AIFs.

2. In particular, CESR is requested to advise on the procedures and arrangements to be implemented by the AIFM, having regard to the nature of the AIF managed by the AIFM, in order to comply with its obligations under Article 18(1).

Issue 9

1. The criteria concerning the procedures for the proper valuation of the assets and the calculation of the net asset value per share or unit to be used by competent authorities in assessing whether an AIFM complies with its obligations under Article 19(1) and Article 19(3).

CESR is invited to consider how these procedures should be differentiated to reflect the diverse characteristics of the assets in which an AIF may invest.

2. The type of specific professional guarantees an external valuer should be required to provide so as to allow the AIFM to fulfil its obligations under Article 19(5).

CESR is asked to consider the impact of the required guarantees on the availability of external valuers to the AIFM industry.

First, AFG members would like to recall the possibility for the AIFM to do the valuation internally (with an appropriate management of potential conflicts of interest). Therefore, it would also make sense if a valuer belonging to the same group as the AIFM could be used, in cases where an external valuer is used (with an appropriate management of potential conflicts of interest).

Second, we would like to highlight the lack of consistency between Art.19.6 which prevents an external valuer from delegating the valuation function to a third party, and Art.20 that allows delegation chains (provided some conditions are fulfilled). We believe that there might be cases whereby a delegation of the valuation by the external valuer might be justified and should be allowed provided some conditions are fulfilled. In terms of economies of scale, which benefit ultimately to investors by reducing costs, it is important to allow for such valuation delegation chains.

Third, we believe that the professional guarantees to be provided by external valuers should be materialised at European level, in order to ensure the same level of safety throughout Europe. For example, a frame of reference or the compliance to recognised international norms might be a possible option. In any case, the guarantees should not be limited to the premium paid by the AIFM.

Last, we wish to remind ESMA that the requirements of the AIFMD and those of the UCITS directive should be consistent so that a management company managing both types of funds does not have to comply with contradicting obligations.

3. The frequency of valuation carried out by open-ended funds that can be considered appropriate to the assets held by the fund and its issuance and redemption frequency.

With regards to frequency, we are of the opinion that the official net asset value of an open-ended AIF should be calculated at least each time there are subscriptions or redemptions in the AIF.

Issue 10

1. CESR is invited to advise the Commission on the content of rules that are necessary and proportionate to ensure that an AIFM fulfils the conditions under Article 20(1) and Article 20(2).

2. In particular, CESR is invited to advise the Commission on the following, which are applicable both to cases of delegation and sub-delegation:

a) the criteria that competent authorities should use to assess whether the reasons supplied to justify the entire delegation structure of an AIFM are objective.

AFG is of the opinion that the AIFM Level 2 should not require more details than the UCITS Directive, in particular knowing that the AIFM passports are limited towards professional investors only, contrary to the UCITS Directive passports which apply to retail investors as well. It is sufficient to recall that the management company giving the delegation shall remain responsible for any decision to delegate one or more of its functions. There should be only the requirement for the AIFM to assess whether a delegation is justified, to carry out due diligence obligations on these delegations and that monitoring mechanisms on these delegations are under its control.

Besides, there is no concept of "*objective reason*" in the UCITS directive.

b) the circumstances under which a delegate should be considered to have sufficient resources to perform the tasks delegated to it by an AIFM; and to be of sufficiently good repute and sufficiently experienced to perform these tasks.

c) the types of institutions that should be considered to be authorised or registered for the purpose of asset management and subject to supervision. CESR is invited to consider whether to employ general criteria or to specify categories of eligible institution in this context.

d) in the event of a delegation of portfolio or risk management to an undertaking in a third country, how cooperation between the home Member State of the AIFM and the supervisory authority of the undertaking should be ensured.

e) the circumstances under which a delegation would prevent the effective supervision of the AIFM, or the AIFM from acting, or the AIF from being managed, in the best interest of its investors.

3. CESR is invited to advise the Commission on the content of rules that are necessary and proportionate to ensure that an AIFM fulfils the conditions under Article 20(3).

4. In particular, CESR is invited to advise on:

a) the type of evidence necessary for an AIFM to demonstrate that it has consented to a sub-delegation

b) the criteria to be taken into account when considering whether a sub-delegation would result in a material conflict of interest with the AIFM or the investors of the AIFM; and for ensuring that portfolio and risk management functions have been appropriately segregated from any conflicting tasks; and that potential conflicts are properly identified, managed, monitored and disclosed to the investors of the AIF.

c) the form and content the notification under Article 20(3) (b) should take in order to ensure that the supervisory authorities have been properly notified.

5. CESR is also invited to advise the Commission, in relation to Article 20(2), on the conditions under which the AIFM would be considered to have delegated its functions to the extent that it had become a letter-box entity and could no longer be considered to be the manager of the AIF.

AFG deems that an AIFM is not a letter-box entity as long as it can control the delegations and that it performs at least one of the investment management functions listed in Annex I of the Directive.

PART II: DEPOSITARY

AFG would like to share the following three general comments on the depositary:

- **AFG wishes to recall that the depositary has a general obligation to act in the best interests of investors**

- **AFG would like to recall that the Directive that requires that each AIF should have a single depositary does not prevent an AIF from having several prime brokers**

- **AFG believes that the role and responsibility of the depositary should be defined according to the type and nature of assets held in safekeeping, i.e. whether they can be held in custody or not.**

Issue 11

1. CESR is requested to advise the Commission on the necessary particulars to be found in the standard agreement evidencing the appointment of the depositary. In its advice, CESR should take into account the consistency with the respective requirements in the UCITS Directive.

As explained previously, AFG supports aligning the requirements in the AIFMD on those in the UCITS Directive, unless the specificities of AIFs justify tailored provisions.

2. CESR is encouraged to provide the Commission, if possible, with a draft model agreement.

AFG members believe that drafting a model agreement would be a near impossible task, as Member States have each their own contract law and AIFs legal structures. Rather, we think that a list of obligations and mentions required in the agreement between the AIFM and the AIF's depositary would be more relevant and still very efficient in terms of convergence. This approach was rightly followed in UCITS IV Level 2. This would in particular reassert the core missions that the depositary may not waive and that the depositary has a general obligation to act in the best interests of investors.

In particular, two points should be explicitly tackled in such agreements:

- First, the cases for exemption of liability for the depositary should be reduced to an only strictly necessary minimum;

- Second, the depositary should not be allowed to add extra obligations for AIFMs beyond this list of obligations and mentions to be provided by ESMA.

Otherwise, if contracts are allowed to be flexible depending on the 'rapport de force' between the depositary and the AIFM, it would lead to a high heterogeneity which would ultimately be detrimental to a fair competition among AIFMs and to investors.

Issue 12

1. CESR is requested to advise the Commission on the criteria for assessing whether the prudential regulation and supervision applicable to a depositary established in a third country with respect to its depositary duties are to the same effect as the provisions laid down in European law.

In this regard, CESR is invited to take into account at least whether the depositary:
- is subject to specific capital requirements for the safe-keeping of assets.
- is subject to supervision on an ongoing basis.
- provides sufficient financial and professional guarantees to be able to effectively pursue its business as a depositary and meet the commitments inherent to that function.
- is subject to rules as stringent as those laid down in Article 21 AIFMD

We propose that the depositary located in a third country should comply with the following criteria:

- **The depositary is an entity regulated by a specific local regulation on the activity of banks and custodians, imposing specific capital requirements, and specific guarantees (insurance guarantees or mutualised fund guarantee supervised by local authorities);**

- **The depositary must be under the supervision of an official local authority supervising the activity of banks in the country where it is located.**

ESMA could make a list of entities eligible as depositaries in each third country in collaboration with their local authorities.

2. CESR is requested to advise the Commission specifying the criteria for assessing that prudential regulation and supervision of a third country applicable to the AIF depositary with respect to its depositary duties established in a third country is to be considered as effectively enforced. Inter alia, CESR should take into account whether the depositary is subject to the oversight of a public authority, meaning that, at least:
- the authority has the power to request information from the depositary
- the authority has the power to intervene with respect to, and sanction, the depositary

The issue no 12 relates to passports for non-EU AIFM and non-EU AIFs and as such is not as pressing as other matters dealt with in ESMA's call for evidence, considering that third country provisions will not be implemented before 3 years after the entry into force of the AIFMD. However, we would like to share some preliminary thoughts on the topic of non EU AIFs' depositary.

A comparative legal study of various legislations seems hardly feasible in practice. Instead, it appears more practical to require third country depositaries to request a declaration from their own national competent authorities certifying that their legislation is equivalent to the European legislation, at least if the related third country funds wish to benefit from the AIFM passport. Such declarations would be centralised by ESMA.

Furthermore, we are of the opinion that non EU AIFs marketed in the EU should disclose in their investor information documents if their depository is located in a third country and is regulated by the authority of a third country, and therefore not directly submitted to the provisions of the AIFM European Directive, but submitted to a local equivalent regime.

Issue 13.1

1. CESR is requested to advise the Commission on the conditions for performing the depositary functions pursuant to Article 21(6). CESR is requested to specify conditions for the depositary to ensure that:
- the AIF's cash flows are properly monitored;
- all payments made by or on behalf of investors upon the subscription of shares or units of an AIF have been received and booked in one or more cash accounts opened in the name of the AIF or in the name of the AIFM acting on behalf of the AIF or in the name of the depositary acting on behalf of the AIF at an entity referred to in Article 18 (1) (a) to (c) of Commission Directive 2006/73/EC in accordance with the principles set forth in Article 16 of Commission Directive 2006/73/EC.
- where cash accounts are opened in the name of the depositary acting on behalf of the AIF, none of the depositary's own cash is kept in the same accounts.

We agree that the depositary's own cash should not be kept in the same accounts as the cash belonging to AIFs. We actually advocate that sub-custodians segregate cash in 3 accounts: own cash, investment fund cash (i.e. for AIFs and UCITS, as being cash managed on behalf of third clients) and other clients' cash. In particular, it should be possible to differentiate at all times cash in foreign currency kept abroad by a sub-

custodian from cash belonging to its other clients. The ultimate goal must be to guarantee the practical ability to give the relevant cash back to the appropriate clients.

Moreover, from a systemic risk perspective, which is the main aim of AIFMD, this segregation in 3 different types of accounts is the best way to reduce this systemic risk to the minimum.

In its advice, CESR should take into account the legal structure of the AIF and in particular whether the AIF is of the closed-ended or open-ended type.

We believe there is no need to differentiate these conditions depending on the legal structure or type of the AIF, as it might generate an unintended arbitrage between different types of AIFs. Furthermore, there is no harmonised definition of closed-ended or open-ended funds at European level, and the borderline between the two categories is unclear very often (e.g. "hybrid" funds).

2. CESR is requested to advise the Commission on the conditions applicable in order to assess whether:
- an entity can be considered to be of the same nature as the entity referred to in Article 18 (1) (a) to (c) of Commission Directive 2006/73/EC, in the relevant non-EU market where opening cash accounts on behalf of the AIF are required;
- such an entity is subject to effective prudential regulation and supervision to the same effect as the provisions laid down in European Union law and which is effectively enforced.

Please refer to issue 12.

3. CESR is requested to advise the Commission on the conditions applicable in order to determine what shall be considered as the relevant market where cash accounts are required.

Issue 13.2

1. CESR is requested to advise the Commission on:
- the type of financial instruments that shall be included in the scope of the depositary's custody duties as referred to in point (a) of Article 21(7), namely (i) the financial instruments8 that can be registered in a financial instruments account opened in the name of the AIF in the depositary's books, and (ii) the financial instruments that can be "physically" delivered to the depositary;
- the conditions applicable to the depositary when exercising its safekeeping custody duties for such financial instruments, taking into account the specificities of the various types of financial instruments and where applicable their registration with a central depositary, including but not limited to:
o the conditions upon which such financial instruments shall be registered in a financial instruments accounts opened in the depositary's books opened in the name of the AIF or, as the case may be, the AIFM acting on behalf of the AIF;
o the conditions upon which such financial instruments shall be deemed (i) to be appropriately segregated in accordance with the principles set forth in Article 16 of Commission Directive 2006/73/EC9), and (ii) to be clearly identified at all times as belonging to the AIF, in accordance with the applicable law; and what shall be considered as the applicable law.

2. CESR is requested to advise the Commission on:

- the type of "other assets" with respect to which the depositary shall exercise its safekeeping duties pursuant to paragraph 7(b), namely all assets that cannot or are not to be kept in custody by the depositary pursuant paragraph to Article 7(a);
- the conditions applicable to the depositary when exercising its safekeeping duties over such "other assets", taking into account the specificities of the various types of asset, including but not limited to financial instruments issued in a 'nominative' form, financial instruments registered with an issuer or a registrar, other financial instruments and other types of assets.

First, AFG would like to propose a clear definition of assets "held in custody": we believe that they should be defined as all the assets that can be registered in an account open in the name of the custodian (for example a nominee account) on behalf of clients (hence the necessity of segregating the accounts), which includes the cash.

In addition, we think that depositaries should all register in their books the same types of assets, regardless of the Member State where they are located, in order to ensure that the obligations attached to these instruments are harmonised throughout the EU.

Furthermore, we also are of the opinion that the obligation to return the assets should apply to any AIF asset and registered in the depositary's name as well as to any asset held in custody by the depositary.

Regarding segregation of assets, the approach we propose for the segregation of cash (please refer to issue 13.1) should be applied more generally to all assets held by the sub-custodian, i.e. assets should be segregated in 3 accounts, namely: own assets, investment funds (i.e. AIFs and UCITS, i.e. assets managed on behalf of third clients) and other clients' assets.

3. To that end, CESR is requested to advise the Commission on:

- the conditions upon which the depositary shall verify the ownership of the AIF or the AIFM on behalf of the AIF of such assets;
- the information, documents and evidence upon which a depositary may rely in order to be satisfied that the AIF or the AIFM on behalf of the AIF holds the ownership of such assets, and the means by which such information shall be made available to the depository;
- the conditions upon which the depositary shall maintain a record of these assets, including but not limited to the type of information to be recorded according to the various specificities of these assets; and the conditions upon which such records shall be kept updated.

4. In its advice, CESR should also consider the circumstances where assets belonging to the AIF, are subject to temporary lending or repurchase arrangements or any type of arrangements under which financial instruments may be re-used or provided as collateral by the AIF or AIFM on behalf of the AIF, whether or not such arrangements involve transfer of legal title to the financial instruments, and advise on the conditions applicable to the depositary to perform its safekeeping duties accordingly.

AFG members are of the opinion that, while the depositary should be able to re-use a collateral, the legal ownership to the relevant financial instruments should not be transferred to it unless this is specified in the collateral agreement.

Issue 13.3

1. CESR is requested to advise the Commission on the conditions the depositary must comply with in order to fulfil its duties pursuant to Article 21(8). The advice shall include all necessary elements specifying the depositary control duties when inter alia verifying the compliance of instructions of the AIFM with the applicable national law or the AIF rules or instruments of incorporation, or when ensuring that the value of the shares or units of the AIF is calculated in accordance with the applicable national law and the AIF rules or instruments of incorporation and procedures laid down in Article 19.

AFG members would like to recall that the depositary performs its control duties only ex post, at a second level, after the AIF has carried out its own duties. For instance, the AIF may be in charge of the subscriptions/redemptions. Indeed, in this case, the AIF is responsible for these activities, as acting as an issuer of shares or units: it is then responsible for the management of its "issuer account (compte émetteur)"; conversely, the depositary actually is then a mere service provider.

Issue 14

1. CESR is requested to advise the Commission on the duties the depositary has to carry out in exercising its due diligence duties pursuant to Article 21(10), namely:
- procedures for the selection and the appointment of any third party to whom it wants to delegate parts of its tasks; and
- procedures for the periodic review and ongoing monitoring of that third party and of the arrangements of that third party in respect of the matters delegated to it.
2. CESR is encouraged to develop a comprehensive template of evaluation, selection, review and monitoring criteria to be considered by the depositary while exercising its due diligence duties under Article 21(10).

We believe that the selection of sub-custodians should be duly documented. It should be based on a procedure clearly set forth indicating how all delegates are selected (all delegates should be selected according to the same procedure). Part of the selection should be based on the solidity of the delegates (e.g. financial, human resources, expertise, skills); moreover, the procedures for controlling the delegates should be clearly defined and accepted by the delegates. The custodian should be able to demonstrate that the delegates are qualified and capable, that they were selected with all due care and that the custodian is in a position to monitor effectively at any time the delegated activities. Such procedures should be part of the custodian activity program approved by its local authority.

Furthermore, the majority of AFG members in our Working Group suggests that the auditor report should specify that the depositary complied in practice with its obligations in line with Directive provisions, in particular in terms of due diligence on its sub-custodians.

Issue 15

1. CESR is requested to advise the Commission on criteria to be satisfied to comply with the segregation obligation whereby the depositary shall ensure on an ongoing basis that the third party fulfils the conditions referred to in Article 21(10)(d)(iv).

AFG believes that segregation should be applied in the accountancy of the custodian and of each of its delegates and sub-delegates. Some of our Members think that segregation should also be compulsory at the level of CSD and ICSD.

In case the depositary delegates the custody of the assets to a third party, such delegation should be explicitly disclosed to investors.

Issue 16

1. CESR is requested to advise the Commission on the conditions and circumstances under which financial instruments held in custody pursuant paragraph 7(a) shall be considered as "lost" according to Article 21(11). In its advice, CESR should take into account the various legal rights attached to the financial instruments depending, for example, on the legal concepts ('ius ad rem' vs. 'ius in personam') used in the jurisdiction where they have been issued and any legal restrictions applicable to the place where they are kept in (sub-) custody.

2. In its advice, CESR should specify circumstances when such financial instrument should be considered permanently "lost", to be distinguished from circumstances when such financial instruments should be considered temporarily "unavailable" (held up or frozen).

To that end, CESR shall consider inter alia the following circumstances:
- Insolvency of, and other administrative proceedings against, a sub-custodian;
- Legal or political changes in the country where financial instruments are held in sub custody;
- Actions of authorities imposing restrictions on securities markets;
- Risks involved through the use of settlement systems; and
- Any other circumstances which may prevent the AIF from using or disposing of its assets that are kept in custody by a depositary or a sub custodian.

In order to harmonise throughout the Union the obligation to return the assets, AFG is of the opinion that depositaries should be explicitly required to return the cash or the assets they hold in custody in any case except in case of complying with the three cumulative criteria of the "force majeure", without any reference to local legislation: otherwise, the whole provision might be void in its practical effects and far from being applied in a harmonised manner – which would create a high lack of safety, knowing that AIFs can be passported. Indeed, the current Level 1 definition already indirectly includes two out of the three criteria of the "force majeure": we just ask to clarify at Level 2 that the criterion of unpredictability should be introduced as well.

Issue 17

1. CESR is requested to advise the Commission on conditions and circumstances for events to be considered as:
- external,
- going beyond reasonable control, and
- having consequences which would have been unavoidable despite all reasonable efforts to the contrary.

2. If possible, CESR is requested to advise the Commission on a non-exhaustive list of events where the loss of assets can be considered to be a result of an external event beyond its

reasonable control, the consequences of which would have been unavoidable despite all reasonable efforts to the contrary. CESR is encouraged to consider the appropriate form (e.g. guidelines) of such a list.

The AIFMD does not use the notion "force majeure" which was precisely defined by French courts: consequently, the AIFMD allows – through the wording of "beyond reasonable control" and the lack of unpredictability criterion - for a wider exemption of responsibility for depositaries.

Furthermore, we believe that it would be very difficult to draw a list of events where the loss of assets can be considered to be a result of an external event beyond its reasonable control, the consequences of which would have been unavoidable despite all reasonable efforts to the contrary - as these events are unforeseeable by nature.

We therefore ask for keeping the criteria as provided indirectly by AIFM, and just adding the criterion of unpredictability.

However, as a complementary measure, the general principle of restitution should be recalled, in case of assets (including the cash) which are held in custody by the depositary.

Issue 18

1. CESR is requested to advise the Commission on the conditions and circumstances under which there is an objective reason for the depositary to contract a discharge pursuant to Article 21(12).

2. In its advice, CESR is encouraged to provide an indicative list of scenarios that are to be considered as being objective reasons for the contractual discharge referred to in Article 21 (12).

AFG believes that the the cases for exemption of liability for the depositary should be reduced to an only strictly necessary minimum (cf. issue 11). More generally, we think that it should be recalled that the depositary should act in the best interest of investors at all times. In particular, the obligations that the depositary has to comply with in case it delegates one or more of its functions, such as obligations of due diligence and of control its sub-custodians, should be reasserted.

However, we are of the opinion that the AIFM Level 2 should not require more details than the UCITS Directive, considering that AIFs are aimed at professional investors through the passport (contrary to the UCITS passport which may allow for the cross-border marketing to retail investors).

Furthermore, there is no concept of "objective reason" in the UCITS directive.

PART III: TRANSPARENCY REQUIREMENTS AND LEVERAGE

Issue 19

1. CESR is requested to provide the Commission with a description of relevant methods by which AIFM increase the exposure of AIF whether through borrowing of cash or securities, or leverage embedded in derivative positions or by any other means, including any financial and/or legal structures involving third parties controlled by the AIF. This description or mapping should distinguish between the various business models and approaches to leverage in the AIFM industry. In its advice, CESR should take into account the guidance provided in recital 14.

2. CESR is requested to advise the Commission on the appropriate method or methods for the calculation of leverage for the purpose of this Directive. The analysis should, inter alia, take into account the appropriateness, accuracy, cost, comparability and practicability of the different methods.

First, let's recall that leverage should be proportionately defined according to the aim of revealing situations presenting real systemic risk.

Leverage can take multiple forms and can origin from various sources (use of derivative instruments, use of borrowing, use of repurchase agreements, use of Prime Broker, etc.), in particular in the case of hedge funds. It is very important to keep flexibility of the definition of Level 1, knowing in any case that AIFs, in particular through the passport, target professional investors only: what is important for professional investors is disclosure, not too strict management techniques which could reveal as contrary to their ultimate benefit.

On the topic of methods to assess some sorts of leverage, AFG would like to refer CESR to its comprehensive guide applying to UCITS (*'CESR's Guidelines on Risk Measurement and the Calculation of Global Exposure and Counterparty Risk for UCITS', July 2010*). At least, we believe that those general principles applying to UCITS (i.e. using VaR and other methods identified by CESR for UCITS funds) should also be applied to AIFs.

More specifically, in the case of private equity funds and real estate funds, AFG wishes to recall that the leverage at the level of target companies should not be taken into account in the calculation of the leverage of the AIF (cf. recital 14 of the Directive).

Similarly in case of securities issued by companies, the leverage inside those companies should not be taken into account.

Issue 20

1. CESR is requested to advise the Commission on the content and format of the annual report. In its advice, CESR should consider whether all or any of the information referred to in Article 23 should be included in the annual report and the need for appropriate explanatory notes.

As mentioned previously, we generally believe that the requirements in the AIFMD should be as far as possible aligned on those of the UCITS IV directive and that annual reports for AIFs should have a similar content and format to annual reports for UCITS.

Some AFG members are of the opinion that the annual report should include if relevant and in agreement with the auditors, information on the writedowns on remaining assets in the portfolio that may be justified (beyond a mere statement on potential side pockets or gates), as well as the percentage assets in the portfolio that are illiquid, written down or side pocketed.

But once again, the needs of investors for disclosure are different when they invest in hedge funds, real estate funds or private equity funds for instance, and such differences should be taken into account.

2. CESR is requested to advise the Commission on the content and the format of a balancesheet or a statement of assets and liabilities. In its advice, CESR should specify in particular:

- the appropriate presentation, elements and level of detail of the AIF's assets;
- the appropriate presentation, elements and level of detail of the AIF's liabilities;
- the appropriate presentation, the elements and level of detail of net assets (shareholders' or unitholders' equity); and
- the statement of cash inflows to and outflows from the AIF.

The elements and level of details for the assets, liabilities, net assets (shareholders' equity) and cash inflows and outflows that should show in the AIF annual report should include all significant assets and liabilities as separate line items. Total net assets should be disclosed with the breakdown of the net asset value per share (for a unitised fund). Significant line items for an AIF usually include investments (long and short shown separate), receivables/payables, cash, unrealized on derivative contracts, and any other line items deemed significant. It is important to disclose assets and liabilities gross so that the user can calculate the balance sheet leverage. Cash inflows and outflows should be disclosed by type (operating, investing, financing) to provide transparency to the user as to where the fund's cash surplus or deficit comes from.

3. CESR is requested to advise the Commission on the content and format of an income and expenditure account for the financial year. In its advice, CESR should specify in particular the elements and the level of detail of AIF's income and expenditure accounts.

All significant income and expenditure accounts should be reported as separate line items in such a way that the AIF discloses the total net investment income or loss. Significant line items for an AIF usually include interest/dividends, management and performance fees, and professional fees. In addition, realised gains and losses for the year and unrealized gains and losses at the annual report date should be included as separate disclosures.

4. CESR is requested to advise the Commission on the content and format of the report on the activities of the financial year. In its advice, CESR should consider specifying inter alia:

- statement explaining how the fund has invested its assets during the relevant period in accordance with its published investment policy;

An annual report should include a disclosure (usually in the footnotes) explaining the type of investments that the fund is allowed to make during the year in accordance with its investment policy, and the purpose and risks associated with each investment type.

- overview of the AIF's portfolio and, where appropriate, the AIF's major investments;

A schedule of investments should be included in the financial statements which summarises the types of investments held, at fair value. Any significant investments (usually over 5-10%) should be disclosed as a separate line item, at fair value.

- financial results; and

Financial results should be disclosed in the financial statement to provide investors with objective data regarding the results of the AIF's operations and significant ratios as a measure to compare them with the results of other AIFs. In general, the financial results should include share information, total return, and expense ratios.

5. CESR is requested to advise the Commission on how material changes in the information listed in Article 23 during the financial year covered by the report should be best presented in the annual report.

6. CESR is requested to advise the Commission on the content and the format of the remuneration disclosure required under points (e) and (f) of Article 22(2) including the details on the form of remuneration.

Given that staff salaries are not paid by the AIF, a breakdown in the annual report of the AIF between fixed and variable remuneration paid by the AIFM to its staff does not seem relevant. However, management fee and performance fees that are paid to the AIFM could be disclosed in the annual report.

Issue 21

Regarding issues 20 & 21, AFG thinks legitimate to bear in mind the obligations contained in the UCITS Directive, when drafting the obligations in the AIFMD.

However, investors in AIFs are mainly professionals that might not require as much detail as investors in UCITS (mainly retail investors). Consequently, the requirements applying to AIFs should be tailored to the needs of professional investors and not be as burdensome as those applying to UCITS.

In addition, we believe that the risk profile of the AIF should be provided only according to the strategies followed by the manager.

1. With respect to the disclosure obligations in Article 23(4), CESR is requested to advise the Commission on:
- the appropriate frequency of such disclosures;
- the criteria for assessing the liquidity of assets and procedure for calculating the percentage referred to in Article 23(4)(a) and the format of such disclosures; the information and the essential elements to be included in the description of the arrangements referred in points a) and b) of Article 23(4) including the use of gates, suspensions and side pockets; the essential information, and the format thereof, of the risk factors, including relevant risk measures and metrics used to assess the sensitivity of the AIF portfolio to movements in interest rates, credit

spreads, equity markets, etc, counterparty risks the extent of rehypothecation and information on indebtedness of entities controlled by the AIF to be disclosed by the AIFM to enable appropriate description of the current risk profile of the AIF; and
- the information and the essential elements to be disclosed by the AIFM to enable appropriate description of the risk management systems employed by the AIFM to manage these risks including results of recent stress tests.

Such disclosures should be at least annual.

2. With respect to the disclosure obligations in Article 23(5), CESR is requested to advise the Commission on:
- the appropriate frequency of such disclosures;
- the essential information, and the format thereof, to ensure an appropriate description of changes to the maximum level of leverage which the AIFM may employ on behalf of the AIF as well as any right of re-use of collateral or any guarantee granted under the leveraging arrangement; and the leverage measures or ratios, and the format thereof, to be used by the AIFM when disclosing the total amount of leverage employed by the AIF during the reporting period and at the end of the reporting period including those specified according to Article 4.

Issue 22

1. CESR is requested to advise the Commission for the purposes of paragraph 4 on the criteria to be used to determine under which conditions leverage is to be considered as being 'employed on a substantial basis'.

2. CESR is requested to advise the Commission on the content of the obligations to report and provide information referred to in paragraphs 1 through 5. In its advice, CESR should consider developing a comprehensive template to be used by AIFM for reporting to competent authorities the information required under Article 24. In developing such a template, CESR should take into account the reporting template issued by IOSCO on 25 February 2010 for reporting from hedge funds and templates used by national competent authorities.

3. CESR should address inter alia the following elements:
- Assets under management
- Performance and investor information
- Market and product exposure (long and short positions)
- Regional focus
- Turnover and number of transactions, indication of markets in which trading can represent a significant proportion of overall volume, trading and clearing mechanisms
- Leverage and risk
- Asset and liability information
- Counterparty risk

The template should be sufficiently flexible to accommodate the different types, sizes and investment strategies of AIFM, without compromising the objective of effective supervision.

4. CESR is requested to advise the Commission on:

a. the appropriate frequency of such reporting as a function of the potential risks posed by specific types of AIFM; the modalities and forms for data transmission; and whether the same

conditions should apply to the additional information requirements referred to in Article 24(5).

The concept of leverage has no significance in the absolute. It is meaningful only in relation to the liquidity of the assets on which leverage is applied. A leverage of 10/15x in the context of a futures portfolio is not worrisome given the high liquidity of the futures markets. On the contrary, a leverage of 2x for a portfolio of distressed debt is probably quite risky.

Issue 23

1. CESR is requested to advise the Commission on the principles specifying the circumstances in which competent authorities shall exercise the powers granted pursuant to Article 25(3), taking into account different strategies of AIF, different market conditions in which AIF operate and possible pro-cyclical effects following from exercising the provisions. Such principles should guide competent authorities in identifying situations and circumstances in which competent authorities shall exercise the powers referred to in paragraph 3.

AFG would like to recall that competent authorities may impose limits to the leverage used by an AIFM in exceptional circumstances only, which implies an important systemic risk and that in any case such limitations should only apply on a series of objective criteria such as size of market participants, their strategies and their special situation.

It should be noted that counterparties already centralise some information on leverage operations. For instance, prime brokers might be able to contribute to the effort of the competent authorities in collecting and consolidating such data.

Therefore, the best way for regulators to monitor the leverage is to monitor it at the level of "leverage providers", i.e. prime brokers and banks.

In addition, it is important that if regulators decide to impose limits to the leverage in exceptional circumstances, they have to think about the possible immediate consequences for AIF investors: setting limits suddenly should not lead the AIFM to be obliged to reduce positions and liquidate immediately the portfolio. The AIFM should be allowed to reduce the positions *in a reasonable delay, following the principle of acting in the best interests of investors.*

2. In its advice, CESR should consider inter alia to what extent the following aspects might endanger the stability and integrity of the financial system:

- leverage used in different strategies and the size of an AIF's "footprints";
- the concentration of risks in particular markets and risks of spill-over effects; liquidity issues in particular markets; counterparty risks to credit institutions or other systemically relevant institutions; the scale of any asset/liability mismatch; and
- the evolution of prices of assets with respect to their fundamentals.

3. CESR is also requested to advise on the appropriate timing of potential measures referred to in Article 25(3).

*
**

If you need any further information, please do not hesitate to contact myself at +33 1 44 94 94 29 (p.bollon@afg.asso.fr), our Head of International Affairs Division, Stéphane Janin, at +33 1 44 94 94 04 (s.janin@afg.asso.fr) or our Deputy Head of International Affairs Division, Carine Delfrayssi, at + 33 1 44 94 96 58 (c.delfrayssi@afg.asso.fr).

Sincerely Yours,

(Signed)

Pierre Bollon