EFAMA Reply to the Consultation Paper on ESMA’s Technical Advice to the European Commission on possible implementing measures of the Alternative Investment Fund Managers Directive in relation to supervision and third countries

EFAMA\(^1\) welcomes the ESMA Consultation on ESMA’s Technical Advice to the European Commission on possible implementing measures on the AIFMD in relation to supervision and third countries.

The subjects of delegation and cooperation between supervisory authorities are of the greatest importance to EFAMA Members. EFAMA Members already today very widely delegate portfolio management and risk management to specialised managers, including managers in third countries. The delegation can be made both to third party entities or to an entity within the same financial group. Through this delegation, the best access to investment opportunities with the best local expertise in different markets (best knowledge of the local market and local laws/regulations) can be granted for European investors. It is important, that these existing delegation structures may remain in place upon the implementation of the AIFMD and that new delegation structures may be set up where required. EFAMA therefore welcomes ESMA’s approach to begin already today its work on the possible implementing measures of the AIFMD in relation to supervision and third countries.

Regarding the implementing measures proposed by ESMA, EFAMA allows itself to first provide some general comments before answering the questions raised in the Consultation Paper.

\(^1\)EFAMA is the representative association for the European investment management industry. EFAMA represents through its 26 member associations and 56 corporate members approximately EUR 14 trillion in assets under management of which EUR 8 trillion was managed by approximately 54,000 funds at the end June 2011. For more information about EFAMA, please visit www.efama.org.
Table of Contents

General Comments ......................................................................................................................................... 3
Limits of ESMA’s mandate ............................................................................................................................. 3
Alignment with existing UCITS and MiFID framework ................................................................................ 3
Implementing Measures for AIF for professional investors ......................................................................... 3
Inclusion of Explanatory Text into Boxes .................................................................................................... 4
Specific Comments ....................................................................................................................................... 4
III. Delegation (Articles 20 (1)(c), 20(1)(d) and 20(4) ............................................................................ 4
IV. Depositary (Article 21(6)) ................................................................................................................... 8
V. Supervision ................................................................................................................................................ 11
V.I. Co-operation between EU and third country competent authorities for the purposes of
Article 34(1), 36(1) and 42(1) of the AIFMD ............................................................................................. 11
V.II. Co-operation arrangements between EU and non-EU competent authorities as required by
Articles 35(2), 37(7)(d) and 39(2)(a) of AIFMD .......................................................................................... 14
V.III. Co-operation and exchange of information between EU competent authorities ............................ 14
V.IV. Member State of reference: Authorisation of non-EU AIFMs – Opt-in (Article 37(4)) ................. 17
General Comments

Limits of ESMA’s mandate

EFAMA would like to remind ESMA not to go beyond the Level 1 text and the mandate initially received. Some of the implementing measures proposed in the published Consultation Paper go beyond the requirements on the AIFMD Level 1 text. By going beyond these requirements, ESMA risks undermining the well balanced Level 1 Text in certain areas (please refer to answer on specific points below). Other parts of the proposals go beyond the advice the Commission has requested at this point in time (please refer to answer on specific points below).

Alignment with existing UCITS and MiFID framework

EFAMA appreciated the general approach taken by ESMA to seek, in providing its draft technical advice on possible implementing measures of the AIFMD, as far as possible an alignment with the existing UCITS and MiFID framework while ensuring that rules are appropriate and proportionate for the specific circumstances of the AIFM, the AIF and their investors (as reflected in its first Consultation Paper on advice to Parts I to III of the Commission request published in July 2013).

In the draft advice on possible implementing measures in relation to supervision and third countries published in this second consultation paper, ESMA seems to impose requirements going beyond the existing UCITS and MiFID framework. EFAMA encourages ESMA to review its draft technical advice in order to seek a better alignment of the AIFMD framework with the existing UCITS and MiFID frameworks.

Many EFAMA Members which will need to seek authorisation as AIFM, already hold a UCITS or MiFID license. For part of their UCITS and MiFID activities, delegation arrangements based on the existing UCITS and MiFID requirements exist and have been firmly and successfully in place for many years, including to entities outside of the EU. Very frequently, one delegation agreement is concluded with the entity outside of the EU, covering services for a broad range of UCITS and AIF. Divergences are difficult and costly to implement in the operational set-up of managers which will hold several licences.

EFAMA considers that the proposed requirements go beyond the existing UCITS and MiFID framework. These existing frameworks for delegation have proven successful over time. Imposing requirements going beyond these existing delegation frameworks will be more burdensome without bringing added value to investors. EFAMA therefore asks ESMA to amend its proposal to achieve greater alignment with the existing UCITS framework.

Implementing Measures for AIF for professional investors

EFAMA would like to remind ESMA that the AIFMD has been drafted to regulate all non-UCITS funds and to provide a European passport for marketing to professional investors. The benchmark of regulation was aiming at regulation for funds for professional investors. The AIFMD leaves it to
national legislators and regulators in the Member States to prepare stricter provisions for funds for retail investors at national level.

EFAMA considers that this approach should also be followed in the preparation of the Level 2 measures. The measures should be drafted to provide a minimum regulation for non-UCITS for professional investors. Any stricter provisions to regulate funds for retail investors should be left to the discretion of the Member States.

Against this background, a number of provisions in the ESMA draft technical advice, in particular regarding delegation, seem too strict because they go beyond the existing requirements under UCITS and MiFID. EFAMA asks ESMA to review and modify these proposals.

**Inclusion of Explanatory Text into Boxes**

EFAMA appreciates the helpful, detailed and precise information provided in the explanatory text throughout the Consultation Paper. On the other hand, EFAMA considers that the text in the boxes in some instances is not sufficient and difficult to understand without the explanatory text. Therefore, EFAMA encourages ESMA to include the necessary information from the explanatory text into the Boxes and indicates relevant examples throughout its answer below.

**Specific Comments**

**III. Delegation (Articles 20 (1)(c), 20(1)(d) and 20(4)**

<table>
<thead>
<tr>
<th>Box 1</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. In order to fulfill the requirement set out in Article 20(1)(d) of the AIFMD a written arrangement should exist between the competent authorities of the home Member State of the AIFM or ESMA and the supervisory authorities of the undertaking to which delegation is conferred.</td>
</tr>
<tr>
<td>2. Where the undertaking sub-delegates any of the functions delegated to it, a written arrangement should exist between the competent authorities of the home Member State of the AIFM or ESMA and the relevant supervisory authorities of the undertaking to which sub-delegation is conferred.</td>
</tr>
<tr>
<td>3. Where the sub-delegate further delegates any of the functions delegated to it the conditions in paragraph 2 shall apply mutatis mutandis.</td>
</tr>
<tr>
<td>4. With respect to the delegated functions from the entity to which functions were delegated or sub-delegated, the arrangement referred to in paragraphs 1 and 2 above should entitle the competent authorities to:</td>
</tr>
<tr>
<td>a) obtain on request the relevant information necessary to carry out their supervisory tasks as provided for in AIFMD;</td>
</tr>
<tr>
<td>b) obtain access to the documents relevant for the performance of their supervisory duties</td>
</tr>
<tr>
<td>Maintained in the third country;</td>
</tr>
<tr>
<td>----------------------------------</td>
</tr>
<tr>
<td>c) have the right to request an on-site inspection on the entity to which functions were delegated or sub-delegated. The practical procedures for on-site inspections should also be detailed in the arrangement;</td>
</tr>
<tr>
<td>d) receive immediately information from the supervisory authority in the third country in the case of breach of regulations;</td>
</tr>
<tr>
<td>e) ensure that enforcement actions can be performed in cases of breach of regulations.</td>
</tr>
</tbody>
</table>

5. The third country undertaking should be deemed to satisfy the requirement under Article 20(1)(c) when it is authorised or registered for the purpose of asset management based on local criteria which are equivalent to those established under EU legislation and is effectively supervised by an independent competent authority.

Q1: Do you agree with the above proposal? If not, please give reasons.

**General Comments**

**MoUs based on International Standards**

EFAMA supports the proposal in the explanatory texts Para. 1 and 7 to use MoUs based on international standards such as the IOSCO MoUs. In this context, EFAMA suggests that ESMA should reflect in its advice the terminology used in the IOSCO MoUs.

EFAMA welcomes the suggestions that MMOUs could be negotiated by ESMA to obviate the need that third country regulators conclude different bilateral cooperation arrangements and to ensure a level playing field. In this context, one EFAMA Member underlined that the written arrangement must exist between the competent authorities of the home Member State and the supervisory authorities of the undertaking to which delegation is conferred. It pointed out that the AIFMD does neither provide for a requirement nor for the possibility concerning arrangements between supervisory authorities of the undertaking to which delegation is conferred and ESMA.

EFAMA understands that it will be difficult to conclude a large number of MMOUs and MoUs in the short time until July 2013. EFAMA gladly remains at ESMA’s disposal to establish, based on comments by EFAMA Members, a list of countries with which the conclusion of MMOUs and MoUs is more urgent than others.

EFAMA would highly appreciate if the MMOUs and MoUs concluded would be published on a centralized website, for example the ESMA website, as well as on the websites of the competent authorities. This would greatly enhance legal certainty for all stakeholders concerned.

**Alignment with UCITS and MiFID framework**

In its draft advice on implementing measures regarding delegation, ESMA introduces requirements going beyond the existing UCITS and MiFID frameworks. These requirements are not provided for in the AIFMD Level 1 text. EFAMA encourages ESMA to review its draft technical advice and to bring it
into line with the UCITS and MiFID frameworks, as has been its approach in ESMA’s draft advice to Parts I to III of the Commission’s request. Further, the benchmark of the requirements under the AIFMD should be to set a robust framework for funds for institutional investors. Therefore, ESMA should in its advice not go beyond the existing requirements under the UCITS directive which is providing a framework for funds for retail investors.

More generally, EFAMA is concerned that third countries supervisors may not be able or willing to accept some of the conditions (eg. enforcement-related requirements) considered by ESMA in relation to the supervisory cooperation arrangements and thus could refuse to sign the required cooperation agreements.

EFAMA therefore urges ESMA to review its advice regarding delegation requirements to bring it in line with and not go beyond the existing UCITS and MiFID requirements.

**Inclusion of Explanatory Text into Box 1**

EFAMA members consider that parts of the Explanatory Text regarding Box 1 should be included into the Box in order to avoid future diverging or contradictory interpretation by regulators.

EFAMA urges ESMA to include into Box 1 parts of the Explanatory Text Para. 12 stating that where the conditions cannot be met (for example in case of non-existence of MoU between the authorities or lack of the authorisation of the delegate for purposes of asset management), delegation may still take place subject to prior approval by the competent authorities of the home Member State of the AIFM.

EFAMA also encourages ESMA to include parts of Explanatory Text Para. 1 into Box 1 to state explicitly that these requirements only apply in case of delegation of core functions such as portfolio management and risk management.

Furthermore, EFAMA suggests that ESMA introduces Explanatory Text Para. 11 into Box 1 to provide the necessary explanation on and interpretation of the scope of the envisaged right to request on-site inspections.

**Explanatory Text Para. 6**

The Explanatory Text Para. 6 mentions that written arrangements between competent authorities must be in place before the delegation starts.

EFAMA draws ESMA’s attention to the large number of existing delegation cases already in place today. In many cases, one single delegation agreement exists to cover delegation for several UCITS and AIF. In most cases, these agreements have been reviewed and approved by the competent authorities and auditors. ESMA’s requirement of written arrangements between authorities which must be in place prior to the delegation cannot apply for these existing delegations. EFAMA
therefore urges ESMA to modify its advice to accommodate such existing delegation cases. In particular for existing delegation cases which are fully in line with the UCITS and MiFID requirements, the requirement of a written arrangement prior to entry into force of the implementing measures to the AIFMD should not apply.

Box 1 Para. 1

EFAMA understands that the written arrangement which should exist between the competent authority and the supervisory authority may either be a general MoU covering all cases or a confirmation or exchange of letters establishing the supervisory cooperation regarding a specific delegation case. Already today, exchanges of letters between supervisors exist regarding existing delegation cases and should be sufficient even after the entry into force of the implementing measures of the AIFMD, in particular to avoid disruptions.

Box 1 Para. 4

EFAMA considers the text of Box 1 Para. 4 regarding on-site inspections is unfortunately not clear and fears it may lead to future diverging interpretation.

EFAMA therefore suggests that ESMA introduces Explanatory Text Para. 11 into Box 1 to provide the necessary explanation and interpretation of the scope of the envisaged right to request on-site inspections. Furthermore, it should be specified that on-site inspections may only be performed in accordance with existing international treaties (which as a general rule do not allow for foreign supervisors to perform on-site inspections directly without the presence of the local supervisory authority).

With respect to sub-paragraph d), EFAMA would appreciate clarification of the term “breach of regulations”, in particular whether this term refers to a breach of regulations of the jurisdictions where the relevant undertaking is domiciled or a breach of regulations which are specific to the AIFM and AIF.

EFAMA also suggests that ESMA should confirm explicitly that the on-site inspections must be limited to the specific case of delegation for which the competent authority requests the inspection and may not “on the spot” be extended to other delegation cases or other activities of the entity to which functions were delegated.

Box 1 Para. 5

EFAMA is concerned about the equivalence requirements introduced by ESMA in Box 1 Para. 5. By introducing equivalence requirements and equivalence tests ESMA goes beyond the requirements in the Level 1 text of the AIFMD and beyond the current UCITS and MiFID framework.
In particular, Box 1, paragraph 5 requires that the third country entity should be “authorised or registered for the purpose of asset management based on local criteria which are equivalent to those established under EU legislation.” Paragraph 10 of the Explanatory Text states that the equivalence assessment of the legislation should be made “by comparing the eligibility criteria and the on-going operating conditions locally applicable” to the corresponding requirements in the EU.

By contrast, there is no requirement for equivalence in the Level 1 text which requires that the entity is authorised or registered for the purpose of asset management, but does not specify the criteria for authorisation or registration.

The Level 1 text also included a carve out for a situation where the entity (EU or non-EU) is not authorised or registered. In such a scenario the AIFM must seek prior approval for its supervisor, before going ahead with the delegation. Some EFAMA Members for example, delegate portfolio management with prior approval by the competent authorities to group entities outside the EU which are not authorised as asset managers. If authorisation for the purpose of asset management and supervision is not required by the Level 1 text, there is no justification for introducing an equivalent requirement at Level 2.

EFAMA would appreciate if ESMA could modify its advice in the light of the comments above.

EFAMA therefore urges ESMA to review its advice regarding delegation requirements to bring it in line with the existing UCITS and MiFID requirements.

Q2: In particular, do you support the suggestion to use as a basis for the co-operation arrangements to be signed at EU level the IOSCO Multilateral Memorandum of Understanding of May 2002 and the IOSCO Technical Committee Principles for Supervisory Co-operation?

EFAMA supports the proposal in the explanatory texts Para. 1 and 7 to use MoUs based on international standards such as the existing IOSCO MoUs. In this context, EFAMA strongly suggests that ESMA should not go beyond the requirements set out in these existing IOSCO MoUs and should reflect in its advice the terminology used in the IOSCO MoUs.

IV. Depositary (Article 21(6))

Box 2

1. For the purposes of the assessment provided for in Article 21 (6) the following criteria should be met:

   a) The entity should be subject to authorisation and on-going supervision by an independent competent authority with adequate resources to fulfill its tasks;

   b) The local regulatory framework should set out criteria for the eligibility to act as depositary that are equivalent to those set out for the access to the business of credit institution or investment firm;
c) The capital requirements imposed in the third country should be equivalent to those applicable in the EU as set out in Article 21 (6) (b) depending on whether the entity is equivalent to a credit institution or to an investment firm;

d) The operating conditions are equivalent to those set out for credit institutions or investment firms within the EU depending on the nature of the entity;

e) The requirement on the performance of the specific duties as AIF depositary established in the third country regulatory framework are equivalent to those provided for in Article 21 (8) to (15) and in the relevant implementing provisions;

f) The local regulatory framework provides for the application of sufficiently dissuasive sanctions in cases of violations by the depositary;

g) The liability to the investors of the AIF can be invoked directly or indirectly through the AIFM, depending on the legal nature of the relationship between the depositary, the AIFM and the investors.

Q3: Do you agree with the above proposal? If not, please give reasons.

EFAMA considers that the provisions of Article 21.6 AIFMD defining the conditions that must be fulfilled to allow the appointment of a depositary established in a third country are extremely important to ensure the existence of a level playing field in terms of investors protection and to avoid any regulatory arbitrage in the choice of the country of establishment of the depositary. We also welcome the mandate given to ESMA to advise the Commission in the definition of the specific criteria that should be used to ensure that the third-country depositary is subject to effective prudential regulation and supervision which are of the same effect as Union Law and are effectively enforced.

EFAMA believes however that some of the criteria proposed by ESMA under Box 2 are inadequate to reach that purpose, either because they are not sufficiently clear, or because they go beyond the requirements of the Level 1 text to such an extent that, in practice, the conditions that are required to appoint a depositary established in a third country would become very difficult, if not impossible, to achieve, thus becoming a market barrier.

We would therefore like to make the following recommendations:

**Regulatory and supervisory framework which have “the same effect” as Union Law**

We note that Article 21.6(b) AIFMD does not mention “equivalency” but rather “the same effect”. A holistic view of the prudential regulatory and supervisory environment of a third country should be taken in accordance with the objectives/results-driven approach of the AIFMD rather than looking for exact matching of certain requirements as per the equivalence-based approach followed in Box 2 which may not be possible to achieve.

To illustrate our concern, paragraph 1(e) of Box 2 stipulates that the duties of the depositary in the third country regulatory framework should be equivalent to those referred to in Articles 21.8 to 21.15 AIFMD, covering among other the depositary liability regime. In our view, it is rather unlikely that any third country will have similar provisions in its regulatory framework (which is precisely why
Article 21.6(e) AIFMD stipulates that “the depositary shall **by contract** be liable to the AIF or to the investors of the AIF, consistently with paragraphs 12 and 13, and shall expressly agree to comply with paragraph 11”). Contractual measures can be used effectively to provide investor protection. This should not be addressed by requiring third countries to have a regulatory framework equivalent to the one in the EU.

Similarly, EFAMA believes that it is not realistic to expect the regulatory framework of a third country to contain equivalent provisions to EU law concerning the eligibility criteria (Box 2, paragraph 1(b)), the capital requirements (Box 2, paragraph 1(c)) and the operating conditions (Box 2, paragraph 1(d)) applicable to depositaries (please also refer to our answer to question 4 below).

**EFAMA therefore urges ESMA to remove any reference to the wording “equivalent” in the entire Box 2 and to replace it with “to the same effect” in order to remain consistent with the spirit and the letter of the Level 1 text.**

**Requirements concerning the competent authorities of the third country**

In Box 2, paragraph 1(a), ESMA stipulates that the depositary established in a third country should be subject to on-going supervision by an independent competent authority “with adequate resources to fulfill its tasks”.

EFAMA considers that this criterion is insufficiently clear and that it would be very difficult (and politically sensitive) to assess if a third country competent authority is equipped with “adequate resources”.

The same holds true in our opinion concerning the application of “sufficiently dissuasive” sanctions as foreseen in Box 2, paragraph 1(f).

EFAMA therefore recommends the use of less subjective criteria to assess the adequacy and the effectiveness of the third country supervisory framework. **In this context, EFAMA strongly welcomes the reference made by ESMA in paragraph 5 of the Explanatory Text to the IOSCO principles.** We are, indeed, of the opinion that a depositary should be considered to be subject to an adequate supervision if the third country regulator fulfills the criteria set out in Part II (“The Regulator”) of the IOSCO Objectives and Principles for Securities Regulation and relevant methodology.

Furthermore, we believe it is important that third country competent authorities are able to present their case.
EFAMA's reply to ESMA’s consultation paper on AIFMD in relation to supervision & third countries

Who is in charge of assessing that the regulatory framework and supervision of a third country have “the same effect” as Union law?

Finally, EFAMA believes that there is a need to clarify which entity is responsible to determine that a depositary established in a third country is subject to effective prudential regulation and supervision which have the same effect as Union law and are effectively enforced.

It is our understanding of the Level 1 text (Article 21.6, last paragraph of the AIFMD), that it is the EU Commission’s role to positively define (through the adoption of implementing acts) which countries meet the above-mentioned requirements.

However, we find paragraph 7 of the Explanatory text to be slightly confusing in this respect in the sense that it mentions that “the European Commission, having verified that the above-mentioned criteria are met, may issue decisions declaring a given third country jurisdiction as equivalent”.

For the avoidance of doubt, EFAMA would therefore recommend ESMA to replace the word “may” by the word “shall” in this last sentence and to include paragraph 7 of the Explanatory text in Box 2 of its final advice.

Q4: Do you have an alternative proposal on the equivalence criteria to be used instead of those suggested in point b above?

EFAMA is of the view that the proposed criterion referred to in point b is very strict and may prove difficult for third countries to achieve. Again, we therefore recommend replacing the “equivalence” criteria by the words “to the same effect”.

Furthermore, we do not consider it appropriate to require that a third country depositary must, in any event, be a credit institution or an investment firm, whereas Article 21.3(c) AIFMD provides that it may also be an entity “of the same nature”.

V. Supervision

V.I. Co-operation between EU and third country competent authorities for the purposes of Article 34(1), 36(1) and 42(1) of the AIFMD

Box 3

1. The co-operation arrangement with the third country competent authority should be in writing and provide for:

   a) exchange of information for supervisory purposes;
   b) exchange of information for enforcement purposes;
   c) the right to obtain all information necessary for the performance of the duties
EFAMA urges ESMA not to go beyond the mandate initially received by the Commission. In particular, EFAMA wants to remind ESMA that the Commission’s request for Technical Advice does at this point in time not cover the case of non-EU AIFMs marketing EU or non-EU AIFs in Member States without a passport. These cases for the time being still fall under the national private placement regimes and ESMA should refrain from including them into its advice. EFAMA therefore does not agree that the cases referred to in the 3rd bullet point of Explanatory Text Para. 2 to Box 3 should already be addressed by ESMA under the current advice.

Box 3 Para. 1 and Explanatory Text Para. 1, 4, 5 and 11

EFAMA supports the proposal in the Explanatory Text Para. 5 to establish cooperation arrangements taking into account the IOSCO Multilateral Memorandum of Understanding with respect to cooperation for enforcement purposes and, for supervisory purposes, the IOSCO Technical Committee Principles for Supervisory Co-operation. In this context, EFAMA suggests that ESMA should reflect in its advice the IOSCO terminology. EFAMA urges ESMA to include the explanatory text para. 5 into the text of Box 3 Para. 1 to avoid future diverging interpretation.

EFAMA welcomes the suggestions in Explanatory Text 4 that the cooperation arrangements would take the form of negotiated MMOU centrally negotiated by ESMA, again to obviate the need that third country regulators conclude different bilateral cooperation arrangements and to ensure a level playing field.

EFAMA understands that it will be difficult to conclude a large number of cooperation arrangements in the short time until July 2013. EFAMA gladly remains at ESMA’s disposal to establish, based on comments by EFAMA Members, a list of countries with which the conclusion of cooperation arrangements is more urgent than others.
Furthermore, EFAMA is in favour of the idea raised in Explanatory Text 11 that the agreements could be signed as a joint agreement between all authorities involved should several Member States be concerned.

EFAMA would highly appreciate if the cooperation arrangements concluded would be published on a centralized website, for example the ESMA website, as well as on the websites of the competent authorities. This would greatly enhance legal certainty for all stakeholders concerned.

**Box 3 Para. 1d**

EFAMA considers that the text of Box 3 Para. 1d regarding on-site inspections should be completed in line with Box 1 Para. 4 and EFAMA suggests that ESMA introduces Box 1 Explanatory Text Para. 11 into Box 3 to provide the necessary explanation and interpretation of the scope of the envisaged right to request on-site inspections. In particular, it should be specified that on-site inspections may only be performed in accordance with existing international treaties (which in most cases do not allow for foreign supervisors to perform on-site inspections directly without the presence of the local supervisory authority).

Again, EFAMA further suggests to explicitly confirm that the on-site inspections must be limited to the specific case for which the competent authority requests the inspection and may not on the spot be extended to other cases or other activities of the entity to which functions were delegated.

**Box 3 Para. 2**

Some EFAMA Members questioned whether the ESMA proposal in Box 3 Para. 2, requiring the third country competent authority to enforce EU legislation and national implementing legislation, was practically feasible and legally allowed. They mentioned that as a general rule a supervisor may only ensure the enforcement of, or compliance with, the laws and regulations applicable in its jurisdiction. These EFAMA Members would be grateful if ESMA could review its advice accordingly.

**Explanatory Text Para. 7**

EFAMA deems the requirement much too stringent that the competent authority in the third country should be able to meet the standards of data protection requested by the Data Protection Directive. As of today, only a handful of countries meet these standards. Should ESMA insist on the requirements, it would effectively become impossible for EU AIFM to manage non-EU AIF. Further, delegation to most countries would be impossible and as a result would mean that European investors would no longer be able to access regional expertise for their investments.

EFAMA therefore suggests that it should be sufficient that the competent authority in the third country should respect strong standards of data protection.
Q6: In particular, do you support the suggestion to use as a basis for the cooperation arrangement to be signed at EU level the IOSCO Multilateral Memorandum of Understanding of May 2002 and the IOSCO Technical Committee Principles for Supervisory Co-operation?

EFAMA supports the proposal in the explanatory text Para. 5 to establish cooperation arrangements taking into account the IOSCO Multilateral Memorandum of Understanding with respect to co-operation for enforcement purposes and, for supervisory purposes, the IOSCO Technical Committee Principles for Supervisory Co-operation. In this context, EFAMA suggests that ESMA should reflect in its advice the IOSCO terminology. EFAMA urges ESMA to include the explanatory text para. 5 into the text of Box 3 Para. 1 to avoid future diverging interpretation.

V.II. Co-operation arrangements between EU and non-EU competent authorities as required by Articles 35(2), 37(7)(d) and 39(2)(a) of AIFMD

<table>
<thead>
<tr>
<th>Box 4</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. The relevant provisions set out in Box 3 above could apply.</td>
</tr>
<tr>
<td>2. The final decision on the necessary safeguards in the case of a third country passport will be reassessed at the moment of the evaluation by ESMA required by Article 67 (i.e. before the entry into force of the relevant provisions in 2015)</td>
</tr>
</tbody>
</table>

Q7: Do you agree with the above proposal? If not, please give reasons.

Some EFAMA Members underlined, that on principle in order for a 3rd country passport to be provided there should be an absolute level playing field with respect to EU domiciled managers/funds. Any possibility of a lower standard for 3rd countries in relation to a passport runs the risk of rendering the AIFMD ineffective.

Furthermore, please refer to our comments under Box 3 above.

V.III. Co-operation and exchange of information between EU competent authorities

Q8: Do you agree with the above proposal? If not, please give reasons.

Explanatory Text 8

EFAMA understands that ESMA will be preparing advice regarding the cooperation and exchange of information between EU competent authorities based on its advice regarding implementing measures under Article 24.
EFAMA is extremely concerned about the proposed implementing measures under Article 24 as set out in ESMA’s consultation paper published in July 2013. For easy reference, please find below the comments EFAMA has raised regarding the draft implementing measures for Article 24:

**EFAMA Comments regarding Box 109 of the ESMA Draft Technical Advice to the European Commission on Possible Implementing Measures of the AIFMD**

“EFAMA is very concerned about the suggested reporting requirements to competent authorities which are extremely onerous. Our members are concerned about the volume of information and potential costs, particularly if this is required quarterly.

EFAMA strongly recommends that rather than quarterly reporting, reporting should be on an annual basis for all or at least most AIFs. The reporting deadline should be in line with that required for the annual report.

The reporting requirements largely exceed what is necessary to assess and manage systemic risks. The requirements are too detailed and reporting is required too frequently for majority of funds. A distinction should be drawn between hedge funds and other kinds of funds, between large funds with potential systemic implications and smaller funds.

ESMA proposes quarterly reporting for all AIFs on the basis of the extensive template provided in Annex V. Information on particulars of risk and liquidity management may be even required in a more frequent cycle by the competent authority of the AIFM. Many asset managers would then face the challenge to prepare quarterly reports for several dozens, or even hundreds, of AIFs. This task will involve high operational costs on a permanent basis as it will not be possible to fully automate the computation of the reporting items according to the reporting template in Annex V. Such significant costs must be considered a continuing factor to drag down the fund performance to the detriment of AIF investors. Our members estimate that the cost of implementing a quarterly reporting would be at least from half a person to one person a year.

EFAMA is fully aware of the fact that reporting to authorities is considered one of the cornerstones of the Directive for detecting potential systemic risks. However, in defining the applicable requirements ESMA must pay due regard to the proportionality principle as a general guideline for its recommendations. Measures taken for identifying systemic risk must still be commensurate to the probability of materialization of such risks in certain vehicles. It is incontestable that the potential for systemic risk in funds applying speculative trading strategies and an unlimited level of leverage is much higher than in funds with a conservative approach to leverage and clear rules on portfolio composition.

As the layout and content of the ESMA reporting template derives from the IOSCO work on reporting for hedge funds, most of the information required would not be relevant for other alternative funds. Moreover, it is important to bear in mind that, given the broad definition of an AIF as per the Directive, a significant proportion of AIF’s will not pursue alternative strategies at all but will be plain-vanilla funds investing only in long position over listed securities that had not opted for the UCITS status. Most of the disclosure require under the pro-forma are not relevant for these
unleveraged funds. Imposing these onerous reporting requirements to types of funds when not relevant is not in line with the “proportionality” principle.

Hence, we believe that the reporting requirements should ensure a proper differentiation between the types of AIF having regard to the corresponding probability of systemic risk. In EFAMA’s opinion, such differentiation could be performed according to the predominant investment strategy which shall be specified for each AIF as the first item in the reporting template.

ESMA itself has categorized the AIF investment strategies depending on the AIF type in the sample guidance for reporting included in the consultation paper. On the basis of these categories, the reporting duties should be attached first and foremost to AIFs following hedge fund strategies (column 1) and to funds of hedge funds (column 3). The remaining types of AIF should be granted significant reliefs in their reporting obligations towards authorities. This should pertain both to the “Other Funds” category which comprises UCITS-like long-only funds and to “Private Equity Funds” displaying a static risk profile which certainly does not justify more frequent reporting. Real estate funds the risk profile of which bears similarities with private equity investments should also be included in the “Other Fund” section.

EFAMA proposes to define the UCITS-like AIFs the following way: The AIF invests in assets which may be either eligible or equivalent according to the UCITS Directive and considers the risk spreading rules as well as the investment limits as provided in UCITS including the limits on leverage or such rules and limits which can be considered as equivalent to UCITS. This definition includes individual modifications according to national law.

EFAMA would indeed welcome a “decision tree” approach whereby the responses given to initial questions on the strategy, leverage and size would trigger a tailored report. EFAMA notes from Annex V that only section 1 is applicable to all AIFMs; Sections 2 and 3 only apply to an AIF ‘which is of a material size’. Much will depend therefore 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.

This approach would reconcile the legitimate concern of ESMA to establish the tools for an adequate supervision, the flexibility requested by the Commission and the efficiency objective of the industry. In EFAMA’s view it is highly disproportionate to expect the same reporting quality from highly leveraged hedge funds and traditional real estate or long-only funds for the purpose of identifying systemic risk. This view appears to be backed by the new strategy of the EU Commission to exempt certain vehicles from the AIFMD scope of application and to submit them to a “lighter regulatory regime” precisely for the reason of their negligible relevance in systemic terms, see The Commission consultation on Venture Capital funds.

Detailed EFAMA comments on Annex 5

• Page 422, section 1 : under the proposed format, the funds that do not pursue an alternative strategy, which can be very numerous as mentioned above, will be mingled in an “other funds”
category including as well infrastructure and commodity funds as well as an “other” category. EFAMA wonders whether it makes sense to mix funds with such different profiles.

• Page 423 and 424, individual exposures per categories of instruments: EFAMA believes that a category of cash and cash equivalent (for money market funds) should be added as well as a category “other assets” under point c) real assets (for assets such as art, wine,...).

• Page 423: EFAMA wonders why the G10 bonds are split per maturity and not the Non-G10 bonds (what is the purpose of this information?). EFAMA would also suggest considering the distinction between “investment grade” and “non-investment grade” similarly as for the corporate bonds, as EFAMA do not understand the relevance of the distinction between G-10 and Non-G-10.

• Page 425: typical deal size: the type of information required should be clarified.

• Page 425, point 4, value of turnover: formula for calculating turnover should be defined to order to allow consistency in the reporting. Turnover on money market instruments and derivative is usually not a relevant information as it is a direct consequence of the roll forward of short term positions. EFAMA would then suggest to remove these from the reporting.

• Page 426, section 1, 4, c): EFAMA assumes that there is a typo and this should read other assets rather than other funds?

• Page 426, section 2, point 6: if the fund is distributed through intermediaries (for instance, retail funds, feeders, funds of funds...), this information will not necessarily be accessible and the AIFM might not be in a position to report.

• Page 427, section 2: AIFM should not be required to disclose “expected” return and risk profiles to regulators. Such disclosure would be pure conjecture.

• Page 427, section 3, point 9: the category “infrastructure fund” mentioned here is not included as a category per say under question 1. As this section focuses on typical “hedge fund” risks, all fund categories other than hedge funds (for instance the unleveraged funds invested in listed securities as mentioned above) should be exempted from this section. Indeed, expected return cannot be assessed upfront for traditional funds taking long position on the markets as the return will largely derive from the beta.

• Page 429, section c) liquidity profile is not relevant for closed-end funds. They should be exempted from this reporting.

• Page 431, 18, i): if the fund is distributed through intermediaries (for instance, retail funds, funds sold through feeders, funds of funds, structures...), this information will not necessarily be accessible and the AIFM might not be in a position to report.

• Page 434: the category “other funds of funds” will mix up alternative and non-alternative strategies. Will this information be useful?”

V.IV. Member State of reference: Authorisation of non-EU AIFMs – Opt-in (Article 37(4))

Box 5

1. In cases of conflict between competent authorities of several Member States, the Member State of reference should be identified taking into account the Member State in which the AIFM intends to develop most effective marketing for its AIFs pursuant Article 37(4) (h).
2. The competent authorities identified by non-EU AIFM as the potential authorities of reference should immediately upon reception of the request, and no more than 48 hours following the reception of the request, contact each other and ESMA in order to consult on whether any other EU competent authorities or ESMA could potentially be involved pursuant to Article 37(4).

3. Where other EU competent authorities could potentially be involved, ESMA should immediately inform them.

4. The information referred to in paragraph 2 above should include the submission made by the non-EU AIFM, including in particular the details referred to in the last subparagraph of Article 37(4).

5. Within one week of their initial consultation or, where applicable, of receipt of the information by the other EU competent authorities, all the relevant competent authorities should exchange their views and jointly take a decision on the identification of the Member State of reference.

6. ESMA should facilitate the agreement between the relevant competent authorities.

Q9: Do you have any suggestions on possible further criteria to identify the Member State of reference?

EFAMA understands that providing criteria to identify the Member State of reference is difficult. EFAMA suggests that ESMA’s proposal could include a non-exhaustive list of criteria which could be applied by each AIFM to identify its Member State of Reference.

One possible criterion could be the criterion in the Explanatory Text Para. 2, namely the Member State into which the AIFM intends to develop its marketing activities. However, this should not be the only criterion, as marketing efforts may be done in waves targeting successively different Member States and only applying the criterion mentioned would frequently lead to a change of Member State.

Any criteria which leads to a frequent change of Member State should be avoided as it will not only create unnecessary monitoring and constant determination of the Member State of Reference but will also prove confusing and disruptive to investors and competent authorities.

In practice, to determine the Member State of Reference, consideration should be given to a number of criteria. EFAMA suggests that a list of non-exhaustive criteria should be used to identify the Member State of reference. These could include but should not be limited to either to the place where the distribution activity is developed from, or the place where the administration happens or the place where the investors are based (provided whichever one is chosen by the AIFM does not potentially lead to frequent changes of the Member State of Reference). Another of the non-exhaustive criteria could be the suggestion mentioned in Annex IV: Feedback on the call for evidence.
EFAMA’s reply to ESMA’s consultation paper on AIFMD in relation to supervision & third countries

para. 25 to take into consideration the pre-existing presence in the EU of other group entities when the AIFM is an affiliated entity of a group.

Q10: Do you think that any implementing measures are necessary in the context of Member State of reference given the relatively comprehensive framework in the AIFMD itself?

EFAMA suggests providing for implementing measures regarding ex-post checks to confirm the Member State of reference.

Q11: Do you agree with the proposed time period for competent authorities identified as potential authorities of reference to contact each other and ESMA?

Some EFAMA Members considers that the proposed time period for the competent authorities is very ambitious and proposes that it could be modified to 1 month. Other EFAMA Members welcome a shorter period.

Brussels, 22 September 2011

[11-4064]