European Securities and Markets Authority

Reply form for the Draft regulatory technical standards under the ELTIF Regulation

31 July 2015

Responding to this paper

The European Securities and Markets Authority (ESMA) invites responses to the specific questions listed in the ESMA Consultation Paper on Draft regulatory technical standards under the ELTIF Regulation, published on the ESMA website.

Instructions

Please note that, in order to facilitate the analysis of the large number of responses expected, you are requested to use this file to send your response to ESMA so as to allow us to process it properly. Therefore, ESMA will only be able to consider responses which follow the instructions described below:

- use this form and send your responses in Word format (pdf documents will not be considered except for annexes);
- do not remove the tags of type <ESMA_ QUESTION_ELTIF_RTS_1> - i.e. the response to one question has to be framed by the 2 tags corresponding to the question; and
- if you do not have a response to a question, do not delete it and leave the text “TYPE YOUR TEXT HERE” between the tags.

Responses are most helpful:

- if they respond to the question stated;
- contain a clear rationale, including on any related costs and benefits; and
- describe any alternatives that ESMA should consider

Naming protocol

In order to facilitate the handling of stakeholders responses please save your document using the following format:

ESMA_ELTIF_RTS_NAMEOFCOMPANY_NAMEOFDOCUMENT.

E.g. if the respondent were ESMA, the name of the reply form would be:

ESMA_ELTIF_RTS_ESMA_REPLYFORM or

ESMA_ELTIF_RTS_ESMA_ANNEX1

To help you navigate this document more easily, bookmarks are available in “Navigation Pane” for Word 2010 and in “Document Map” for Word 2007.

Deadline

Responses must reach us by **14 October 2015.**

All contributions should be submitted online at www.esma.europa.eu under the heading ‘Your input/Consultations’.

Publication of responses

All contributions received will be published following the end of the consultation period, unless otherwise requested. **Please clearly indicate by ticking the appropriate checkbox in the website submission form if you do not wish your contribution to be publicly disclosed. A standard confidentiality statement in an email message will not be treated as a request for non-disclosure.** Note also that a confidential response may be requested from us in accordance with ESMA's rules on access to documents. We may consult you if we receive such a request. Any decision we make is reviewable by ESMA's Board of Appeal and the European Ombudsman.

Data protection

Information on data protection can be found at www.esma.europa.eu under the headings 'Legal notice' and 'Data protection'.

General information about respondent

Name of the company / organisation	Association Française de la Gestion financière (AFG)
Confidential[1]	☐
Activity	Investment Services
Are you representing an association?	☒
Country/Region	France

Introduction

Please make your introductory comments below, if any:

<ESMA_COMMENT_ELTIF_RTS_1>
The Association Française de la Gestion financière ("**AFG**") thanks ESMA for the draft Regulatory Technical Standards ("**RTS**") and detailed explanations and costs-benefits analysis and welcomes the opportunity to reply to the questions related to the RTS. We would like to stress out the following points.

We consider that the ELTIF Regulation will support the development of closed-end funds in our jurisdiction and we would recommend that ESMA gives more guidelines and illustrations to better define the Life-Cycle as mentioned in article 18(3) of Regulation (UE) 2015/760. It is also important that all stakeholders keep in mind that a maturity gap can exist between the maturity of the underlying asset and the end of life of the ELTIF fund. We clearly understand that articles 3 and 4 of the RTS are written with the purpose of defining the divestment process for eligible investments that the ELTIF is still invested in one year before the end of life of the ELTIF.

Turning to the rules related to the definition of eligible hedging derivatives, the AFG welcomes the fact that ESMA wants to rely on a definition of eligible hedging derivatives that would be as broad as possible, and would recommend that ESMA goes one step further by providing a simple definition of eligible hedging derivatives. That definition should rather be based on eligible hedging derivatives' economic impact instead of relying on the IFRS definition, which might be too restrictive, lead to potential technical and accounting constraints and is not necessarily used by all asset managers in all jurisdictions across Europe.

The ELTIF Regulation will facilitate the development of a new asset class and enlarge the scope of the asset management business; the ability for asset managers to extend loans under the conditions defined in the ELTIF regulation is one of the new measures that will ensure the success of the Capital Market Union and the European Commission plan to boost investment across Europe. AFG also takes the opportunity of this ESMA consultation on the RTS to question the restriction on eligible real estate assets (commercial property or housing) limitation to "long-term investment projects that contribute to the objectives of smart, sustainable and inclusive growth". AFG would welcome additional guidelines from ESMA in order to widen the scope of eligible real estate projects when, for instance, an ELTIF fund finances a real estate project development to replace an older building by an energy efficient one.
<ESMA_COMMENT_ELTIF_RTS_1>

[1] The field will used for consistency checks. If its value is different from the value indicated during submission on the website form, the latest one will be taken into account.

Q1 Do you agree that the abovementioned pieces of legislation and associated regulatory framework are relevant for the purpose of the present advice on Article 9(3) of the ELTIFs Regulation? Which other pieces of legislation and associated regulatory framework do you identify for that purpose?

<ESMA_QUESTION_ELTIF_RTS_1>
The IFRS rules, CESR's guidelines and OTC clearing regulations provide sufficient points of comparisons. We do not think that another piece of regulatory framework should be studied in detail in order to make further analysis on the regulatory framework for the use of financial derivatives for the RTS at the level 1. We have also studied the broader definition of derivative instruments provided by EIOPA on the Public Consultation on Basis Risk.

We would stress the fact that IFRS should not be directly used in the RTS and would recommend that the RTS defines eligible hedge instruments without specifically referring to IFRS rules.
Thus we would strongly recommend that the paragraph (a) of article 1 of the RTS is removed, and would suggest the following wording for article 1:

"A financial derivative instrument shall be considered as serving the purpose of hedging the risks inherent to other investments of the ELTIF as referred to in Article 9(2)(d) of Regulation (EU) 2015/760 when, by itself or in combination with other financial derivative instruments, directly or through closely correlated instruments, it does not result in material basis risk and meets both of the following criteria:

a) the exposure covered by the financial derivative instrument is sufficiently similar in nature to the risk exposure it seeks to reduce;
b) the changes in value of the exposure covered by financial derivative instruments closely mirror the changes in value of the risk exposure it seek to reduce and an economic relationship exists between the hedged item and the financial derivative instruments."

<ESMA_QUESTION_ELTIF_RTS_1>

Q2 Do you think that the main risks that are necessary to be covered at the level of the ELTIF are currency, inflation and interest rate risks? If no, which types of risk would the manager of an ELTIF potentially have to cover in your view?

<ESMA_QUESTION_ELTIF_RTS_2>
We agree that the main risks that have to be covered at the level of the ELTIF are principally currency, inflation and interest rate risks but would argue that an ELTIF fund manager may want to have the ability to hedge other types of risk when for example the fund holds a real asset or a financial instrument (including financial instruments authorised in the bucket of 30% of other assets) that carries a certain type of additional risk that the fund manager does not want to have. A case could be made for hedging against the default risk of the contractor that guarantees the completion of an infrastructure during the construction phase. As another example, an ELTIF fund manager may wish to hedge against a temporary exposure to a change in price of agricultural products because he holds land for future infrastructure investments.
<ESMA_QUESTION_ELTIF_RTS_2>

Q3 Do you think that the approach to hedging should not limit ex ante the scope of risks that ought to be covered by the manager of the ELTIF?

<ESMA_QUESTION_ELTIF_RTS_3>
Further to our reply to question 2 we would clearly argue that it is very difficult to limit ex ante the scope of risk that can be covered by the manager of an ELTIF fund. Besides, ELTIF funds are managed in the long term and we could reasonably argue that it is hard to predict today the type of liquid derivative instruments that will be used in the future for hedging purposes.
<ESMA_QUESTION_ELTIF_RTS_3>

Q4 On the contrary, do you think that the approach to hedging should be tailored to the specific case of ELTIFs, and their possible eligible investments? Do you think that in this case the risks that might have to be covered by the manager of the ELTIF should be limited to the types of risk that were mentioned in question 2?

<ESMA_QUESTION_ELTIF_RTS_4>
We consider that it is not possible to define and limit the type of hedging instruments that can be used by the ELTIF manager.
<ESMA_QUESTION_ELTIF_RTS_4>

Q5 Do you identify any consequences in terms of costs or scope of the eligible investments of the ELTIF if the risks that might be covered at the level of the ELTIF are limited to those that were mentioned in the impact assessment of the Commission?

<ESMA_QUESTION_ELTIF_RTS_5>
Same reply as for question 2: we do think that the ELTIF manager should be able to cover a larger range of risks than the risks mentioned in the impact assessment (i.e. currency, interest rates and inflation).
<ESMA_QUESTION_ELTIF_RTS_5>

Q6 Do you agree with the proposed approach? Should you disagree, please provide reasons and propose an alternative approach and justify it.

<ESMA_QUESTION_ELTIF_RTS_6>
Among the two proposals (the average life-cycle or the longest life-cycle), we are in favor of retaining the longest life-cycle of all the individual assets that the ELTIF is investing in to define the end of life of the ELTIF as specified in article 18(3) of the Regulation (UE) 2015/760.

Nevertheless, the definition of the illiquidity profile and economic life-cycle, as mentioned in the paragraph 3 of article 18 of the Regulation (UE) 2015/760, is not clear and would need to be detailed with examples, in particular in the recital preceding the RTS. For some eligible assets, it seems to be difficult to estimate the illiquidity profile and economic life-cycle ("**Life-Cycle**"). For example, on real estate assets, there is no maturity and a recommended holding period which could be different from one property to another (depending on the rent roll, the refurbishment program, etc.). Some infrastructure projects are very long-term in nature up to 50 years; nevertheless the underlying asset or financial instrument linked to the infrastructure could be sold on the market before the maturity of the infrastructure or the procurement contract. Another good example of the gap between the Life-Cycle and the real maturity of the underlying asset can be given in capital investment where an equity investment is perpetual but is sold in most cases by the private equity fund to the market or to other investors every 5 to 7 years.

On this basis we recommend that article 2 of the RTS include a reference to normal market practice for assets where the illiquidity profile and economic life cycle is significantly different from the underlying maturity of those assets in order to make sure that the "sufficient length rule" set in paragraph (3) of article 18 of the Regulation (UE) 2015/760 enables an ELTIF fund to have a shorter end of life than the maturity of the underlying asset. In addition, further indications or examples illustrating the case for a fund that invests in assets that have very long maturities or are perpetual in nature but have a liquidity cycle with a defined length of time to be designated as an ELTIF could be written in point (4) of the recital preceding the RTS in order to provide pan-European guidelines to be used by regulators when granting the authorization to designate a fund as an ELTIF.
<ESMA_QUESTION_ELTIF_RTS_6>

Q7 Do you agree with the risks identified and the related proposed criteria? Would you suggest the introduction of any additional/alternative risks/criteria? Please provide details and explain your position.

<ESMA_QUESTION_ELTIF_RTS_7>
We agree with the very detailed list of risks, but would recommend that points 3(e) (risk associated with legislative changes) and 3(f) (political risk) are taken out from Article 3 because they are already implicitly included in point (g) (overall conditions…).
<ESMA_QUESTION_ELTIF_RTS_7>

Q8 Do you agree with the proposed valuation criteria? Would you suggest the introduction of any additional/alternative criteria? Please provide details and explain your position.

<ESMA_QUESTION_ELTIF_RTS_8>
We clearly agree with article 4 of the RTS in particular relying on AIFMD valuation rules.
<ESMA_QUESTION_ELTIF_RTS_8>

Q9 Do you agree that the abovementioned pieces of legislation and regulatory material are relevant for the purpose of the RTS on Article 25(3) of the ELTIFs Regulation? Which other pieces of legislation and regulatory material do you consider relevant for that purpose?

<ESMA_QUESTION_ELTIF_RTS_9>
Yes. We understand that the regulatory technical standards (RTS) referred to in points (a) and (c) of Article 8(5) of Regulation (EU) No 1286/20146 (the PRIIPs Regulation) mentioned in Article 22(4) of the ELTIFs Regulation are to be delivered to the Commission by 31 March 2016, which makes it impossible for ESMA to take them into account while drafting the present RTS under Article 25(3) of the ELTIFs Regulation. This situation should evolve.
We are also of the view that it is appropriate to use the existing work on cost disclosure under the UCITS Directive as a basis, meaning CESR's guidelines on the methodology for calculation of the ongoing charges figure in the key investor information document (n°10-674, n°10-1321 and n°583/2010).
<ESMA_QUESTION_ELTIF_RTS_9>

Q10 Do you agree with the abovementioned assumptions?

<ESMA_QUESTION_ELTIF_RTS_10>
Yes. We agree that elements of paragraphs (2) to (9) of the CESR's guidelines on the methodology for calculation of the ongoing charges figure in the key investor information document (KIID) (the CESR's guidelines) should be taken into account.

We agree adding the general principles governing the internal procedures of the ELTIF fund manager in relation to defining and calculating the costs of the ELTIF fund, if it is based on the equivalent rules for UCITS set out in paragraph (1) of the CESR's guidelines. We also agree that elements of paragraphs (10) to (18) of the CESR's guidelines should be taken into account.

We agree that some of the costs covered by Article 25(2) are entry costs borne by the investor, and that a specific methodology should therefore be set up if it were decided to include them in the overall ratio. But we would argue strongly that this approach lacks consistency and feel that set-up costs paid once at the start should be clearly separated from other types of costs that are ongoing charges. In the unlikely case of inclusion in an overall cost ratio, it would be necessary to make an assumption on the duration of the holding period of the investment, and the amortization methodology for these up-front costs.
<ESMA_QUESTION_ELTIF_RTS_10>

Q11 Do you agree that the types of costs mentioned in the present paragraph are annual costs that could be expressed as a percentage of the capital?

<ESMA_QUESTION_ELTIF_RTS_11>
Yes. We agree that management and other costs (including administrative, regulatory, depositary, custodian, professional service, appraisal and audit costs) are annual costs ('ongoing charges'), that could be for example expressed as percentage of the capital, and where an assumption on the duration of the investment

is not necessary to calculate the corresponding costs to be included in the numerator of the overall ratio. Conversely, up-front charges should preferably be identified as such and not included in ‘ongoing charges’ (see Question 14 below).

However, we are of the opinion that performance fees should not be seen as 'costs' but rather as a sharing of the increase of the fund NAV that benefits to the investors in a first place, and should not be seen as a 'cost' *per se*. They also correspond to a part of the performance generated by the work of the manager and we see no interest in expressing this amount as a percentage of the total commitments of the fund.
Furthermore, in most cases, the performance fees will only be paid to the fund manager at the end of life of the ELTIF fund, or when an investment hurdle is met.
<ESMA_QUESTION_ELTIF_RTS_11>

Q12 Do you think that performance related fees would be relevant costs to be taken into account in the case of ELTIFs?

<ESMA_QUESTION_ELTIF_RTS_12>
As mentioned above, performance fees are not a cost of the ELTIF *per se* as they are a portion of the wealth generated by the fund manager and are generally based on the growth of the NAV.
<ESMA_QUESTION_ELTIF_RTS_12>

Q13 How would you include performance related fees in the overall ratio referred to in paragraph 2 of Article 25?

<ESMA_QUESTION_ELTIF_RTS_13>
We do not think that performance related fees should be included into the calculation, because it would be irrelevant. Like in UCITS Funds, performance-related fee payable to the management company or any investment adviser shall not form part of the amount to be disclosed as ongoing charges.

We agree that investors should receive information about all costs and charges they will bear directly or indirectly when investing in an ELTIF. However, performance fees and generally speaking, all volatile fees (e.g. transaction costs) can only be estimated ex-ante on a best effort basis with reasonable assumptions. We are also concerned about the consistency and convergence of the Directives / Regulations applicable to Asset Managers in Europe. In this perspective, the ESMA’s Technical Advice to the Commission on MiFID II and MiFIR define the performance fees as an **incidental cost**, rather than an ongoing charges. It would therefore not be relevant to include such a fee in the overall ratio referred to in paragraph 2 of Article 25, this ratio aiming to give the potential investors an overview of the ongoing charges they will support when investing in the fund.
<ESMA_QUESTION_ELTIF_RTS_13>

Q14 Do you agree that the types of costs mentioned in paragraph 54 are fixed costs and that an assumption on the duration of the investment is necessary to calculate these costs in the numerator of the overall ratio mentioned in Article25(2), provided that this overall ratio is a yearly ratio?

<ESMA_QUESTION_ELTIF_RTS_14>
No. We do not agree that costs of setting up the ELTIF fund and distribution costs should be included into the overall ratio calculation. In addition to the answer provided as part of the Q13, we believe the type of cost mentioned in paragraph (54) should be considered as one-off charges i.e. costs and charges that are paid to the investment firm at the beginning of the investment services provided. The objective of an overall ratio, whatever its frequency, should be to present to potential investors the level of ongoing cost and charges they will bear when investing in an ELTIF. This ratio should therefore not include one-off charges.
In addition, we agree that an assumption on the duration of the investment would be necessary to calculate these costs in the numerator of the overall ratio mentioned in Article 25(2). However, we do not recommend to mix cost and charges well-known in advance (e.g. management fees expressed with a percentage) with other costs and charges assessed based on assumptions (e.g. distribution). It could otherwise be necessary to add specific mentions and disclaimers to state that these estimations are only based on assumptions and

may deviate from costs and charges that the investors will actually support. This situation may be a source of confusion and ambiguity to the investors, and potentially force the Asset Managers to reconcile ex-ante and ex-post cost and charges, in case of a significant deviation.
<ESMA_QUESTION_ELTIF_RTS_14>

Q15 Do you agree that the types of costs mentioned in paragraph 54 may be considered as fixed costs in the case of an ELTIF?

<ESMA_QUESTION_ELTIF_RTS_15>
No. We do not agree that costs of setting up the ELTIF fund and distribution costs should be included into the overall ratio calculation. We believe the type of cost mentioned in paragraph (54) should be considered as one-off charges rather than a fixed cost. The expression “fixed cost” is not precise enough to make it clear to the investors that they will not support these fees on an ongoing basis. These fees should not be considered as fixed costs in order to avoid any confusion to the investors.
<ESMA_QUESTION_ELTIF_RTS_15>

Q16 Do you agree with the proposed requirements? Would you suggest the introduction of any additional/alternative requirements? Please provide details and explain your position.

<ESMA_QUESTION_ELTIF_RTS_16>
We agree with the proposed requirements for the facilities available to the retail investors, as they are in line with the current practice under the UCITS Directive.

However, we would suggest to take into account the new communication technology commonly used now-adays such as web site and telephone. The AIFM should have the ability to choose to put in place facilities for retail investors either through physical facilities or through on-line / telephone facilities.
<ESMA_QUESTION_ELTIF_RTS_16>

Q17 What would you consider as appropriate specifications for the technical infrastructure of the facilities?

<ESMA_QUESTION_ELTIF_RTS_17>
As mentioned above, we would suggest to clarify in the Article 6 that the current market practices and the recent technological progress related to the distribution models are also taken into account.
<ESMA_QUESTION_ELTIF_RTS_17>

Q18 In the event that the RTS enter into force after the date of application of the ELTIF Regulation and authorisations are granted between the date of application of the ELTIF Regulation and the date of application of the proposed RTS, do respondents see a need for specific transitional/grandfathering provisions for the proposed RTS?

<ESMA_QUESTION_ELTIF_RTS_18>
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<ESMA_QUESTION_ELTIF_RTS_18>

Q19 Do you agree with the above-mentioned reasoning in relation to the possible costs and benefits of the options as regards hedging? Which other costs or benefits would you consider in this context?

<ESMA_QUESTION_ELTIF_RTS_19>
Yes, we strongly agree with the proposed approach and the benefit of a pan-European standardisation of the hedging risk policy and we insist on the need to widen the scope of products that an ELTIF fund manager can invest in.
<ESMA_QUESTION_ELTIF_RTS_19>

Q20 Do you agree with the assessment of costs and benefits above for the proposal on the sufficient length of the life of the ELTIF? If not, please explain why and provide any available quantitative data on the one-off and ongoing costs (if any) that the proposal would imply.

<ESMA_QUESTION_ELTIF_RTS_20>
We agree with the assessment of costs and benefits. The ELTIF manager has to determine the individual assets with the longest life-cycle into which the ELTIF plans to invest in.
<ESMA_QUESTION_ELTIF_RTS_20>

Q21 Do you agree with the assessment of costs and benefits above for the proposal on the criteria for the assessment of the market for potential buyers? If not, please explain why and provide any available quantitative data on the one-off and ongoing costs (if any) that the proposal would imply.

<ESMA_QUESTION_ELTIF_RTS_21>
We agree with assessment of costs and benefits and would stress that closed-ended funds that invest in less liquid and non-standard assets need to have the discipline of setting up plans for selling the assets they own throughout the life cycle and holding period of the assets even though the ELTIF fund is closed-ended.
<ESMA_QUESTION_ELTIF_RTS_21>

Q22 Do you agree with the assessment of costs and benefits above for the proposal on the criteria for the valuation of the assets to be divested? If not, please explain why and provide any available quantitative data on the one-off and ongoing costs (if any) that the proposal would imply.

<ESMA_QUESTION_ELTIF_RTS_22>
We agree with the assessment.
<ESMA_QUESTION_ELTIF_RTS_22>

Q23 Do you agree with the above-mentioned reasoning in relation to the possible costs and benefits of the option taken by ESMA as regards common definitions, calculation methodologies and presentation formats of costs of ELTIFs? Which other types of costs or benefits would you consider in this context?

<ESMA_QUESTION_ELTIF_RTS_23>
We agree that the proposed approach is unlikely to lead to significant additional costs to the extent that it provides clarifications on the Level 1 provisions and does not impose additional obligations beyond those already set by the ELTIFs Regulation, except the clarification that the cost disclosure information mentioned in the ELTIFs Regulation should be similar to the cost disclosure information as presented in the UCITS KIID.

Nevertheless, several Member states may wait for the PRIIPs Regulation in order to fully implement ELTIF. The two Regulations should be clearly separated.
<ESMA_QUESTION_ELTIF_RTS_23>

Q24 Do you agree with the assessment of costs and benefits above for the proposal on the facilities available to retail investors? If not, please explain why and provide any available quantitative data on the one-off and ongoing costs that the proposal would imply.

<ESMA_QUESTION_ELTIF_RTS_24>
TYPE YOUR TEXT HERE
<ESMA_QUESTION_ELTIF_RTS_24>