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AFG response to ESMA consultation
on possible implementing measures of the Alternative Investment Fund Managers Directive

The Association Française de la Gestion financière (AFG)[1] is grateful for the opportunity to respond to ESMA's consultation on possible implementing measures of the Alternative Investment Fund Managers Directive (the AIFMD or the Directive).

General comments

AFG appreciates the approach adopted to ensure that the implementing measures of the AIFMD are **as far as possible in line with existing regulations** such as the UCITS Directive or the MiFID. Many AIFMs also manage UCITS funds or provide MiFID services and it would be very difficult for them to apply inconsistent sets of rules. However, this should of course not prevent where appropriate any differentiation between UCITS and AIFs due to the partly different nature of these two types of funds.

[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 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).

AFG generally supports the implementation of the principle of **proportionality** throughout all level 2 measures, in particular with regards to risk and liquidity management. Indeed, we should bear in mind that **the large majority of AIFs throughout Europe are "UCITS like" funds** that would be subject to too burdensome and costly requirements if the rules were applied in an indiscriminate manner to all AIFs whatever their type or size. For instance in France, nationally regulated "general purpose" funds represent an AUM of EUR 560 Billion (bearing in mind that French investment funds in the scope of the AIFMD total AUM is EUR 712 billion). The same proportion is true throughout Europe. It should in particular be ensured that such principle of proportionality is applied regarding the general operating conditions (risk management) and transparency.

Proportionality should also obviously apply **depending on the size of the AIFM**. Based on the French experience, small-sized, dynamic boutiques are crucial to the making of a competitive environment with larger managers, both at national and cross-border levels. Such level of competition throughout Europe must be maintained to the benefit of investors.

We find the information provided in the **explanatory text** throughout the consultation paper detailed and very helpful. On the other hand, the text proposed in the boxes might lack clarity in some instances. It would therefore be useful to include some of the explanations or definitions contained in the explanatory text in the boxes themselves. This is for example the case for provisions which should be applicable to specific funds only.

AFG would like to request a general clarification: are **AIFs with only one investor** caught by the directive or not? There is a risk of regulatory dumping if this is not applied in the same way throughout the EU: for example, to our knowledge, Luxembourg intends to put them out of the scope of the directive, while Germany and France will put them in, based on different interpretations of the Directive. **Clarification on this point must be urgently done at EU level.**

Our main concerns relate to the following key issues:

- For the calculation of the leverage of funds of hedge funds, we believe that the **leverage** that exists at the level of the underlying hedge funds should not be taken into account, in the same way that the leverage of target companies it not taken into account in the calculation fo the leverage of Private Equity Funds. Indeed, it would be very difficult in practice to aggregate the leverage of each underlying hedge funds (cf. box 2 p.5).

- Additional capital and insurance requirements should be aligned with **current practices** - e.g. potential liability risks to be covered should not include risks in relation to **fraud** – and should be capped (cf. box 6 p.6).

- The proposed measures on inducements should only apply to **direct marketing** by the AIFM (cf. box 18 p.11).

- AIFMs should only be required to check in the **documentation** of the securitisation product that the originator sponsor or original lender pledges to fulfil this retention requirement throughout the life of the product (box 35 p.15).

- Delegations of portfolio management should **only be allowed to entities authorised for collective portfolio management**, as otherwise it would offer an easy way to circumvent the requirements of the Directive (box 67 p.18).

- On the topic of depositaries, the Madoff case hit funds located in several Member States as their national depositary legislation was not clear enough to guarantee the restitution of the funds' assets. We therefore urge ESMA to ensure through the AIFMD L2 measures that protection of funds' assets is guaranteed at the same level throughout Europe for the future – especially as AIFs can be passported from one Member State to another. Our requests are based on this context and aim at ensuring fund investor protection, which is in our view the core role of ESMA Members. In particular, we believe that all financial instruments that are held in custody within the depositary's network and "registered" in an account open in the name of the custodian should be considered as **kept in custody**, as the only one which can claim these assets is the depositary itself (box 78 p.22)

- In addition, assets should be segregated in three parts at the level of the depositary or sub-custodian: apart from the own depositary's (or own sub-custodian's) assets, **client assets should be split in two parts**, between an account open for funds' assets and another account for the rest of the clients' assets in order to ensure the right protection of fund investors in case of depositary bankruptcy and to enable an easy and prompt transfer of the fund assets to another depositary thanks to an easy identification of fund assets in the bankrupted depositary – as already successfully tested in real cases in the past (cf. box 89 p.27).

- The methods to be used to measure the exposure of an AIF should be in line with the methods applicable to **UCITS** (i.e. **commitment or VaR, at the choice of the AIFM**). The gross method of calculation is highly misleading and is not relevant (cf. box 93 p.30).

- Reporting to competent authorities should be made on an **annual** basis (cf. box 109 p.32).

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Detailed comments

Please find below AFG detailed comments (ESMA's proposals are shown in italics).

Article 3 exemptions

Box 1 - Calculation of the total value of assets under management

3 – We support the exclusion of cross-holdings in the calculation of the value of total assets under management (AUM) as this will avoid double-counting the same assets.

4 – "AIFMs should implement and apply procedures to monitor the value of total assets under management"

We feel that there might be some inconsistency between the requirement to calculate the total value of AUM and the obligation to monitor it. It would be useful to specify that such monitoring does not involve a "full and proper" valuation of the assets but an estimate.

Where the value of the assets is not calculated on a frequent basis, AIFMs should be allowed to use estimations of the value of the assets in the portfolio. Indeed, it would be too burdensome and costly to require them to produce "full and proper" calculations (involving for example the obligation to resort to external valuers for real estate funds) on a more frequent basis.

5.a – "Where the total value of assets under management exceeds the threshold the AIFM should notify the competent authority without delay stating whether the situation is considered to be of a temporary nature."

We think that the requirement "without delay", which means immediately, is not realistic in practice. We would therefore suggest re-wording as follows:

"the AIFM should notify the competent authority without undue delay"

In addition, we believe that the delay granted to notify the competent authority should be of one month where the net asset values (NAVs) of all the AIFs considered are calculated on a monthly basis and longer if the NAVs of the AIFs considered are calculated on a less frequent basis: as far as possible, we must consider the AUMs calculated for NAV purposes, and not a *permanent* calculation of the AUMs. It would be a practical case of proportionality to be applied for this Directive.

5.b – "The situation should not be considered to be of a temporary nature if it is likely to continue for a period in excess of three months."

We believe that the temporary nature of the situation should be assessed over a period longer than 3 months - depending on the frequency of the NAV calculation, i.e. a period of at least 6 months as some NAVs are calculated on a monthly basis or sometimes at an even lower frequency. It would be a practical case of proportionality to be applied for this Directive.

As explained above, ESMA should make clearer in its Boxes that "monitoring" does not imply "calculating", as some NAVs are calculated at a low frequency and not on an ongoing basis.

Q2 - Do you think there is merit in ESMA specifying a single date, for example 31 December 2011 for the calculation of the threshold?

No. In our view, the date for the calculation of the threshold should remain at the discretion of AIFMs. The preferred date will probably be determined by the date of the annual, external audit report of the fund, taking into account the fact that some AIFMs may manage funds located in different jurisdictions with potentially different accounting periods. Allowing AIFMs to choose the calculation threshold themselves will allow them to pick the date that involves as few intermediary NAV calculations as possible, considering the "closing" dates of the AIF they manage.

Q3: Do you consider that using the annual net asset value calculation is an appropriate measure for all types of AIF, for example private equity or real estate? If you disagree with this proposal please specify an alternative approach.

AFG does not consider that using the annual net asset value calculation is an appropriate measure for all types of AIF.

The AIFMD will cover a very broad universe of AIFs and a differentiated solution needs to be found to achieve a satisfactory result. The differences between AIFs covered, for example differences due to assets classes into which the funds are invested and differences due to the open-ended or closed-ended nature of the AIFs, should be reflected in the solution found. Taking these differences into account, different methods of calculating assets under management should be implemented. It would therefore be useful to define different types of AIFs, for each of which it would then be possible to set a specific calculation method.

Box 2 - Calculation of Leverage

We believe that the approach to be followed should be proportionate and reasonable. In particular, we agree the chosen method might have to be adjusted for some types of AIFs. For instance, it would be useful to specify here – in addition to the rules in box 95 - that for private equity and venture capital funds the leverage that exists at the level of the portfolio company and for funds of hedge funds the leverage that exists at the level of the underlying hedge funds shall not be taken into account in the calculation of the leverage.

However, we call for consistent calculation methodologies for each fund type and each asset category, in order to avoid any differences in implementation among Member States for the same fund type or asset category.

Box 3 - Information to be provided as part of registration

2 – "(…) The description of the investment strategy should at least include the following information: (…)"

We think that it is key to harmonise at EU Level what can be required from national regulators, both to ensure an equal treatment of AIFMs wherever they are domiciled and also because otherwise pan-European AIFMs might face different requirements from one country to another and it would not be easy to manage. We suggest therefore the deletion of "at least":

"The description of the investment strategy should ~~at least~~ include the following information"

4 – "The updated information referred to in this Article should be provided on a quarterly basis"

We believe that the provision of updated information on a quarterly basis is too frequent and would be too burdensome for both authorities and AIFMs. We therefore suggest that such provision should be made annually.

5 – "Competent authorities may require the AIFM to provide the information set out in paragraph 1

and 2 on a more frequent basis."

As above, we are concerned that a non exhaustive list of information and the discretion allowed to competent authorities regarding the frequency of such information may lead to a lack of harmonisation among the Member States and in turn create difficulties for AIFMs belonging to pan-European groups. We believe that an exhaustive list and a frequency set at EU level would be more appropriate – or it should be decided at EU level by ESMA (in exceptional circumstances for instance).

Box 4 - Opt-in Procedures

AFG approves the approach proposed by ESMA regarding opt-in procedures. Indeed, we believe that there is no reason not to apply the same rules to AIFMs that choose to opt-in.

We further agree that AIFMs should only be required to submit information not previously provided for registration purposes and, in case there has been a material change to that information, to update it.

General operating conditions

Box 6 - Potential risks arising from professional negligence to be covered by additional own funds or professional indemnity insurance

We support the approach set at level 1 to allow AIFMs to choose between additional own funds and professional indemnity insurance in order to cover the potential risks arising from professional negligence.

We ask that ESMA includes in Box 6 the definitions presented on page 29 of its consultation in order to clearly make them binding, taking into account the following amendment to the definition of "relevant person".

Indeed, the definition proposed page 29 is too wide and would imply a heavy cost in terms of covering the responsibility relating to persons "involved in the provision of services to the AIFM under a delegation arrangement to third parties for the purpose of the provisions of collective portfolio management by the AIFM". There is no reason why asset managers should be required to support the risks attached to their delegates. By contrast, depositaries are not required to cover to such an extent the risks attached to their sub-custodians for instance. In particular, we believe that "relevant person" should exclude distributors as AIFMs should not be liable for marketing activities not undertaken by them.

1 – "The AIFM must be able to cover the potential liabilities arising from professional negligence."

We believe that the above requirement is too wide and would generate significant costs for AIFMs. Moreover, there is no reason why the latter should be subject to such an obligation, while other market participants are not. Indeed, no other industry is subject to such unlimited obligation, not even nuclear energy providers, car makers, plane makers, chemical industry or pharmaceutical producers for instance.

We therefore suggest rewording this provision as follows:

"In order to cover the potential liability risks arising from professional negligence, AIFMs are required to have additional own funds or to subscribe to a professional indemnity insurance".

This would be exactly in line with the wording of AIFMD L1 (article 9 para.7 letter a: "have additional own funds which are appropriate to cover potential liability risks arising from professional negligence").

Box 6 para. 2a – AFG does not agree that potential liability risks to be covered include risks in relation to fraud. Risks in relation to fraud are not mentioned in Article 9 AIFMD. Indemnity insurances normally only cover negligent behaviour and not fraud, which are acts of criminal offence committed deliberately and not negligently. Entitlements of third persons that refer to fraud are not part of an indemnity insurance. The scope of potential liabilities of an AIFM should therefore be restricted to risks arising from negligence, not risks arising from deliberate misbehaviour of employees of the AIFM or third parties. We therefore suggest removing para. 2a.

6.2.b.i – "Those risks particularly include negligent loss of documents evidencing title of assets of the AIF"

We suggest rewording as follows:

"Those risks particularly include negligent loss of documents evidencing title of assets of the AIF provided they are not supported by the depositary or any other entity, for instance a "notaire" in the case of real estate funds."

2.c – "Risks in relation to business disruption, system failures, process management: Losses arising from negligent failure resulting in or not adequate prohibiting the disruption of business or system failures, from failed transaction processing or process management"

We believe that this obligation would be too costly for AIFMs and needs to be re-worded. Indeed, AIFMs cannot be held liable indefinitely. Moreover, current practice in the insurance industry is that losses resulting from mechanical failures are excluded from insurance coverage, unless the loss is a result of an intervention or manipulation of the AIFM. We are if the opinion that AIFMs should have an obligation of means rather than an obligation of result.

Explanatory text point 9 p.34 – "If an AIFM negligently failed to carry out sufficient due diligence on an investment which turned out to be a fraud (e.g. a pyramid scheme such as the Madoff funds), the AIFM's liability to third parties must also be covered."

We believe that AIFMs cannot be held liable to third parties in case of investments that turn out to be frauds provided they have fulfilled their obligation to perform sufficient due diligence regarding these investments.

As explained above, fraud is usually not covered by insurance policies. For instance, under French law one cannot be responsible for fraud made by a third party over which one has no control. Risks in relation to fraud are not relevant here, especially when investors in the funds are

professionals. **There need to be a consistency between UCITS and AIF regimes in order to ensure that a management company managing both types of funds does not have to subscribe two different insurance policies for each segment of its business.**

Q9: The risk to be covered according to paragraph 2 (b)(iv) of Box 6 (the improper valuation) would also include valuation performed by an appointed external valuer. Do you consider this as feasible and practicable?

Yes. We support ESMA's proposal that the AIFM should be liable for valuations performed by an appointed external valuer, according to the general principle that the AIFM is responsible for the valuation. However, due allowance should be made for adequate capital backing or insurance coverage provided by the external valuer, so that there is no double layer of safeguards for the same liability risks.

Box 7 - Qualitative Requirements

We support the implementation of the principle of proportionality regarding the obligation to perform operational risk management activities independently.

Box 8 - Quantitative Requirements

1 - **We prefer option 1** as it is more straightforward and less volatile than option 2, partly based on the "relevant income" which might be difficult to interpret and determine in practice and might lead to an unlevel application by national authorities.

In our opinion, the requirements in terms of own funds may prove too burdensome in particular for "UCITS like" funds. We therefore urge ESMA to apply proportionality in developing these measures.

4 – We believe that the competent authority of the home Member State of the AIFM should be allowed to increase the additional own funds requirements in exceptional circumstances only and provided it can justify such an increase to ESMA, so that it could approve it. In addition, we would suggest ESMA to set a maximum amount of additional own funds that national authorities may request. This would avoid any regulatory excesses.

Conversely, we believe that the possibility for the competent authority of the home Member State of the AIFM to reduce the additional own funds requirements a their own discretion is not appropriate. Indeed, **such national derogations might lead to regulatory dumping, as these reductions would only depend on the relevant AIFM and authority. We therefore think that such reductions should be allowed under the supervision of ESMA, in order to avoid any regulatory excesses and ensure a better articulation of the action of the different national authorities, therefore a better harmonisation of the implementation of European regulations.**

Box 9 - Professional Indemnity Insurance

The calculation of the coverage of the insurance as proposed in points 2 & 3 seems extremely complicated. Moreover, it depends on the claims received by the AIFM - for instance, it is not clear what happens if the AIFM does not receive any.

1.c – "There are no exclusions regarding liability risks listed in Box 1"

We understand that this provision refers to Box 6 – not Box 1. However, the list presented in box 6 is not exhaustive, and it is impossible for an insurance to cover each and every potential risk arising from professional negligence! No insurance policy can cover all risks with no exception. Indeed insurance companies need to define the risks to be covered and the maximum compensation they can offer for each defined risk, hence the exclusions and limits set out in insurance policies.

It would therefore be appropriate to describe the risks to be covered in an exhaustive manner, with minima and maxima.

1.d – "*Any defined excess is covered by own funds"*

We think that this wording is unclear. We suggest clarification as follows:

"any defined excess i.e. any amount falling under the threshold triggering the application of the insurance ("franchise" in French)"

1.e – "The insurance is taken out from an insurance undertaking authorized to transact professional indemnity insurance, which is subject to prudential regulation and ongoing supervision and has sufficient financial strength with regard to the claims paying ability"

We suggest that the sentence should stop after the words "ongoing supervision". Where an insurance company is licensed and under prudential supervision it should not be the task/responsibility of the AIFM to assess the ability of the insurance company to pay claims. As the insurance company is regulated there should be the assumption that it is able to pay claims and in practice the AIFM will not be able to verify if this is the case.

3.c – Box 8 as proposed by ESMA provides for potential increases or decreases of the percentage used in the calculation of the amount of additional own fund required. Consequently, we believe that the coverage of the insurance for all claims in aggregate per year cannot be based on this amount.

4 – We suggest re-wording as follows:

"**The AIFM should review the policy and its compliance with the requirements ~~at least~~ once a year [as a higher frequency would be disproportionately burdensome] and in the event of any material change [for the same reason] which affects compliance of the policy with the requirements."**

Indeed, these amendments would ensure a better harmonisation at EU level. It would moreover make the frequency of the review by the AIFM more stable and more reasonable to implement.

Box 10 - Duty to act in the best interests of the AIF or the investors of the AIF and the integrity of the market

1 – "AIFM should apply appropriate policies and procedures for preventing malpractices that might reasonably be expected to affect the stability and integrity of the market."

In our opinion, there is no reason why AIFMs should be subject to such obligation while other market players are not. This would distort competition and prevent the establishment of a level playing field. Such market integrity topics must be tackled in horizontal market legislation (e.g. the Market Abuse Directive).

2. "AIFM should act in such a way as to prevent undue costs being charged to the AIF and its investors."

It seems difficult to assess the "undue" nature of costs. We would therefore urge ESMA to provide for a clear and precise definition of what "undue costs" are.

Box 11 - Due Diligence requirements

It would be useful to clarify in box 11 itself that the requirements set in paragraphs 4 and 5 only apply to AIF invested in specific types of assets i.e. assets which have a long duration, which are less liquid such as private equity and real estate funds (cf. Explanatory text - points 11, 12, 14 & 15 p.44).

It should be noted that most AIFMs already have due diligence in place as it is inherent to their business (due diligence is natural and necessary). Generally, they already document their investment decisions.

It should however be kept in mind that due diligence is charged to the fund; therefore additional requirements will necessarily imply additional costs for the AIF.

In addition, there is another reference to the "integrity of the market", which is new as compared to the UCITS Directive and should be repealed as this notion should be applied to all market participants through an horizontal market legislation (see our comment on Box 10 above).

4.a – the AIFM should "set out and update a business plan consistent with the duration of the AIF and market conditions"
4.b – "seek and select possible transactions consistent with the plan referred to under point (a)"

The requirement to "**update** a business plan consistent with **market conditions***"* does not seem applicable to all types of funds, especially in situations where market conditions are volatile. A differentiation should be made among funds (real estate funds, private equity funds, funds of funds, nationally regulated retail funds).

As a consequence of the above, it seems difficult to implement the requirement set out in paragraph 4.b.

5 - AIFM should retain records on the activities performed pursuant to paragraph 4 for a period of at least five years.

We believe that keeping such records for a set period of five years would be more appropriate and ensure a full harmonisation.

Explanatory text - point 15 p.44

"AIFM should also maintain evidence of significant investment opportunities"

We think that such requirement is too intrusive and suggest re-wording it as follows:

"**AIFM should also maintain evidence of significant investments ~~opportunities~~. Indeed, portfolio management is the exclusive responsibility of AIFMs. Moreover, it would be burdensome and costly to keep record of investment opportunities**."

Box 14 – Execution of decisions to deal on behalf of the managed AIF

We welcome the clarification in Explanatory Text 21 that Box 14 paragraph 1 shall apply to all AIF while paragraphs 2-5 only apply to those types of AIF which acquire or sell financial instruments or other assets for which best execution is relevant. We strongly urge ESMA to include this clarification directly into the text of Box 14 to avoid diverging or contradictory future interpretations.

Box 15 – Placing orders to deal on behalf of AIFs with other entities for execution

We welcome the clarification in Explanatory Text 24 that Box 15 paragraph 1 shall apply to all AIF while paragraphs 2-5 only apply to those types of AIF which acquire or sell financial instruments or other assets for which best execution is relevant. We strongly urge ESMA to include this clarification directly into the text of Box 15 to avoid diverging or contradictory future interpretations.

Box 16 - Handling of orders – general principles

In our opinion the requirements proposed in box 16 are too prescriptive and too detailed. We welcome the clarification in Explanatory Text 25 that Box 16 does not apply where the investment in assets is made after extensive negotiations on the terms of the agreement. Again, we strongly urge ESMA to include this clarification directly into the text of Box 16 to avoid diverging or contradictory future interpretations.

Box 17 - Aggregation and allocation of trading order

3 & 4 - We believe that it is questionable whether AIFMs should be at all allowed to aggregate transactions for own account and transactions for AIFs, UCITS or clients' account. Indeed, there should be Chinese Walls in place preventing that kind of practice.

Box 18 - Inducements

First and foremost, we would like to clarify that the provisions in box 18 only apply in relation to the distribution of funds (AIFs or UCITS) it manages, and not in relation to discretionary mandates (which are covered by MIFID). Indeed, although the latter are not in the scope of the Directive, they might be part of the activities of an AIFM.

AFG understands that the proposed measures should apply to direct marketing by the AIFM only. We strongly disagree that they should also apply to "indirect marketing". Indeed, we do not believe that distribution via intermediaries constitutes part of the fund management services as specified in Annex I to the AIFMD. External intermediaries who are not tied agents act in their own capacity and under their own responsibility. Their relationship to the AIFM is based upon distribution agreements which set out the duties and obligations of each party and ensure compliance with their respective legal requirements. Third-party distribution cannot be deemed part of the collective portfolio management activities and the term "marketing" in Para. 2 (b) of Annex I of the AIFMD[2] can only refer to direct distribution by the AIFM, by its tied agents, and possibly to marketing on behalf of the AIFM by a placing agent for a closed-end investment company IPO.

We do not see why distribution fees should generate conflicts of interest; fees and commissions received by intermediaries as remuneration for the distribution service are a necessary cost and are already regulated, subject to the conditions of Art. 26 (1) (b) of the MiFID Level 2 Directive and to disclosure to investors at the point of sale. In any case, we strongly believe that the AIF or the AIFM on behalf the AIF must be able to pay retrocessions to distributors or clients. In this respect, the KIID introduced for UCITS is in our opinion a good information tool for clients that would be useful also for AIFs' investors.

We suggest ESMA to develop rules that are in line with the UCITS directive, i.e. disclosure should be made to the AIF, not to the AIF's investors. This would ensure consistency with existing regulations and a better harmonisation.

Finally, we would welcome clarification regarding the treatment of ongoing fees which are not distribution fees. Indeed, we doubt it would be useful to inform investors on all the different components of these ongoing fees, as investors are interested in the global cost of their investment. Therefore, we believe that a further split of the fees would not be relevant. In any case, the AIFMD regulates the marketing to professional investors which may ask for further information on a tailored basis. Consequently, the Directive should leave these disclosure rules to contractual provisions.

Box 19 - Fair treatment by an AIFM

In our view, option 1 allows for a limited and restrictive requirement and therefore provides for more legal certainty than option 2 which, being too flexible, would not allow harmonisation at EU level. We therefore favour option 1.

Boxes 20 to 30 - Measures on conflicts of interest and on risk management

We strongly support the implementation of the principle of proportionality in the proposed measures on conflicts of interest and on risk management.

Regarding measures on conflicts of interest (boxes 20 to 24), we support the alignment with MiFID and UCITS Directive, as far as possible, as this approach will allow consistency among the rules

[2] Marketing is defined in Article 4 (1) (x) of the Level 1 text as '… *a direct or indirect offering or placement at the initiative of the AIFM or on behalf of the AIFM of units or shares of an AIF it manages to or with investors domiciled or with a registered office in the Union*'.

applying to AIFs and UCITS and consequently not generate any additional burden for management companies managing both types of funds.

Box 24 – Strategies for the exercise of voting rights

In France, management companies are already required to have a voting policy in place with regards to investments in listed companies.

Regarding private equity funds, it seems natural that AIFM will exercise their voting rights relating to the companies they invest in.

Regarding real estate funds, it would not be appropriate to require AIFM to have a voting policy in place. Indeed, voting rights are only attached to a minor part of the assets in the portfolios of such funds.

Box 26 - Risk Management Policy

1 – "AIFM shall establish, implement and maintain an adequate and documented risk management policy which identifies all the relevant risks to which the AIF they manage are or might be exposed to."

We think that this requirement is too broad and suggest re-wording it as follows:

"AIFM shall establish, implement and maintain an adequate and documented risk management policy which identifies all the material relevant risks to which the AIF they manage are or might be exposed to."

Box 28 - Measurement and Management of Risk

We suggest further alignment with the UCITS directive and re-word as follows:

3.b - "Conduct, where appropriate, periodic back tests"
3.c - "Conduct, where appropriate, periodic stress tests and scenario analyses"

Box 29 - Risk Limits

We believe that the list of risks proposed in box 29 is not applicable to all types of funds. For example, it is not possible to integrate financial market risks in stress tests for real estate funds. Therefore, proportionality is needed depending on the type of fund or management.

We therefore suggest re-wording paragraph 2 as follows:

"The qualitative and quantitative risk limits for each AIF, shall, at least, cover the following risks, **where relevant**"

Box 31 - Liquidity Management Definitions

We would like ESMA to amend the definition of "special arrangement" so as to include for instance suspensions of an AIF, which by nature are special arrangements according to us.

Some AFG members foresee the use of gates, in the prospectus of the AIFs they manage and use them in the normal course of the liquidity management. In our members' view, these tools, provided that they are disclosed in the prospectus, should not be considered as special arrangements. For better clarity, our members would like to make a clear distinction between two types of gates: those that are disclosed in the prospectus and are part of the normal process of liquidity management and those that are implemented in exceptional situations and in this respect are seen as special arrangements.

Box 32 - Liquidity Management Policies and Procedures

e – "AIFMs shall implement appropriate policies and procedures to ensure that the redemption policies of the AIF are disclosed to investors, in sufficient detail and with sufficient prominence"

We believe that such a requirement would be impossible to fulfil. The description of policies and procedures referred to can only be disclosed to investors in general terms – not in such a detailed manner.

f – In order to allow for appropriate flexibility, we suggest re-wording this requirement as follows:

"AIFMs shall identify the types of circumstances where tools and arrangements may be used in both normal and exceptional circumstances"

h – "AIFMs shall document their liquidity management policies and procedures, review these on at least an annual basis and update these for any changes or new arrangements"

In order to limit this requirement, we suggest re-wording it as follows:

"update these for any material changes or new arrangements."

Explanatory text - point 15 p.80

"AIFMs are required to consider not only their obligations to investors, but also their obligations to counterparties, creditors and other third parties".

We believe that such an obligation would definitely be too wide if it also covered third parties. Moreover, we are not aware of any other market participant subject to such a requirement. We therefore suggest re-wording as follows:

"AIFMs are required to consider their obligations to investors".

Explanatory text - point 18 p.80

"AIFMs should implement appropriate policies and procedures to ensure that the redemption terms applicable to a particular AIF are disclosed in sufficient detail and with sufficient prominence to investors"

As explained above, we think that such a requirement would be impossible to fulfil. The description of policies and procedures referred to can only be disclosed to investors in general terms – not in such a detailed manner.

Explanatory text - point 25 p.82

We agree to disclose in the prospectus the principles underpinning the policies and procedures but not the practical details of the implementation of those principles, which may very significantly.

Q20: It has been suggested that special arrangements such as gates and side pockets should be considered only in exceptional circumstances where the liquidity management process has failed. Do you agree with this hypothesis or do you believe that these may form part of normal liquidity management in relation to some AIFs?

We believe that the use of special arrangements such as gates and side pockets should not be restricted to exceptional circumstances, as we feel that the definition of "exceptional circumstances" is not precise enough. Therefore, we urge ESMA to provide for a clear and precise definition of "exceptional circumstances".

As explained previously (please refer to our comment on box 31), gates disclosed in the AIF's prospectus may be used in the normal course of the liquidity management. Our members believe that these tools should not be considered as special arrangements and would like to make a clear distinction between two different types of gates: those that are disclosed in the prospectus and are part of the normal process of liquidity management and those that are seen as special arrangements to be used in exceptional circumstances only.

Boxes 35 to 37 - Measures on investment in securitisation positions

In our opinion AIFMs can not be required to verify that the originator, sponsor or original lender retains a net economic interest retained of at least 5%. AIFMs can only check in the documentation of the securitisation product that the originator sponsor or original lender pledges to fulfil this retention requirement throughout the life of the product. Only regulators are in a position to control that the originator sponsor or original lender complies with such obligation.

Besides, requiring AIFMs to verify that the originator, sponsor or original lender retains a net economic interest retained of at least 5% would go beyond the requirements in CRD IV and would impose an obligation solely on AIFMs – and not on other market players – thus preventing the establishment of a level playing field.

Box 39 - Requirements for monitoring procedures

We support the implementation of the principle of proportionality regarding the establishment of formal monitoring procedures. Indeed, such requirement needs to be adapted to the size of the relevant AIFM and/or its activity.

Boxes 40 & 41

We would like here again to reassert the need for proportionality in the implementation of the proposed requirements.

Box 42 - Introduction of new underlying exposures to existing securitisations

We urge ESMA to ensure that the requirements set in the AIMFD are consistent as far as possible with the provisions contained in CRD.

In addition, we suggest the introduction of a transitional period for investments held by AIF at the entry into force of the new rules, as it would not be in the interest of AIFs' investors to immediately dispose of holdings that would prove non compliant with the new AIFMD rules.

Box 43 – Investments by UCITS

We generally support the alignment of the rules in the UCITS directive with that of the AIFMD, provided it is done in a proportionate manner.

Box 44 - General requirements on procedures and organisation

We generally support the implementation of the principle of proportionality and the alignment, as far as possible, with MiFID and the UCITS directive.

Box 46 - Electronic data processing

2. "AIFM should ensure a high level of security during the electronic data processing as well as integrity and confidentiality of the recorded information, as appropriate".

The requirement to ensure the integrity of the information does not apply to depositaries for instance so we cannot see any reason why it should apply to AIFMs.

Besides, it might be useful to specify that the confidentiality of the information should only apply to confidential information.

Box 48 - Control by senior management and supervisory function

g - "The AIFM should ensure that its senior management […] approves and reviews on a periodic basis the risk management policy and arrangements, processes and techniques for implementing that policy including the risk limit system for each managed AIF"

We believe that this requirement would prove too burdensome if it had to be performed exclusively for instance by the CEO. We therefore are of the opinion that the definition of senior management should not be strictly understood. In other words, the obligation to approve and review the risk management policy and arrangements, processes and techniques could be performed by any person deemed senior enough to do so.

Box 49 – Permanent compliance function

3 - We appreciate that it is not required to establish an independent compliance function if this would be disproportionate for the AIFM. This clarification is however only reflected in the Explanatory Text Para. 15. We would suggest that it should be included into the text of the Box to avoid future diverging interpretation by competent authorities.

Box 51 - Personal transactions

4. "'personal transaction' means a trade in a financial instrument or other asset effected by or on behalf of a relevant person"

We believe that it should be clarified that the assets are **those relevant to the concerned AIF**.

4.b.ii "any person with whom he has a family relationship, or with whom he has close links"

We are concerned that this requirement might prove too wide and burdensome.

Box 52 - Recording of portfolio transactions

AFG would like to make sure that the proposed requirements are suitable for real estate funds.

Q23: Should a requirement for complaints handling be included for situations where an individual portfolio manager invests in an AIF on behalf of a retail client?

No. We believe that the rules contained in MiFID are sufficient.

Boxes 53 & 54 – Recording of subscription and redemption orders & Recordkeeping requirements

We understand that these requirements are based on the existing UCITS framework. However, it should be clarified that they are only applicable to the direct distribution of the AIF (i.e. to direct orders) and that different solutions regarding the recording of orders must be permitted in case of indirect distribution.

Box 56 - Models used to value assets

We agree that senior management should be able to understand and validate the valuation model and methodology. This is fundamental and consistent with the general principle that the responsibility of the valuation belongs to the AIFM (principle set at Level 1).

Box 57 - Consistent application of the valuation methodologies

It would not make sense to apply the exact same policies, procedures and valuation methodologies to all AIFs having the same AIFM. Indeed, they have to be tailored to the type of AIF (e.g. real estate fund, private equity fund…) and to the type of asset in the portfolio of the AIF (e.g. geographical zone).

We therefore suggest re-wording as follows:

The policies and procedures shall be applied across all AIFs having the same AIFM, taking into account investment strategies, the type of assets, time zones and local valuation rules and, if applicable, the existence of different external valuers.

Box 59 - Review of individual values

This requirement may prove burdensome, especially for small-sized AIFMs. We believe that these rules should be proportionate to the size of the AIFM.

Box 63 – Delegation

We welcome the proposals by ESMA in Box 63. The Explanatory Text Para. 9 and 11 are considered very important for the understanding of the proposals in Box 63, in particular the term of "critical and important functions". We therefore urge ESMA to include the clarifications of Explanatory Text Para. 9 and 11 directly into Box 63.

Box 65 - Objective Reasons

AFG supports option 2. Indeed, option 1 implies a subjective criteria ("a more efficient conduct") and is redundant (principle already set at in the Directive at Level 1).

Option 2 is in line with the criteria for best selection in the MiFID. However, we would like to clarify that the criteria proposed in option 2 are not cumulative and re-word as follows:

"Objective reasons for delegating tasks include but are not limited to one or several of the following criteria"

Box 66 – Sufficient resources and experience and sufficiently good repute of the delegate

We feel that these proposed requirements are too detailed and burdensome, and go far beyond what is required under the UCITS directive. We therefore ask for a closer alignment between the approach taken under the AIFMD and the one followed for the UCITS framework.

Box 67 - Types of institution that should be considered to be authorised or registered for asset management and subject to supervision

We think that authorising management companies to delegate to credit institutions would lead to regulatory arbitrage and a stretch of the directive's rules. It could fully void the aim of AIFMD if its requirements can be easily circumvented through the use of a credit institution. **Therefore, we very strongly believe that delegations should be allowed to entities authorised for investment management only.**

It is even more crucial here as we have to bear in mind the fact that the Directive will also apply to entities located in third countries.

Box 69 – General principles for sub-delegation of AIFM functions

AFG supports this possibility of sub-delegation.

Box 71 – Criteria to be taken into account when considering whether a delegation/ sub-delegation would result in a material conflict of interest with the AIFM or the investors of the AIF; and for ensuring that portfolio or risk management tasks haven been functionally and hierarchically separated from any other potentially conflicting tasks within the delegate/ sub-delegate; and that potential conflicts of interest are properly identified, managed, monitored an disclosed to the investors of the AIF

1.b. "the AIFM is aware"

We believe that this wording is too vague and suggest replacing it as by "has been informed" so that an objective criteria can be used in order to assess whether the AIFM knew the information.

Box 73 - Letter-box entity

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.

2. "key areas"

We believe that the relevant areas should be defined as the functions described in Annex I of the level 1 directive (i.e. portfolio management and risk management).

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Depositaries

AFG would like to share the following 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 (in other words, whether the depositary can claim their property);

- In particular, the Madoff case hit funds located in several Member States as their national depositary legislation was not clear enough to guarantee the restitution of the funds' assets. We therefore urge ESMA to ensure through the AIFMD L2 measures that protection of funds' assets is guaranteed at the same level throughout Europe for the future – especially as AIFs can be passported from one Member State to another. Our requests below are based on

this context and aim at ensuring fund investor protection, which is in our view the core role of ESMA Members.

Box 74 – Contract appointing the depositary

AFG members believe that drafting a model agreement appointing the depositary would unfortunately be a near impossible task, as Member States have each their own contract law and AIFs legal structures. We therefore support the drafting of a list of particulars to be included in the written agreement between the AIFM and the AIF's depositary. This approach was rightly followed in UCITS IV Level 2. This list should in particular reassert the core missions that the depositary may not waive and state 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.

We generally agree with the list of particulars shown in box 74.

However, for the avoidance of any doubt, we recommend to amend item 2 in Box 74 so as to read "A description of the type of assets that will fall within the scope of the depositary's **safekeeping and oversight** functions (...)".

We think that the description of the type of assets under item 2 should also include a description of the geographic zones in which the AIF/AIFM plans to invest as this is essential information to allow the depositary to fulfil its obligations.

We would also like to clarify that the obligation set in paragraph 7 only implies that, in the contracts it agrees with third parties, the AIFM sets the obligation for the latter to provide information to itself and to the AIF's depositary.

Additionally, we believe that in paragraph 9 modifications to offering documents are not relevant. We therefore suggest re-wording as follows:

"The procedures to be followed when a modification to the AIF rules, instruments of incorporation ~~or offering documents~~ is being considered, detailing the situations in which the depositary should be informed, or where a prior agreement from the depositary is needed to proceed with the modification"

Finally, we would like to amend paragraphs 7, 10 and 12 to cover only the relevant or necessary information in order to have a more realistic wording:

Para 7 : ~~All~~ **the relevant information it needs**
Para 10: ~~all~~ **necessary information**
Para 12: ~~all~~ **necessary information**

Explanatory text - point 10 p.144

"ESMA has specifically imposed an obligation on the AIFM to ensure the depositary has access to all relevant information it needs including from third parties (e.g., administrators, prime brokers, etc.) to ensure it can fulfil its obligations. »

As explained above, we would like to highlight the fact that the depositary remains responsible for sourcing information from third parties. Of course, the AIFM should facilitate its access to such information, for instance in agreeing with third parties that they must provide information to the depositary; however, it is not responsible for making sure that the depositary actually receives it.

Box 75 – Cash Monitoring – general information requirements

AFG broadly agrees with the general information requirements proposed by ESMA, subject to the following remarks:

- Here again we would like to that only the relevant or necessary information is covered.

  "The AIFM should ensure the depositary is provided, upon commencement of its duties and on an ongoing basis, with ~~all~~ relevant information it needs to comply with its obligations"

- Second bullet point: it ought to be clarified that the obligation to inform the depositary prior to the opening of new cash accounts does not imply that the depositary has any influence in the choice of the counterparties where the accounts are opened. Indeed, this is purely an investment decision for which the AIFM is the only responsible.

- Third bullet point: this requirement to provide "… all information related to cash account …" is drafted in very broad terms and appears to be too extensive, given that the regulatory purpose (as described in paragraph 4 of explanatory text) is only to enable timely access by the depositary to the cash account. In line with the introductory paragraph in Box 75, the wording should therefore be amended to read as follows: "the depositary is provided with the necessary information related to the cash accounts opened at a third party entity, directly from those third parties in order for the depositary to have access to the information regarding the AIF's cash accounts it needs to comply with its obligations and have a clear overview of all the AIF's cash flows".

- Third bullet point: this requirement to provide "… all information related to cash account …" is drafted in very broad terms and appears to be too extensive, given that the regulatory purpose (as described in paragraph 4 of explanatory text) is only to enable timely access by the depositary to the cash account. In line with the introductory paragraph in Box 75, the

wording should therefore be amended to read as follows: "the depositary is provided with the necessary information related to the cash accounts opened at a third party entity, directly from those third parties in order for the depositary to have access to the information regarding the AIF's cash accounts it needs to comply with its obligations and have a clear overview of all the AIF's cash flows".

- Finally, AFG has concerns regarding the last sentence in box 75 which seems to impose an obligation of result on the AIFM.

Box 76 – Proper monitoring of AIF's cash flows

AFG prefers option 2, as option 1 would be too complicated and too costly to implement.

Box 78 – Definition of financial instruments to be held in custody - Article 21(8) (a)

We generally think that the scope of "Financial Instruments to be held in custody" should be kept wide, based on the general notion of the owner of the assets.

All financial instruments that will be held in custody within that network and "registered" in an account open in the name of the custodian (for example a nominee account or on behalf of clients) should be considered as kept in custody, as the only one which can act, claim, suit….etc the property of those assets is the depositary itself.

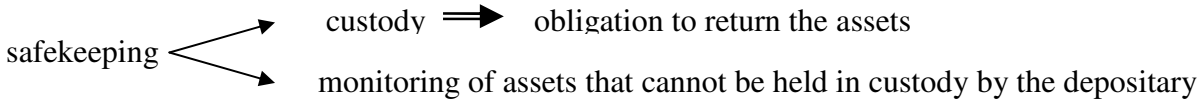
That means that wherever such an account is opened, with a sub-custodian, a CSD, or a registrar, and open in the name of the depositary or its delegate, the assets held/registered in this account fall in the custody side with all obligations attached.

Conversely, for all financial instruments which are registered directly in the name of the AIF, it is the AIF that is empowered to act, claim, suit,….etc and as such will not fall in the custody obligation but in the monitoring one.

We would suggest therefore splitting the financial instruments in the following way:

"Financial Instruments (transferable securities, money market instruments and units of collective investment undertakings – as listed in Annex I, section C of Directive 2004/39/EC3) that are registered/held in an account directly in the name of the AIF, or the AIFM representing the AIF, with a capacity of claiming ownership belonging to the AIF, or the AIFM representing the AIF, would not enter in the definition of Custody.

Financial Instruments (transferable securities, money market instruments and units of collective investment undertakings – as listed in Annex I, section C of Directive 2004/39/EC4) belonging to AIF that are registered/held in an account directly or indirectly in the name of the Depositary are considered as kept in Custody by the depositary".



Of the options proposed by ESMA, AFG prefers option 1 (we however suggest some amendments to the wording of option 1 - please see below). Indeed, the definition of financial instruments held in custody cannot be based on the possibility to transfer them through a specific settlement system. Additionally, AIFMs would be prevented from investing in non EU markets where there are no settlement systems fulfilling the criteria set by ESMA. More generally, the definition of financial instruments to be held in custody should be compatible with local laws.

Consequently, we suggest the below definition of financial instruments to be held in custody:

"Pursuant to Article 21 (8) (a), financial instruments belonging to the AIF should be included in the scope of the depositary's custody function when they meet all the criteria defined below:

1. they are transferable securities, money market instruments or units of collective investment undertakings – as listed in Annex I, section C of Directive 2004/39/EC;

2. they are not posted as collateral in accordance with the provisions set out in Box 79; and

3. they are registered or held in an account directly or indirectly in the name of the depositary as it is the only one that can claim the assets.

Additionally, financial instruments which can be physically delivered to the depositary should be held in custody.

All financial instruments that will be held in custody within the depositary's network and "registered" in an account open in the name of the custodian (e.g. a nominee account or on behalf of clients) should be considered as kept in custody, as the only one which can act, claim, suit….etc the property of those assets is the depositary itself.

Financial instruments that are directly registered with the issuer itself or its agent (e.g. a registrar or a transfer agent) in the name of the AIF should not be held in custody unless they can be physically delivered to the depositary. Further, financial instruments which comply with the definition set out above will remain in custody when the depositary is entitled to re-use them whether that right has been exercised or not. Where the financial instruments have been provided by the AIF or the AIFM acting on behalf of the AIF to a third party under a temporary lending agreement, they will no longer be held in custody by the depositary and fall under the definition of 'other assets' in accordance with Article 21 (8) (b).

~~In the context of Option 1,~~ Where the financial instruments are registered directly with the issuer or its agent making the depositary the only registered owner on behalf of one or more unidentified clients, the financial instruments should be held in custody. However, such financial instruments should not be held in custody if the depositary is clearly identified in the register as acting on behalf of the AIF and thus the AIF is clearly identified as the owner of the financial instruments and is in a position to claim ownership of these assets.

Any financial instrument that does not comply with the above definition should be considered as 'other asset' under the meaning of the AIFMD Article 21 (8) (b) and be subject to record keeping duties."

Box 79 - Treatment of collateral

We prefer option 2.

However, in order to clarify that the instruments posted as collateral may be held in custody by the entity that receives them, we suggest re-wording as follows:

"Financial instruments posted as collateral should not be held in custody by the entity that posted them"

Moreover, the draft advice does not explicitly deal with collateral received by the depositary or any sub-custodian for the benefit of the AIF. We are of the view that any financial instruments received as collateral should be regarded as having been "entrusted to the depositary for safe-keeping" within the meaning of Art. 21(8) AIFMD.

Besides, we strongly believe that the obligation to return the assets should not be restricted to assets that are not pledged. Indeed, the amount of the AIF's assets pledged by the bank may be more than the value of the loan contracted by the AIF.

In any case, 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.

Q34: How easy is it in practice to differentiate the types of collateral defined in the Collateral Directive (title transfer / security transfer)? Is there a need for further clarification of option 2 in Box 79?

We feel that a differentiation of the types of collateral between title transfer and security transfer would make no difference.

Explanatory text - point 35 p.160

"ESMA believes it is sufficient to require the depositary to ensure the financial instruments are subject to due care and protection."

In our opinion the obligation to return the assets should apply to any financial instrument belonging to the AIF that are registered/held in an account directly or indirectly in the name of the depositary. Indeed, the obligation to return the assets should be attached to all assets kept in custody.

Box 80 - Safekeeping duties related to financial instruments that can be held in custody

In Europe, due diligence on CSDs does not make sense as CSDs do not operate in a competitive environment.

Box 81 - Safekeeping duties related to 'other assets' – Ownership verification and record keeping

AFG supports option 1 as is it more realistic (option 2 would be too burdensome and costly). We would however clarify that there might be several relevant third parties and re-word as follows:

1.ii. "the depositary should […] have access to documentary evidence of each transaction from ~~the~~ a relevant third party on a timely basis"

Q36: Could you elaborate on the differences notably in terms of control by the depositary when the assets are registered directly with an issuer or a registrar (i) in the name of the AIF directly, (ii) in the name of the depositary on behalf of the AIF and (iii) in the name of the depositary on behalf of a group of unidentified clients?

We believe that the right to claim the assets should be the criteria used to determine whether the latter are held in custody or not.

Q39: To what extent does / should the depositary look at underlying assets to verify ownership over the assets?

Explanatory text paragraph 5 p.176

We suggest including this provision in a box in order to make it binding.

Box 82 – Oversight duties – general requirements

AFG supports controls by the depositary performed 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 service provider.

We suggest re-wording paragraph 3 as follows:

"The depositary is required to establish a clear and comprehensive escalation procedure to deal with situations where ~~potential~~ irregularities are detected in the course of its oversight duties, the details of which should be made available to the competent authorities upon request."

Box 84 - Clarifications of the depositary's oversight duties

4. Where the depositary considers the calculation of the value of the shares or units of the AIF has not been performed in compliance with applicable law or the AIF rules or the provisions of Article 19, it should notify the AIFM and ensure timely remedial action has been taken in the best interest of the AIF's investors.

AFG believes that the auditor, rather than the depositary, should be in charge with the AIFM to look at this. The depositary verifies the method of calculation, not the calculation itself.

Box 86 - Clarifications of the depositary's oversight duties

We support option 2 as it provides further detail on the depositary's oversight duties. In particular, as AIFMs are not members of settment systems, they need to be informed by the depositary when in case of delays in the settlement of transactions. Furthermore, the depositary should be responsible for chasing compensation/payment ("contrepartie") if required.

Box 87 - Clarifications of the depositary's oversight duties

We would like to specify that these obligations are not exhaustive. We therefore suggest re-wording as follows:

"To fulfil its obligation pursuant to Article 21(9)(e), the depositary should in particular be required to"

1. Ensure the net income calculation is applied in accordance with the AIF rules, instruments of incorporation and applicable national law

AFG believes the auditor should be in charge of this.

3. Check the completeness and accuracy of dividend payments and where relevant of the carried interest

We would like to clarify that the depositary is responsible for checking that the dividend payments and where relevant the carried interest payments have been made according to the applicable rules and that is it not responsible for the actual calculations.

Q40: To what extent do you expect the advice on oversight will impact the depositary's relationship with funds, managers and their service providers? Is there a need for additional clarity in that regard?

AFG believes that the tasks - and responsibilities - of the different actors in the value chain should be clearly identified so that there is no conflict among them.

Q41: Could potential conflicts of interest arise when the depositary is designated to issue shares of the AIF?

In our view, the issuance of shares of an AIF should be done by the AIF itself or its AIFM, and not by the depositary which otherwise would be conflicted by interests as it is also responsible for monitoring the relevant fund or AIFM.

Box 88 – Due diligence requirements

AFG believes that the auditor of the depositary in its due diligence of the depositary should check that the depositary has duly fulfilled its obligations. In other words, 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.

Box 89 – Segregation

We support the requirement to segregate all assets that are held in safekeeping i.e. whether they are held in custody or not.

We believe that the obligation of restitution of cash should be made clear (in addition to financial assets held in custody).

In order to protect fund clients, AFG believes that assets should be segregated in three parts at the level of the depositary or sub-custodian: apart from the own depositary's (or own sub-custodian's) assets, client assets should be split in two parts, between an account open for funds' assets and another account for the rest of the clients' assets.

The reason of this suggested segregation among depositary (or sub-custodian) clients' assets is twofold:

- contrary to direct clients that benefit from an individual compensation scheme, AIFs do not benefit from it and therefore should be protected in another way

- contrary to other clients which can open accounts within several custodians, funds (either AIFs or UCITS) cannot open accounts in several depositaries. We agree with this requirement, but it means that the risk related to the depositary's bankruptcy cannot be split among several depositaries

Therefore, in case of bankruptcy of the depositary or sub-custodian, all assets – including the cash - belonging to AIFs (or funds at large) should be rapidly transferred to another depositary (or sub-custodian) – thus acting in the best interest of AIF clients and complying with AIFM fiduciary duties vis-à-vis its clients, as the continuity of the active management of the AIF will be guaranteed, without having to wait for the court resolution of the depositary (or sub-custodian) bankruptcy.

This segregation among clients' assets in two parts was successfully tested in France in the 1990, with the bankruptcy of the Pallas Stern Bank: all the assets belonging to funds were transferred to other custodians in only a few weeks, and therefore the active management of these funds was preserved - without having to wait for the final settlement of the bankruptcy.

In addition, from a technical perspective, there is no difficulty for custodians to set such segregation among clients' assets between funds' assets and other clients' assets, as today this segregation has gone even further, at individual level in many cases:

- for legal reasons, many countries out of Europe already require today a segregation of assets – including both cash and Financial Instruments - which goes even beyond what we are asking for: while we are only asking for separating clients' assets in two omnibus accounts, i.e. funds' assets on the one hand and other clients' asset on the other hand, many countries – with big fund industries – require a segregation fund by fund throughout the whole chain, from the depositary to the CSD. Such a list of countries includes China, Brazil, Chile, India, Korea, Taiwan for instance. Some of these countries have a significant fund industry. Considering that investment funds' assets in some

non EU countries are identified and returned at individual level, it would be paradoxical if Europe did not require at least a segregation in three parts at the level of depositary and sub-custodians, i.e. depositary's (and sub-custodian's) own assets, client funds' assets and other clients' assets;

- in practice, when a big fund client asks a depositary to benefit from a single account in the whole depositary and sub-custodian chain, it gets it if it is big enough to impose it. It clearly shows that technically segregation, even until at individual level, is possible.

We are not asking for a total segregation of assets (Financial Instruments and cash), i.e. fund by fund. It would be technically possible, but would be very costly for European depositaries. Therefore, we are only - but strongly - asking for segregation at the level of clients' assets in two blocks (including both cash and the rest of assets): omnibus funds' assets and omnibus other clients' assets.

Of course, it would imply that, when entering the relationship with the AIFM, depositaries provide the AIFM with a list of countries in which such segregation can be guaranteed. If the legislation in some countries would not allow for such segregation, then this obligation would not apply – and there should be a discharge of responsibility of the depositaries if the AIFM decides to invest in such countries however.

Explanatory text - point 7 p.178

We doubt that the proposed criteria are strict enough.

Box 90 - Definition of loss

We believe that the "permanent" nature of a situation is very difficult too assess in practice. How long does one have to wait until a situation can be considered as permanent?

We suggest rewording paragraph 1.b and 1.c and the second subparagraph of paragraph 2 as follows:

"the AIF has been ~~permanently~~ deprived of its right of ownership over the financial instruments unless it is for a limited period of time"

"the AIF is ~~permanently~~ unable to directly or indirectly dispose of the financial instruments unless it is for a limited period of time"

"Where an AIF is ~~permanently~~ deprived of its right of ownership in respect of a particular instrument unless it is for a limited period of time"

Second last paragraph of the box – AFG believes that the depositary, not the AIFM, should be required to monitor the proceedings and determine whether the assets are effectively lost. Indeed, the AIFM does not have any relationship with the sub-custodian. The AIFM is the client of the depositary and in turn of the sub custodian.

"In case of insolvency of a sub-custodian, financial instruments should be considered 'lost' as soon as one of the conditions set out in §1 is met with certainty and at the latest, at the end of

the insolvency proceedings. To that end, the ~~AIFM~~ custodian on behalf of the AIFM should monitor closely the proceedings to determine whether all or part of the financial instruments entrusted to the sub-custodian are effectively lost."

Explanatory text - point 8 p.180 & point 16 p.181

Please see comment above.

Box 91 – Definition of "external event beyond the depositary's reasonable control, the consequences of which were unavoidable despite all reasonable efforts to the contrary"

We support the approach that an event linked to the sub custodian should be considered as internal.

2. "The event which led to the loss was beyond its reasonable control, i.e. it could not have prevented its occurrence by reasonable efforts"

This requirement should also apply to any sub-custodian.

The above described conditions will apply to the delegate when the depositary has contractually transferred its liability to a sub-custodian.

AFG believes that this should be deleted as it is confusing. The contract will define the obligations of the sub-custodian anyway.

Explanatory text - point 22 p.183

We believe that fraud cannot be considered as an external event beyond reasonable control.

Box 92 – Objective reasons for the depositary to contract a discharge

AFG supports the first paragraph of option 1.

"The depositary will be deemed to have an objective reason to contractually discharge itself of its liability in accordance with the requirements set forth in Article 21 (13) if it can demonstrate that it had no other option but to delegate its custody duties to a third party (e.g. as a result of legal constraints)."

Indeed, option 2 would depend on the weight of the AIFM in its relationship with the depositary. This would not be in favour of small sized AIFMs but in favour of large sized AIFMs.

Q49. Do you see any difficulty with the suggestion to consider as an external event the fact that local legislation may not recognize the effects of the segregation requirements imposed by the AIFMD?

No, we do not see any difficulty with that suggestion. More generally, AFG believes that a proper segregation will allow a clear view of the assets. Indeed, a proper segregation will allow demonstrating that the assets still belong to the AIF when these assets are clearly identified.

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Possible implementing measures on methods for calculating the leverage of an AIF and the methods for calculating the exposure of an AIF

Box 93 -General Provisions on Calculating the Exposure of an AIF

4. "To comply with its obligations with respect to Article 25(3) of Directive 2011/61/EU, AIFM may in addition to calculating exposure under the Gross Method and Commitment Method, and upon notification to the competent authorities of its home Member State, calculate the exposure of an AIF under its management in accordance with the Advanced Method set out in Box 97".

We believe that the number of methods to be used to calculate the exposure of the AIF should be proportionate to the size and type of the AIF, i.e. to the type of assets in its portfolio and the purpose of the leverage. For instance, the use of a single methodology would reduce the burden on asset management companies that manage both UCITS and "UCITS like" funds. In other words, **the choice of the calculation method should be up to the manager, which will be in a position to pick for each AIF it manages the calculation method most suitable to the profile of the AIF.**

The methods to be used should be in line with the methods applicable to UCITS (i.e. commitment or VaR, at the choice of the AIFM). Indeed, most AIFs are "UCITS like funds". For instance in France, nationally regulated "general purpose" funds represent an AUM of EUR 560 Billion (French investment funds in the scope of the AIFMD total AUM = EUR 712 billion). The same proportion is true throughout Europe. However, if an AIF uses borrowing (which is not allowed for UCITS), it should of course be taken into account in the calculation.

In any case, **we strongly believe that the gross method of calculation is highly misleading and is not relevant** with regards to ESMA's objectives. In any case, **it makes no sense to aggregate different notional values.**

Box 95 - Gross Method of Calculating the Exposure of the AIF

We believe that **gross leverage is a highly misleading proxy for the risks ESMA aims at measuring**. This measure is indeed too simple and is not relevant to ESMA's objectives, in particular because it includes the leverage attached to derivatives and exchange rates.

Paragraph 3 – In the same way the exposure that exists at the level of a portfolio company is not intended to be included in the calculation of the exposure of a private equity or venture capital fund, we would like to introduce an exemption for funds of funds i.e. the exposure at the level of the underlying hedge funds should not be taken into account in the calculation of the exposure of the fund of funds.

Indeed, in the case of funds of funds, it is impossible to aggregate the leverage of underlying funds, as the leverage is calculated differently for each underlying fund: it is as a consequence too complicated to consolidate it (in particular, it would be difficult in practice to make real time calculations: underlying funds might change their leverage often, making the calculations quickly outdated). Besides, this is the approach applied to UCITS funds of funds.

Box 96 -Commitment Method of Calculating the Exposure of an AIF

The commitment method is preferable to the gross method, as it allows excluding the leverage attached to derivatives and exchange rates.

The wording of paragraphs 1 and 2 and paragraphs 1 and 4 is not consistent. We suggest rewording this box in line with CESR's Guidelines on Risk Measurement and the Calculation of Global Exposure and Counterparty Risk for UCITS (dated July 2010).

We suggest deleting paragraph 1b and replacing it by paragraph 2.

Box 99 – Exposures involving third party legal structures

First and foremost, we would like to highlight that it would not make sense to include the counterparty risk in the exposure calculation, as there are different ways to limit that risk (margin calls, diversification of risks etc).

AFG is in favour of option 3, as it allows a more precise calculation of the exposure.

Q60: Notwithstanding the wording of recital 78 of the Directive, do you consider that leverage at the level of a third party financial or legal structure controlled by the AIF should always be included in the calculation of the leverage of the AIF?

No**.**

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Transparency requirements

Box 106 - Content and Format of Remuneration Disclosure

We generally support the proposed approach. We strongly believe that the requirements in terms of remuneration disclosure should be proportionate so as not to generate disproportionate additional costs.

We support a presentation of remuneration at an aggregated level, i.e. at the level of the AIFM. Indeed, it would be neither relevant nor possible to present remuneration at the level of the AIF. Moreover, in order to ensure confidentiality of the data, remuneration has to be disclosed in an aggregated manner, in particular for small sized AIFMs. Furthermore, AIFMs do not necessarily have information available to allow all the different elements of remuneration to be allocated to individual AIFs.

In our opinion, the proportionality principle is a key point to define the general framework of the remuneration policies for AIFM. It implies that each management company has a great flexibility to set up all the components of its remuneration policy, in accordance with the general principles established for the sector. In this respect, we would like to highlight one of the strong differences

between the asset management industry and other financial activities: by nature, a management company does not take any risks affecting its own balance sheet or its assets.

Regarding the content of the information to be disclosed, we consider that the remuneration disclosures should be subject to similar exemptions as are available to firms under Directive 2006/48/EC, which effectively allows information which is immaterial, confidential or proprietary to not be disclosed.

Box 107 – Periodic Disclosure to Investors

We support option 1 as this more easily accommodates a variety of different types of funds (option 2 is too prescriptive and not necessarily relevant for all AIFs).

Explanatory text - point 13 p.232

We believe that such borrowing arrangements should not be defined as "special arrangements" as they are not bespoke or separate arrangements (cf. definition p.77 of the consultation paper).

Box 108 - Regular Disclosure to Investors

1.d - "details of changes in any service providers"

We believe that these details should be disclosed in relation to depositaries and auditors only, as it would be very difficult in practice to do so in relation to all service providers.

Box 109 - Format and Content of Reporting to Competent Authorities

We believe that a disclosure on a quarterly basis would be too burdensome and above all not relevant. Indeed, a large part of AIFs are "UCITS like" funds for which a quarterly reporting would generate significant initial and ongoing costs. Moreover, detailed quarterly reporting would certainly exceed what is necessary to monitor systemic risk.

This would certainly be an additional burden especially for small-sized AIFMs and would therefore contradict the general principle of proportionality. For example, one of our members estimates that the cost of implementing a quarterly reporting would be of one person over the first year (in particular in order to set in place the required processes and procedures) and half a person the following years.

We think that an annual basis would be more appropriate. Additionally, we urge ESMA to apply the principle of proportionality based on the size of the AIFM and the types of AIFs it manages.

Q69: Do you agree with the proposed frequency of disclosure? If not, please provide alternative suggestions.

No. Please see our comments on box 109.

Box 110 - Use of Leverage on a 'Substantial Basis'

We believe that the reference to **the gross calculation method should be removed and the choice of the calculation method left up to the AIFM (please refer to our previous comments of the methods of calculating the exposure of an AIF).**

In our opinion, the criteria set out in order to assess whether leverage is employed on a substantial basis are highly judgmental and subjective and could be interpreted very differently by competent authorities and AIFMs. We therefore wonder whether the proposed definition will lead to a consistent approach to leverage. This is particularly the case as the list is noted as being "non exhaustive".

Moreover, we believe that to perform the assessment required under the points d) to f), the AIFM would have to consider consolidated information on the markets and information about investees/counterparties that are not under its control or accessible to it but rather only to the regulators. These points create an obligation that is difficult to discharge effectively.

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Annex V – Pro-forma for AIFM reporting to competent authorities

Only section 1 of annex V is applicable to all AIFMs; Sections 2 and 3 only apply to n AIF 'which is of a material size'. Much will therefore depend on which AIFs fall in this category. We think it critical that these sections need only be completed for AIFs which are of such a size as to pose systemic risk. There is no point in competent authorities being overloaded with information – they will not be able to assess and utilize this volume of information effectively.

We understand that the proposed template is based on the IOSCO template. However, we would like to share some comments on section 3 (risk profile of the AIF). Indeed, some items in the proposed report are not relevant for "UCITS like" funds. For example, the ownership by investor group (cf. p.431) would be difficult to assess, even for funds aiming at institutional investors. It may be difficult, and in some instances impossible, to give such a level of detail where AIFs are distributed through a distribution network.

Market risk profile
AIFMs should be allowed to use different models of VaR, and as many models as AIFs. Indeed, the relevance of the model depends for instance on the type of funds and / or type of assets. Besides, it should be specified that the VaR model is not relevant for some types of funds.

Counterparty risk profile
Some of our members deem the proposed reporting particularly burdensome as it implies treatments that are not commonly used (in particular, number 15 – top 5 trading counterparty for each AIF and 16 – top 3 central CCPs).

Liquidity risk profile
Some of our members are of the opinion that the liquidity table is relevant for portfolios containing listed equities or futures only (e.g. it is not relevant for bonds, OTC instruments or even listed options). This only option is therefore to assess liquidity through estimates based on bid offer. It is fluctuating and impossible to standardise. It all depends on the valuation method and AUM.

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

Sincerely Yours,

(Signed)

Pierre Bollon