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

31 July 2015

Date: 31 July 2015
2015/ESMA/1241

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	CFA Institute
Confidential[1]	☐
Activity	Other Financial service providers
Are you representing an association?	☐
Country/Region	UK

Introduction

Please make your introductory comments below, if any:

<ESMA_COMMENT_ELTIF_RTS_1>
Dear Sirs,

CFA Institute appreciates the opportunity to respond to Consultation Paper ESMA/2015/1239 following the request of the European Commission to ESMA seeking technical advice regarding European Long-Term Investment Fund (ELTIF) Regulation (the "consultation").

CFA Institute is the global association of investment professionals that sets the standard for professional excellence and credentials. The organization is a champion for ethical behaviour in investment markets and a respected source of knowledge in the global financial community. The end goal: to create an environment where investors' interests come first, markets function at their best, and economies grow. CFA Institute has more than 130,000 members in 149 countries and territories, including 128,000 Chartered Financial Analyst® charterholders, and 146 member societies.

By reason of the technical input sought by ESMA, CFA Institute has responded to selected sections of the consultation paper, in relation to the topics of (a) the use of derivatives for hedging purposes, (b) determination of ELTIF lifespan, (c) consideration of the market for potential buyers of the ELTIF's assets, (d) rules on the valuation of ELTIF assets, (e) disclosure of costs, and (f) facilities for retail investors. Our responses to the consultation questions are set out below.

Please do not hesitate to contact us should you wish further elaboration of the points raised.

Yours faithfully,

Sviatoslav Rosov, CFA
Analyst, Capital Markets Policy, EMEA
CFA Institute

Rhodri Preece, CFA
Head, Capital Markets Policy, EMEA
CFA Institute

<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>
As part of the ELTIF Regulation, ESMA proposes that ownership of derivatives assets by the fund is allowed only for the purposes of hedging. A usable definition of hedging is therefore necessary and ESMA proposes to benefit from existing definitions of the term as provided by international and EU legislation. To this end, ESMA proposes three pieces of legislation that are relevant:

1) International Financial Reporting Standard (IFRS) 9
2) Commission Delegated Regulation 149/2012 (regarding RTS on risk mitigation techniques for OTC derivatives contracts not cleared by a CCP).
3) CESR's guidelines on Risk Measurement and the Calculation of Global Exposure and Counterparty Risk for UCITS (10-788)

CFA Institute agrees that these pieces of legislation are relevant and will provide a satisfactory definition of the 'hedging' activity to be permitted under the ELTIF Regulation. We are not aware of other suitable pieces of legislation.
<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>
In the initial proposal of the European commission for a Regulation on ELTIFs there is an Impact Assessment on the issue of whether the use of leverage or financial derivatives should be banned. The Impact Assessment notes currency, inflation and interest rate risks are risks that require hedging in the best interests of investors. CFA Institute agrees that hedging these risks can be beneficial to investors and that there are no other risks for which the use of derivatives should be allowed.
<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>
In Question 2, we have stated that we cannot currently think of any other risks for which the use of derivatives should be allowed. However, given the potentially large range of eligible investment assets that could be held by ELTIFs, we agree with ESMA that the range of risks that are allowed to be hedged is difficult to assess and limit ex ante. We agree that the IFRS definition described above is a suitable base for this definition and should not be further narrowed by the technical standards.
<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>
CFA Institute believes that having a bespoke approach to hedging that is tailored to specific cases of ELTIFs is not desirable as it could lead to regulatory arbitrage and a focus on optimising the use of deriva-

tives rather than achieving long term value for investors. Further, if each fund was to take a bespoke approach that may be incompatible with the notion of a common product type underlying the ELTIF proposals.
<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>
No comment.
<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>
The life of an ELTIF is important for determining the redemption policy of the fund. There are certain instances in which early redemption is possible and also a disposal schedule must be provided no later than one year before the date of the end of the life of the ELTIF. When an ELTIF has assets with different maturities, it is important to estimate an accurate life for the fund that will ensure that the assets with the longer maturity are appropriately taken into account. Otherwise, it may be possible that at some stage an ELTIF portfolio becomes very concentrated in long maturity assets.

CFA Institute supports using the life of the longest maturity asset in the fund to determine the life of an ELTIF, however we believe it is important that the average duration of the fund be clearly disclosed as well. This additional disclosure would enable investors to better determine whether the fund is suitable for their needs, by highlighting the difference between the average duration and the minimum redemption period.

<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>
As part of the proposed RTS, the ELTIF must disclose an orderly disinvestment schedule no later than one year before the date of the end of the life of the ELTIF. We wish to emphasise that this disinvestment schedule should be disclosed to investors as well as regulators. As part of this schedule there should be an assessment of the market for potential buyers.

In making this assessment, ESMA proposes several relevant risks that should be analysed: the risk of illiquidity of the assets upon sale, the risks associated with legislative changes or political changes, or, the risk of deterioration of the economic situation.

CFA Institute agrees that these risks are relevant to the divestment of ELTIF assets at the end of the life of the fund. These three risks are suitably broadly defined that they should allow the ELTIF to consider any conceivable eventuality.
<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>

ESMA proposes to largely base regulatory technical standards for the valuation of assets in anticipation of their orderly disposal on the rules contained in Alternative Investment Fund Managers Directive (AIFMD). These rules state that asset valuation be conducted at least once a year as well as on each issue or subscription or redemption or cancellation of units or shares. However, ESMA proposes to add a requirement that an ad hoc valuation is carried out prior to the beginning of the disposal of assets and, specifically, that this valuation is carried out no more than 6 months before the schedule for orderly disposal is disclosed to the competent authority overseeing the ELTIF. Further, ESMA proposes a definition of fair value based on IFRS 13 which defines fair value as “the price that would be received to sell an asset or paid to transfer a liability in an orderly transition between market participants at the measurement date.”

CFA Institute agrees that the rules for valuation can and should be largely carried-over from AIFMD in order to minimise needless duplication of rules and ease the regulatory burden for ELTIFs.

CFA Institute also suggests consideration be given to the use of independent third parties for the valuation of ELTIF assets. A CFA Institute member survey performed in 2009 on the issue of AIFMD saw over 70% of respondents agree that a mandate for independent third party valuation should be established. We believe consideration should be given to ELTIF assets being valued by independent parties, rather than the ELTIF itself.
<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>
No comment
<ESMA_QUESTION_ELTIF_RTS_9>

Q10 Do you agree with the abovementioned assumptions?

<ESMA_QUESTION_ELTIF_RTS_10>
ESMA proposes to base the presentation and formats of costs, in part, on the Committee of European Securities Regulators (CESR) guidelines for the key investor information document (KIID). As part of the RTS, ESMA wants ELTIFs to disclose an overall ratio of the costs to the capital of the ELTIF. In this instance, capital refers to aggregate capital contributions and uncalled committed capital, calculated after deduction of all fees, charges and expenses borne directly or indirectly by investors.

In addition to the usual on-going charges, ESMA believes that in the case of ELTIFs some of the costs are entry costs borne by the investor and that a specific methodology should be set up to include such costs in the overall ratio. To amortize such costs over the life of the ELTIF some assumptions on the duration of the holding period are necessary and ESMA proposes to use the definition of life of the ELTIF as discussed in Question 6.

CFA Institute notes that amortizing costs across the full life of the fund may result in a disproportionate allocation of expenses towards the end of the life of the ELTIF. We propose that the amortization of costs could be done over the average duration of the fund.

However, CFA Institute disagrees that these costs need to be incorporated into a single overall ratio since their inclusion may limit comparability between ELTIFs with varying fixed entry costs. These fixed costs should be separate from ongoing costs in order to improve comparability.

<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>
ESMA notes that the following costs could be expressed as a percentage of the capital without assuming a duration for the ELTIF (provided the overall ratio is a yearly ratio): management and performance fees, administrative, regulatory, depositary, and custodial, professional service and audit costs.

CFA Institute agrees that the above costs are annual costs that could be expressed as a percentage of capital.
<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>
No Comment.
<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>
CFA Institute considers the inclusion of performance related fees into an overall expense ratio as undesirable. We wish to make the case for a clear distinction and disclosure of performances fees separately from the fixed costs described in Question 11.
<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>
ESMA considers that the costs of setting up the ELTIF and distribution costs are fixed entry costs and can be incorporated into the single overall cost ratio when an assumption about the duration of the ELTIF (i.e. the life of the ELTIF as described in Question 6) is made.

CFA Institute agrees with the technical definition of these costs as fixed costs as well as the need for an assumption as to the duration of the ELTIF if these costs are to be included in the overall cost ratio.

However, CFA Institute disagrees that these costs need to be incorporated into a single overall ratio since their inclusion may limit comparability between ELTIFs with varying fixed entry costs. These should be separate from ongoing costs in order to improve comparability.
<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>
See above.
<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>

In order to provide facilities for making subscriptions, making payments to unit- or shareholders, repurchasing or redeeming units or shares, and making available the information which the ELTIF is required to provide, ESMA proposes adopting the Undertakings for Collective Investment in Transferrable Securities (UCITS) Directive provisions as regards the facilities for retail investors. The key difference between the UCITS and ELTIF provisions is the explicit reference in the ELTIF rules to the provision of facilities allowing subscriptions to the units or shares of the ELTIF.

Other requirements are that the entity providing these facilities should act as a contact point for investors, ensure payments to retail investors in relation to distribution of proceeds and capital, and the rules or instruments of incorporation of the ELTIF should be made available through these facilities.

CFA Institute agrees with the requirements of the entity providing the facilities for retail investors.
<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>
No Comment
<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>
No Comment.
<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>
No Comment.
<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>
No Comment.
<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>
No Comment.<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>
No Comment.
<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>
No Comment.<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>
No Comment.
<ESMA_QUESTION_ELTIF_RTS_24>