

European Parliament Responds to the Commission Proposal for Review of AIFMD

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On 16 May 2022, the Committee on Economic and Monetary Affairs (ECON) of the European Parliament published a [draft report](#) on the European Commission's [proposal](#) for review of AIFMD. We previously [reported](#) on the Commission's proposal at the end of 2021. The new report takes into account many of the concerns raised by the industry and simplifies many of the newly introduced requirements in a helpful manner. It is therefore generally an improvement on the version published last year, but it remains to be seen how many of the proposed changes will be picked up in the course of the legislative process.

The key amendments proposed by ECON can be summarized as follows:

EXTENSION OF 'PROFESSIONAL INVESTOR' DEFINITION

The draft report introduces two additional categories of professional investors, namely:

- Investors committing to investing a minimum of EUR 100,000 who are aware of the risks associated with the envisaged commitment or investment; and
- Investors who are members of senior staff, portfolio managers, directors, officers, agents or employees of the manager or of an affiliate of the manager and have sufficient knowledge about the AIF concerned.

This extension is derived from the EuVECA and EuSEF Regulation and will broaden the potential investor base that can be approached in fundraising, under both the marketing passport and national private placement regimes. However, the definition of professional investors is only expanded for the purpose of marketing under AIFMD, and the definition of "professional clients" under MiFID remains unchanged. Accordingly, offerings to investors that qualify as "professional investors" under the new AIFMD marketing rules appear to continue to trigger special disclosure requirements under PRIIPs (the requirement to publish the key information document) if such investors do not also fall under the existing MiFID definition of "professional client". Also,

investment firms distributing investment funds will still have to treat the members of this new category of professional investors (under AIFMD) as retail clients for purposes of MIFID, if their distribution activity falls within the scope of MiFID.

SIMPLIFY THE NEW LOAN ORIGINATION REGIME

The ECON draft report attests that *“loan originating funds have positioned themselves as a very positive alternative financing instrument for real economy, SMEs and other investors”*. For this reason, the ECON proposed amendments to the Commission’s proposal *“aim to do away with unnecessary risk retention and to caution against creating product specific rules”*.

On this basis, ECON suggests to remove the Commission’s 5% risk retention requirement, applicable to loan origination funds that sell the loan after origination on the secondary market. Instead, the ECON draft will prohibit AIFs whose investment strategy is to originate loans with the sole purpose of selling those loans on the secondary market (the originate-to-distribute model). Under the draft proposed, we expect that private lending funds will still be permitted to sell loans on the secondary market as a matter of opportunistic early exit from a loan that was originally made with the view to hold it to maturity. The same should apply to loans sold before maturity that were held for a considerable period with the aim of earning interest.

Another helpful change in the ECON’s draft report is that loan origination is now not limited to closed-ended funds. If the loan originating fund is not closed-ended, the AIFM needs to be able to demonstrate to its home state regulator that the AIF has robust liquidity management systems. The criteria for “liquidity robustness” will be determined by the Commission through Level 2 regulatory technical standards.

Lending to a single borrower that is a financial institution has been limited to 20% of the fund’s “capital”, commitments or overall subscriptions. The Commission’s original proposal only referred to “capital”. The addition of the term “commitment” provides a less ambiguous definition, especially for closed-ended funds, as that term is already widely used as a reference point for investment limitations.

SIMPLIFY THE RULES AROUND REPORTING OF DELEGATION

The draft report also suggests to remove the requirement of reporting to a competent authority where the AIFM delegates more portfolio management or risk management functions than it retains. Instead, an obligation to regularly report details of delegation

arrangements to the AIFM's competent authority is suggested. The far less tendentious wording of the reporting obligation envisaged by the draft report appears to be a positive development for fund managers.

ANCILLARY SERVICES PERMITTED

The draft report also envisages further loosening the strict limitations on activities AIFMs can engage in, outside of portfolio management. In addition to the permitted non-core activities currently listed in the AIFMD, the draft states that AIFMs should also be able to provide other services not regulated in MiFID which represent a "continuation of services already provided or a use of internal competences", provided it causes no unmanageable conflict of interest. The references to the additional services are not particularly clear, but this appears to be a helpful extension.

REPORTING OF FEES AND EXPENSES

The draft report also suggests several revisions to the changes the Commission envisaged for an AIFM's reporting obligations. In particular, the draft report intends to remove the requirement to report fees and charges directly or indirectly charged to the investments of the AIF, as well as fees and charges borne by the AIFM and its affiliates in connection with the operation of the AIF. This change is welcome, as the references in the earlier draft to fees directly or indirectly charged to the AIF's investments raises difficult questions on scope, and benefit of such disclosure to investors was unclear. The obligation to report fees and charges payable by the AIF remains and should not raise any problems as it already reflects market practice.

NEXT STEPS

We are still at an early stage of the EU legislative process regarding the AIFMD. After the European Parliament, the Council of the European Union will provide its comments. Afterwards the EU legislators will enter into a trilogue to arrive at a final version of the AIFMD II.

We will keep you posted about further changes in legislative process as they arise.

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Please do not hesitate to contact us with any questions.

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