

Report of the AIFMD Stakeholders' Committee on the
Transposition of the AIFM Directive and the Development
of French Innovative Asset Management

Stakeholders' Committee
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Preface

Further to the work of the stakeholder group transposing the UCITS IV Directive into French law, and building on the October 2010 report of the Financial Services High-Level Committee on the " Strategy and Development of the French Asset Management Industry", an AIFMD Stakeholders' Committee sought to assess the issues raised by the AIFM Directive and prepare for its transposition into French law. The Committee brought together stakeholders of the asset management industry along with representatives of institutional investors and retail investors.

Its work enabled French asset managers and depositaries to make recommendations, in keeping with a core principle and four main priority areas intended to guide the transposition of the Directive into French law, identifying the challenges it raises and the industry's vision for the development of French alternative investment funds.

It should be noted that the work was based on the versions of the texts available when the Stakeholders' Committee was holding its meetings.

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Introduction

The Directive on Alternative Investment Fund Managers (AIFM Directive) was adopted by the European Parliament in November 2010 and entered into force on 21 July 2011. It prompts sweeping changes to the regulations governing the European alternative investment fund management industry. The purpose of the Directive is to provide a common set of rules for all alternative investment funds marketed in Europe to ensure a more secure framework for their development and to enhance investor protection. In the past, some industry participants were either unregulated or only loosely regulated. Now, all managers exceeding the thresholds set forth in the Directive will have to undergo an authorisation procedure and meet periodic reporting requirements. Transposing the AIFM Directive into domestic law presents a major challenge for many Member States, since it could bring about structural changes in the industry, depending on how the countries interpret it.

For France this issue is very important. Nearly half of French investment funds could qualify as Alternative Investment Funds (AIFs) within the meaning of the Directive, and nearly two thirds of France's management companies currently manage AIFs. Other investment vehicles that are not yet regulated may also be covered by the Directive. It therefore seemed critical to carry out a review, via an AIFMD Stakeholders' Committee¹ set up at the initiative of the French regulator, in order to discuss the strategic choices to be made when transposing the Directive into French law.

The *Autorité des Marchés Financiers* or AMF (the French securities markets regulator) wanted the broadest possible range of stakeholders to be represented on the Committee. Therefore, the Committee included industry associations, along with asset managers of all investment strategies covered by the AIFM Directive (mainstream asset management companies, "alternative" asset management companies, private equity firms and real-estate specialists). Representatives of institutional investors and retail investors, as well as the relevant national authorities, including the Directorate-General of the French Treasury, the Directorate of French tax legislation, the French prudential regulator, the *Autorité de Contrôle Prudentiel* (ACP) and the Authority in charge of accounting standards (*Autorité des Normes Comptables*), were also involved in the Committee's work. Depositaries, legal counsels and consultants also made major contributions to the discussions. Chaired by two members of the AMF Board, Monique Cohen and Jean-Luc Enguéhard, the Committee started work in November 2011.

The AIFM Directive has a dual objective: regulating alternative investment fund managers and monitoring and containing systemic risks. For this purpose, it introduces the requirement that all alternative investment fund managers be authorised and comply with a set of harmonised rules regarding risk management, conflicts of interest, delegation, valuation, depositaries and disclosure to investors. It also imposes reporting requirements with regard to regulators, including information about the main exposures and leverage of the managed funds. Even though French regulations already include many provisions applying to investment fund managers, including managers other than UCITS management companies, transposing the AIFM Directive means that some provisions of French laws and regulations will have to be revised, as well the AMF General Regulation.

In addition to imposing new requirements and providing a secure framework in which the managers concerned will do business, the AIFM Directive could provide many new development opportunities for French alternative investment fund management. First, simplification of the product range will raise the profile of the funds designated as alternative investment funds and facilitate investors' access to the wealth of various "alternative" strategies implemented by French managers. It will also give France's industry and infrastructure, which enjoy a reputation for high quality regulation, an opportunity to carve out a new position in the European and international financial markets, building on their head start² in terms of compliance with the requirements imposed by the AIFM Directive.

The AIFMD Stakeholders' Committee sought to assess the challenges that the AIFM Directive raises for the French industry and to prepare for its transposition into French law within a framework that gives the industry opportunities to simplify and modernise the product range covered by the Directive, step up the international promotion of the Paris financial centre, put French depositaries on an equal footing with their European competitors and give fresh impetus to the growth of French management companies, while maintaining a high level of investor protection.

¹ The list of the AIFMD Stakeholders' Committee members can be found in Annex 1 to this report.

² French industry players enjoy a head start on transposition since they are already subject to a regulatory framework that is very similar to the requirements set out in the AIFM Directive.

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The Committee's work enabled French asset managers and depositaries to make recommendations to be followed when the Directive will be implemented into French law, identifying the challenges it raises and the industry's vision for the development of French alternative investment fund management.

Part 1: Strategic vision for the development of French alternative investment fund management

1. Giving new meaning to "alternative investment fund management" in terms of innovation and diversity of products

For want of a commonly accepted definition, alternative investment fund management is usually considered as the kind of portfolio management applied to "alternative investment funds," i.e. hedge funds.

Until now, management companies for this type of fund have not been subject to any special regulations in many jurisdictions and they have not been as tightly regulated as management companies managing "conventional" investment funds, particularly with regard to the investment strategies that they use. Given the lack of special regulations, "alternative" investment funds have historically preferred to attract professional and experienced investors (primarily institutional investors and private wealth management customers), and have restricted the distribution of their funds to retail investors.

Furthermore, since the defining criteria vary from one jurisdiction to another or from one legal instrument to another (AIFM Directive, Dodd-Frank Act, US Securities and Exchange Commission, UK Financial Services Authority, etc.), the definition of alternative investment fund management has been unclear until now. It warranted a special harmonised framework and educational and communication efforts aimed at the various categories of customers likely to invest in such funds.

Rather than summing up alternative investment fund management in a single, limited category of funds known as "hedge funds", it could be said that all funds that are not UCITS³ are to be defined as "alternative investment funds". Accordingly, the managers of these funds should be governed by a common set of rules to ensure a more secure framework for their development and to enhance investor protection. This is the approach taken by the AIFM Directive.

This Directive gives an indirect definition of alternative investment fund management by means of the "alternative investment funds" managed by the managers covered by the Directive, which defines⁴ "AIFs"⁵ as collective investment undertakings, including investment compartments thereof, which:

- i) raise capital from a number of investors, with a view to investing it in accordance with a defined investment policy for the benefit of those investors; and
- ii) do not require authorisation pursuant to Article 5 of Directive 2009/65/EC.

The AIFM Directive therefore defines all of the investment vehicles that are not covered by the UCITS Directive as "AIFs"⁶, including UCITS-like funds, hedge funds, private equity funds and real-estate funds.

By making these distinctions, the AIFM Directive gives a more precise definition of alternative investment fund management and provides an internationally recognised European definition for a wide variety of investment funds applying "non-traditional" investment strategies. Such funds have given the French management industry a worldwide reputation for innovation and expertise.

This clarification of alternative investment fund management also provides a specific regulatory framework and limits the confusion that has tarnished the industry's reputation in the past for lack of proper communication and harmonisation across jurisdictions.

³ Undertakings for Collective Investment in Transferrable Securities authorised in accordance with Article 5 of Directive 2009/65/EC

⁴ Article 4 – AIFM Directive

⁵ "Alternative Investment Funds" within the meaning of the AIFM Directive.

⁶ "Alternative Investment Funds"

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2. The French asset management industry today

2.1 French asset management: a dynamic industry and a world leader

At the end of 2011, France had a population of 600 management companies, with a total of EUR 2,636 billion under management, with half invested in French funds and the other half under discretionary mandates or invested in foreign funds⁷.

The population of French management companies has more than doubled in ten years and is continuing to grow with start-ups, mergers, restructuring and consolidation of existing participants.

The French market features a vast array of entrepreneurial management companies specialising in active management, private wealth management, alternative investment fund management, funds of hedge funds and private equity.

The growing activity of many of these companies, along with that of larger companies, on international asset management markets continued in 2011.

France's asset management industry ranks as a world leader⁸. It is the European leader for collective investment management and ranks second worldwide, after the United States. France ranks second in Europe, after Luxembourg, for domiciliation of investment funds and third worldwide.

Over the years, France's asset management industry has built up a competitive and efficient model based on:

- longstanding investment management expertise;
- outstanding development of financial innovation over several decades;
- periodically updated regulations that clearly promote investor protection with due concern for the industry's efficiency;
- high savings levels and sound and diversified distribution networks.

France's asset management industry can also rely on an ecosystem⁹ featuring a wealth of business activities and skills (three French depositaries are in the global top ten), a growing number of specialised entrepreneurial management companies, 11,000 investment funds, including 8,000 investment funds marketed to retail investors.

Two French groups are in the global top ten asset management groups, and four are in the top twenty.

2.2 French alternative investment fund management: untapped demand from institutional investors and private wealth management customers

In addition to private equity funds and real-estate funds that the AIFM Directive classifies as AIFs, other French funds are also concerned, such as UCITS-like funds or hedge funds with non-traditional management strategies.

In 2003, French regulations created new types of investment vehicles, registered funds ("fonds contractuels") and authorised funds with streamlined investment rules ("ARIA" funds¹⁰) that could be used for "alternative investment fund management" strategies. The new vehicles provided French fund managers with new tools that were not subject to the rules of ordinary law and meant for qualified investors only.

The introduction of these new funds in France marked a first phase of innovation in alternative investment fund management that helped promote the French industry and make it more attractive to investors.

On the one hand, registered funds, which are very similar to discretionary investment mandates in terms of flexibility, provide investors with a secure framework for alternative investment funds where the rules are set out in the prospectus and activity follows a specific programme of operations.

On the other hand, ARIA funds also give investors access to direct alternative investment fund management within a regulatory framework where access requirements are set according to the nature of the investors and the riskiness of the funds. Disclosure rules also enhance the security of marketing arrangements for these funds by addressing the specific characteristics of each fund, the strategy used and the sophistication of the investor, who must demonstrate a certain level of financial knowledge and understanding. The streamlined investment rules and the leveraging of this type of product started to develop the competitiveness of the Paris financial centre for alternative investment fund management.

⁷ Source: AMF

⁸ & ⁹ Sources: AFG, *L'industrie française de la gestion d'actifs – Août 2011*

⁹ The notion of ecosystem is defined below.

¹⁰ *Agrésés à Règles d'Investissement Allégées*

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More than 400 of France's 600¹¹ management companies are now managing AIFs, as defined by the AIFM Directive, with a total of €690 billion under management.

In terms of products, France is estimated to have 6,300 AIFs, which break down as follows:

- 4,200 non-UCITS authorised securities investment funds, of which more than 3,800 are UCITS-like funds and the rest are ARIAs;
- 1,500 private equity vehicles, including 800 venture capital funds (FCPR¹²) under streamlined procedure not subject to authorisation;
- 300 real-estate funds (OPCI¹³/SCPI¹⁴);
- 600 registered funds.

The French alternative investment fund management industry, as defined in the AIFM Directive (i.e. non-UCITS) is significant, but it is still primarily concentrated on two segments of the market: UCITS-like funds and private equity funds.

Even though alternative investment fund management is generally thought of as involving hedge funds and registered funds, the proportion of French "alternative" vehicles or hedge funds is still quite small relative to the French asset management market and the international market.

In the past, French institutional investors have been somewhat reluctant to invest in certain types of "quantitative management" alternative investment funds given the market turmoil.

However, they considered that this type of investment strategies could nonetheless meet their needs in terms of risk-reward tradeoff. They felt that they could increase their exposure to such funds to a certain extent, provided that risks were fully identified, that efforts were made to achieve proper transparency, liquidity and disclosure and that the legal framework of the funds (regulations and internal rules) was appropriate.

In addition to private equity and real-estate investment funds, institutional investors are increasingly interested in alternative investment fund management. Family offices and private wealth management customers are willing to invest larger shares of their assets in such funds.

Some types of alternative investment funds offer different strategies, attractive returns and innovative asset classes that may meet the needs of some institutional investors and wealth management customers seeking:

- flexible management within a regulated framework (AIF managers offer dynamic management that is responsive to market events, by monitoring asset allocations of portfolios, for example);
- better performing products over the long term¹⁵, or at least products with a greater resilience compared to that of the equity markets.

In view of recent events involving certain categories of hedge funds, retail investors' image of some alternative investment funds may hinder their development. This image could only be improved in the long term by educational and market promotion efforts backed up by policies to reposition alternative investment fund management and to highlight its usefulness for financing the economy. In the short and medium term, it seems that private wealth management customers are more likely to be interested than the rest of retail investors in products that are more distinctive than UCITS funds. This means that there is still considerable untapped demand from retail investors for alternative investment funds.

The AIFM Directive provides investors with a new regulatory framework and new opportunities. It should therefore improve the prospects for the growth of French alternative investment fund management with institutional investors and private wealth management customers.

¹¹ Source: AMF – Figures as of 31 December 2011

¹² *Fonds Commun de Placement à Risque*

¹³ *Organisme de Placement Collectif en Immobilier*

¹⁴ *Société Civile de Placement Immobilier*

¹⁵ See KPMG/AIMA report of April 2012 on the outperformance of alternative management compared to "traditional" management in the long run, even under adverse market conditions.

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3. Alternative investment funds: an economic opportunity for France

Some alternative investment funds represent an economic opportunity for France, in view of the investment opportunities they open up for French investors (primarily institutional investors and private wealth management customers) and the growth potential that they provide for long-term savings products.

Generally speaking, insofar as asset management primarily benefits the financial market where the manager does business, some French alternative investment funds are contributing to the economic strength of the Paris financial centre.

This is especially true for private equity, which is particularly important for the French economy.

French private equity is a driving force for the financing of France's entrepreneurial development. France is the second largest European private equity market and the preferred investment destination for French private equity funds, accounting for nearly 90% of their investments. In 2011, all segments of private equity combined invested more than €7,800 million in France, supporting the growth of nearly 1,500 French companies. The amount of private equity invested in France grew by 28.5% between 2010 and 2011 and was primarily concentrated on companies in the greater Paris area, both in terms of the number of companies and the amount invested¹⁶.

Private equity contributes to the growth of French companies, thereby creating direct and indirect jobs because it requires skilled investment managers and risk management personnel, and because it invests in companies that then contribute to growth.

In addition, other alternative investment funds, such as real-estate funds and certain types of innovative funds (e.g. long-short strategies), also contribute to financing the economy.

It should be stressed that lawmakers have already acknowledged the economic utility of certain types of funds covered by the AIFM Directive (private equity funds, real-estate funds) by instituting special tax rules for them.

Alternative investment funds may be a helpful means of diversifying portfolios. The wide variety of asset classes and strategies that they provide meet the specific needs of categories of savers or investors whose return and risk diversification requirements may be matched by the many management profiles offered.

4. Strengths and growth opportunities for French alternative investment fund management

4.1 With vast expertise in financial innovation, the Paris financial centre has many of the strengths needed to develop alternative investment fund management

In addition to its vast expertise in private equity and real-estate fund management, France also has many strengths in innovative management.

The worldwide hedge fund market slowed sharply during the 2008 crisis, but it recovered slightly in 2011, exceeding \$2,000 billion¹⁷ in assets under management once again, while the number of funds increased significantly.

The AIFM Directive is thus being transposed at a time when this segment of alternative investment fund management is reviving. This is an effective indicator of the growth of non-traditional asset management.

The hedge fund market is constantly changing (800 funds were created in 2011, and 600 funds were shut down). As of the end of 2011, 40% of the assets were based in the United States and only 8% in Europe, 4% in Asia and 48% spread over the rest of the world (Middle East, emerging countries, etc.)

In addition, 56% of the investors were American, 32% European and 12% spread over Asia and the rest of the world. The vast majority are institutional investors, often from English-speaking countries, with 70% coming from the United States.

The French regulator approved a large number of programmes of operations for the indirect management of funds of alternative investment funds. Even if the assets under management in such funds of alternative investment funds (€15 billion at the end of 2011, for a total of 250 funds) and the average size of French alternative investment funds (€60 million) are still relatively small, French alternative investment fund managers are posting strong growth rates that are likely to be amplified by the new framework created by the AIFM Directive (source: HDF Industry Reports, Q4 2011).

¹⁶ 2011 Activity reports www.afic.data.com/Grant Thornton

¹⁷ Sources: HDF Industry Reports, Q4 2011

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One of the challenges of transposing the AIFM Directive is to give the French alternative investment fund management industry an opportunity to reposition itself and provide the right solutions for French and foreign investors so that it can achieve the same standing as the rest of the French asset management business in relation to its European competitors.

4.2 In terms of international growth, French alternative investment fund management industry has genuine strengths and enjoys a substantial head start in terms of regulation

France's many strengths in terms of asset management are based on sound regulation, a developed market and a substantial investor base, expertise based on strong and renowned academic programmes, as well as experienced depositaries that are already equipped to comply with forthcoming regulations.

France has developed its traditional management industry (UCITS) by providing secure regulation, an extensive range of products and services, high quality auxiliary financial services and appropriate access to institutional investor markets and retail investment markets.

It seems to have the essentials needed to develop the French brand of international innovative management and to enjoy growth rates that could match the recent resumption of the international growth of the alternative investment fund management industry.

The efforts that could be made (described below) and that could make French alternative investment fund management more competitive and enhance its image with institutional investors and private wealth management customers, could include a number of measures to make its product range clearer and easier to understand, with due regard for the specific characteristics of certain asset classes that need to be considered when transposing the AIFM Directive.

Simplifying and rationalising the product range will be central to the recommendations that the Paris financial centre will make for transposing the AIFM Directive. This will raise the profile of French expertise and funds with regard to alternative investment fund management.

The AIFMD Stakeholders' Committee noted areas for improvement, such as making tax rules clearer, since concerns about the stability of such rules are often cited as the main source of foreign investors' hesitations about investing in France.

Furthermore, given investors' new tendency to prefer high quality regulation, France, which has been a pioneer for investor protection, enjoys a head start that will enable it to undertake the transposition of the AIFM Directive, while seizing the opportunities it provides for French firms, which already comply with many of the requirements under the future regulatory framework.

Harmonising regulations across the European Union could give the French industry a competitive advantage, since it is already subject to a very similar set of rules. In this way, the AIFM Directive should represent an opportunity for the French asset management industry.

French market participants have some leeway to reposition themselves on the international market. They should take advantage of the transposition of the AIFM Directive to promote the quality of their ecosystem and their head start in terms of regulatory compliance. They should be part of the collective drive that could give the Paris financial centre the means to develop its alternative investment management in the long-term within a regulatory framework that ensures a high level of investor protection.

4.3 European passport: an opportunity to market the "France" brand on European and international markets

When the AIFM Directive comes into force in July 2013, European managers of European AIFs will be able to obtain a European passport. The passport will enable alternative investment fund managers to market their funds to "professional" investors¹⁸ across Europe, after obtaining authorisation from one national authority in Europe that will then supervise them.

Provided it is adopted by the European Commission, the passport may be extended to non-European managers and/or the marketing of non-European alternative investment funds in 2015. After that, it may replace national private placement arrangements and become the sole mechanism for marketing alternative investment funds in 2018.

¹⁸ Within the meaning of MiFID

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The passport introduced by the AIFM Directive is bound to reshape the market in several ways. First, it will provide investors in alternative investment funds with enhanced transparency and security with regard to products that often have a poor image. Second, it will provide supervisors with a clearer view of the alternative investment funds management market defined in the Directive, where it had previously been both difficult to provide a comprehensive definition of and difficult to ascertain the exact number of market participants and funds. Third, the passport should introduce a kind of certificate of quality for the alternative investment fund management market in Europe, where French products should quickly carve out a place for themselves, given their head start in terms of compliance with the requirements set out in the AIFM Directive. The passport should then be much more effective for French fund managers because of the simplification of the product range described above, which should enhance the international profile of their funds.

The AIFM Directive will harmonise European market participants and products, and the passport it introduces will facilitate marketing. Therefore, the Directive is bound to give fresh impetus to alternative investment funds both inside and outside of Europe, and France could benefit from this development.

5. The ambitions of the Paris financial centre with regard to the AIFM Directive

5.1 Using the Directive to boost the growth of French alternative investment fund management

As explained above, the French asset management industry has many strengths. It also operates in a robust ecosystem. In addition to the functions performed by French management companies on their own, there are many other professions that contribute to the renowned expertise and qualities of French portfolio management and administration processes. In addition to the management industry players and their talents, the quality and reputation of the French ecosystem are built on its depositaries, brokers, market infrastructures, regulators, accountants and legal experts, valuation experts, universities and researchers. They have made France a world leader in asset management.

Following the simplification measures implemented for the transposition of the UCITS IV Directive, the AIFMD Stakeholders' Committee recommended using the transposition of the AIFM Directive as an opportunity to improve the French asset management industry further in order to clarify regulations and products and promote the development of non-traditional management in France and in other countries.

The AIFM Directive could boost the growth of the Paris financial centre and makes it possible to build a growth strategy for French alternative investment funds based on four priority areas:

- clarifying and rationalising the French asset management product range;
- optimising the eligibility criteria of alternative investment funds for certain types of investors;
- optimising the strengths and advantages of French asset management;
- adopting a communications plan for the French alternative investment fund management industry, backed by promotion of its asset management expertise, the French ecosystem and the secure framework that it provides for investors.

These actions should:

- develop French investors' demand for alternative investment fund management;
- make the Paris financial centre more attractive to foreign investors;
- reposition French alternative investment fund management on the international market.

5.2 A legitimate, realistic and progressive goal

The size of the French alternative investment fund management industry, compared with some other leading markets, means that the French industry can achieve significant growth in the long term by progressively repositioning itself across the different asset classes defined by the AIFM Directive (innovative management, private equity, real estate, etc.) This repositioning will require efforts by all components of the French alternative investment fund management industry.

First, French market participants will need to be identifiable to investors in order to make their products more attractive. They will also have to retain the best talents and attract others to France, while differentiating themselves through innovation and competitiveness. Finally, each type of alternative investment fund must be accessible to the largest possible number of investors, provided their risk profiles are appropriate for the customer categories, and investors need reassurance about what they perceive as unstable tax French regimes.

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The AIFM Directive could also make it possible to attract alternative investment fund management companies to locate in France, which represents a major economic challenge for the Paris financial centre. The AIFM Directive could be an opportunity for Paris to promote the virtues of its ecosystem (regulatory quality, diverse range of expertise, Directive-compliant service providers), which provides an attractive location for alternative investment fund management companies and for the products that they manage.

The AIFM Directive introduces a new context for European alternative investment fund management industry players, based on improved transparency and enhanced investor protection.

It also creates an opportunity for French industry players, with their renowned expertise and high quality ecosystem, to:

- make their products more attractive and clearer;
- promote their potential;
- become key players in the newly recast European non-traditional asset management market.

Part 2: Transposition guidelines

1. Transposition involves strategic challenges, as well as technical challenges for the Paris financial centre

As part of the work by the AIFMD Stakeholders' Committee, it was important that work on transposing the AIFM Directive into French law give due consideration to the challenges involved for the French economy and for the stakeholders, including mainstream and specialised asset management players, private equity firms and depositaries.

The transposition proposals described below are based on the challenges that have been identified by all of the stakeholders in the French asset management ecosystem.

It is clear that the challenges raised by the AIFM Directive for the French alternative investment fund management industry have more to do with market positioning and competitiveness than with any fundamental problems with its actual transposition into French law, even though the challenges differ and involve different priorities, depending on the activities of individual stakeholders and their head start in terms of compliance with the AIFM Directive.

The Directive imposes the same set of rules for alternative investment fund management industry players throughout the European Union and, in a way, upholds the choices made by jurisdictions that are renowned for their rigorous financial regulations. The Paris financial centre already has a regulatory framework that is very similar to the requirements in the AIFM Directive. This enables it to use the transposition in order to highlight strategic recommendations aimed at repositioning its alternative investment funds and giving fresh impetus to the growth of its market.

Asset management industry players have shown their determination to make their product range clearer and more attractive, and to continue their efforts to promote the Paris financial centre. In addition to efforts to promote French alternative investment fund management with regard to institutional investors and private wealth management customers, which is bound to increase demand from French investors, the international promotion drive initiated as part of Paris Fund Industry and/or Paris Europlace should also be stepped up considerably so that the AIFM Directive allows French products to penetrate new markets and grow. Under these circumstances, it seems necessary to give the French alternative investment fund management industry the best chance to achieve the same size and influence as the rest of the French asset management industry in relation to its European competitors.

French private equity firms rank second in the European market. They have had to adapt to many regulatory changes in recent years and must now cope with the AIFM Directive under less favourable circumstances than in the previous period, with a financial crisis, and with problems in finding the funding in France that they need for the survival of their business model. Despite their contribution to financing local entrepreneurship, French private equity houses fear they will have to rely exclusively on international capital to finance their growth in view of the problems that they are having in raising funds from French institutional investors. Funding from these investors has dried up since the tightening of prudential requirements¹⁹. However, a number of specific proposals for their

¹⁹ Solvency Directive II, CRD IV, proposed IORP II Directive

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industry could enable it to grow and improve the existing system as part of the transposition of the AIFM Directive, while providing solutions adapted to their business.

Meanwhile, the real estate fund industry is preparing for those funds, which have been governed by specific laws and regulations until now, to be brought under the AIFM Directive, while, at the same time, brushing up their investment rules to comply with the laws and regulations that will now apply to real estate investment companies (SCPIs) as well. The industry could thus take advantage of the transposition to bring French real estate funds under the alternative investment fund management legal and regulatory framework, modernise the funds and identify them on the European market. They see the AIFM Directive as the forerunner of European quality certification for real estate funds that French experts would like to be a part of and that would continue to benefit the national economy by providing solutions for several categories of real estate users and by creating jobs in the real estate industry.

French depositaries see the AIFM Directive as an opportunity to clarify and harmonise the role and responsibilities of depositaries through a strong and highly detailed regulatory framework that entails a high level of accountability, like that found in the current framework for French depositaries. Given the circumstances, it is critical that the transposition of the AIFM Directive enables French depositaries to capitalise on their head start in terms of compliance with the requirements imposed by the Directive, while preventing unfair competition from rivals that do not offer the same level of security for investors. In addition to helping them increase their market share, the Directive is also an opportunity for French depositaries to develop a number of ancillary activities to complement their "conventional" depositary functions. The AIFM Directive clarifies the rules for depositaries seeking to exercise other functions, such as external valuer functions, net asset value calculation, or prime broker functions, provided that potential conflicts of interest are properly managed. For the sake of the competitiveness and attractiveness of the Paris financial centre, the transposition of the AIFM Directive should ensure that the implementation of these measures does not depend on compliance with new national rules that would hinder French depositaries from seizing these opportunities. For French depositaries, the clarification and harmonisation effort made with the adoption of the AIFM Directive will constitute a common foundation and working basis for any future legal and regulatory initiatives by the EU in this area.

In view of the challenges raised for each of them by the transposition of the AIFM Directive, the stakeholders have made several strategic and technical recommendations based on a core principle and four main priority areas.

These are described below.

2. Core principle: transpose the AIFM Directive faithfully into French law

The AIFMD Stakeholders' Committee approaches the implementation of the AIFM Directive with an eye to the opportunities it could bring for the French asset management industry, while continuing to ensure a high level of investor protection. The result of this approach is a strong recommendation for faithful transposition of the Directive, without adopting additional national rules that could hamper the competitiveness of French industry players and products.

The AIFMD Stakeholders' Committee feels that the AIFM Directive opens up cross-border opportunities by creating a common regulatory foundation for alternative investment fund management industry players in the European Union and by introducing a European passport, thus contributing to a more open European market for alternative investment fund management.

In France, this will mean an increase in the number of foreign funds (managed by French or foreign managers) on the market or French funds managed by managers located in another Member State. It will also promote the development of industry players managing alternative investment funds in France and mean more business for French depositaries.

However, the introduction of additional national rules could limit the benefits of the cross-border opportunities for the growth of general purpose and specialised fund management companies and of French depositaries. Given the pan-European dimension of the Directive, the rules to protect French investors must be carefully calibrated to ensure that they are not circumvented by entities offering cross-border opportunities from another Member State. To prevent French investors from being tempted to invest in funds that partially or totally escape supervision by the French regulator, France must take an open, European approach, which implies faithful transposition of the

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Directive. This position implies that the French regulator will drop some national rules and amend others to achieve optimal harmonisation of its regulatory framework with the European framework.

In this context, with an increasingly integrated European market and keen international competition, foreign industry players and their products will be able to come to France and offer their services without the French regulator having any say in the matter. Consequently, the AIFMD Stakeholders' Committee felt that it was critical to encourage these market participants and products to locate to France so that they do business and market their products under the supervision of the French regulator, which can then fulfil its role of protecting investors and fighting financial instability. It will then be up to France to ensure that the faithful transposition of the Directive maintains investor protection as a top priority. In fact, investor protection should be a key concern for all of the Member States when they transpose the AIFM Directive into their national laws. The AIFMD Stakeholders' Committee therefore suggests that the faithful transposition of the Directive should be backed by a number of measures described below when strictly necessary.

This means that harmonisation is critical for the transposition of the Directive in the different Member States. The European Commission and ESMA seem to be the most appropriate bodies to achieve this harmonisation through implementing measures and technical standards. These measures will provide a precise definition of the requirements for operational implementation of the rules set out in the Directive in order to prevent any differences in the Member States' interpretation or enforcement of the rules. For example, potential differences in Member States' interpretation of the AIF depositaries' tasks and obligations could lead to disparities in the level of investor protection between jurisdictions, proving the need to ensure European harmonisation of the regulations and the way they are implemented.

Recommendation 1	Transpose the AIFM Directive faithfully into French law.
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3. First priority area: Step up the international promotion of the Paris financial centre

3.1. Make the Paris financial centre more attractive to French and foreign managers and investors.

With the introduction of the European passport for management companies governed by the AIFM Directive, the AIFMD Stakeholders' Committee discusses the efforts that will be necessary to clarify French regulations for managers and products, particularly with regard to foreign investors, along with the efforts necessary to clarify the tax rules that could deter a number of foreign industry players from locating their operations in France.

Therefore, the AIFMD Stakeholders' Committee calls for a clarification of the tax rules and greater predictability, or even stability, of tax rules for managers and investors; and for entering into tax agreements with other countries that recognise the tax transparency of French funds.

Furthermore, new accounting, technical or regulatory provisions could also be introduced to complement the Paris financial centre's efforts during the transposition of the AIFM Directive into French law. Such provisions could include the introduction of more distinctive products, authorisation for alternative investment fund managers to accept and handle direct orders, broader eligibility of loans and commodities, listings for registered funds and the introduction of real estate capitalisation funds.

These reforms and measures are aimed at enhancing the attractiveness of French managers and the French ecosystem (lawyers, service providers, auditors, depositaries, advisers, etc.) and should offer new opportunities for foreign managers and investors.

Recommendation 2	Make the Paris financial centre more attractive to French and foreign managers and investors.
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3.2. Step up promotion of the French regulator's expertise and responsiveness

The French regulator enjoys an international reputation for expertise and responsiveness, as well as for the quality of its support for managers during the authorisation process for companies and products.

With the introduction of the European passport for management companies governed by the AIFM Directive, the French regulator could expand its disclosure of performance indicators relating to its services, such as average

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processing times²⁰ for authorisation applications for management companies and products. Rapid processing times contribute to:

- the development of new participants in the French market, who in turn contribute to competition;
- the responsiveness of managers, who have to market products that rely on strategies based on fleeting economic realities, requiring them to show a capacity for adapting to demand more and more quickly.

Before doing so, the French regulator should define indicators that will optimise its international promotion and focus more on how well it meets industry players' expectations.

Recommendation 3 Step up promotion of the French regulator's expertise and responsiveness.

3.3. Promote French alternative investment fund management in international markets by stepping up the actions to promote the Paris financial centre initiated during the transposition of the UCITS IV Directive.

French alternative investment fund management could be advertised to institutional investors and private wealth management customers to give fresh impetus to the industry. These two investor constituencies could both increase their exposure to alternative investment funds significantly if the resources used to promote them result in a better understanding and perception of this type of investment management.

The promotional action initiated during the transposition of the UCITS IV Directive should therefore be stepped up with regard to French alternative investment fund management in order to advertise it to French private wealth management customers and institutional investors. This is primarily the role of the representative industry associations.

The AIFMD Stakeholders' Committee suggests stepping up the international promotion plan for the Paris financial centre and the French ecosystem in order to persuade foreigners to invest in French products or delegate portfolio management to French companies, which will involve improving their perception of French administrative procedures. The purpose is to raise the profile of French alternative investment fund management, by rallying embassy trade offices and French Chambers of Commerce in other countries, as well as foreign Chambers of Commerce in France. To this end, the recommendations in the 15 October 2010 report on the "Strategy and Development of the French Asset Management Industry" by the Financial Services High-Level Committee need to be stressed. These recommendations called for:

- Systematic action, by the regulator in particular, to promote the French regulatory framework on international markets, by developing bilateral agreements, by highlighting the French framework in dealings with foreign regulators and, where warranted by the agenda, by including management companies and depositaries in discussions with foreign regulators when they visit Paris. Developing a positive international message about alternative investment fund management and rallying the embassy trade offices, French Chambers of Commerce in other countries to this cause, along with foreign Chambers of Commerce in France;
- Creating a marketing website in English and possibly other languages that is a one-stop information shop for foreign industry professionals and increase the number of special advertising features published in English;
- Launching a series of promotional actions by more systematically participating in and organising topical international conferences in other countries or in Paris, by organising road-shows promoted by the French Asset Management Association (AFG) and ²¹involving industry professionals and, where appropriate, political figures and the regulator, and by publishing more in foreign financial management journals and attending more job fairs at international universities;
- Setting up an organisation for international promotion under the aegis of the AFG that brings together Paris Europlace and all of the stakeholders (depositaries, transfer agents²²fund administrators, lawyers, auditors, etc.) in conjunction with the regulator and the public authorities. A committee would be set up to coordinate the actions in progress or in the initial phases and to define a coherent promotion policy. The committee's monthly meetings would bring together the people from each body responsible for implementing this assertive promotion policy. The AFG would provide the committee secretariat and run the meetings,

²⁰ Fast track authorisation processing time for equivalent funds is 8 days ("*procedure par analogie*"); average times are 20 days for new collective investment schemes, 2 months for new management companies and 1 month for extension of a management company's programme of operations (averages in 2011).

²¹ Association Française de la Gestion financière

²² centralisateurs

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supplementing its resources to fulfil this task.

These recommendations will require the French ecosystem to continue the international promotion of French asset management initiated by Paris Europlace and continued more recently with the transposition of the UCITS IV Directive (involving industry players, collective management, UCITS and "alternative" funds, along with discretionary investment management, etc.). Moreover, they will require more narrowly targeted actions carried out by the AFG with the close involvement of the regulator, the French Ministry of Finance and Paris Europlace within the framework of Paris Fund Industry initiative.

The promotion of the Paris financial centre with regard to alternative investment fund management can also be achieved through practical measures, such as:

- facilitating access to information about authorisation procedures and locating in France, which could require, among other things, the optimisation of the various electronic and physical media made available to foreign industry players;
- the possible introduction of a registration certificate for proving the legal existence of mutual funds to foreign investors could be considered.

Finally, the promotion of French alternative investment fund management could also be based on initiatives by the FINANCE INNOVATION competitiveness cluster and, more specifically, on the launch of the "EMERGENCE" fund designed to provide seed money²³ for new and innovative management companies in France.

Recommendation 4	Promote French alternative investment fund management in international markets by stepping up the actions to promote the Paris financial centre initiated during the transposition of the UCITS IV Directive.
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4. Second priority area: Seize the opportunities opened up by the AIFM Directive to give fresh impetus to the development of robust and competitive French management companies

4.1. Maintain a single management company regime that can be modulated by adding a programme of operations that matches the specific characteristics of each type of investment strategy

French asset management companies have a head start for the implementation of the AIFM Directive because of their organisational structure and, more specifically, because of their risk management system and transparent reporting system.

The single regime of French asset management companies provides a common core onto which programmes of operations that suit the specific characteristics of each type of management can be grafted. For the sake of competitiveness, the French model with a single management company regime that can be modulated should be maintained since it is clearer for foreign investors.

However, care should be taken to ensure that the management companies' programmes of operations suit the specific characteristics of each type of investment strategy, particularly in the case of private equity and real estate funds.

Principle of proportionality

The AIFM Directive calls for a risk control function to be instituted. This function needs to be instituted with regard to two criteria:

- i) the size of the managers
- ii) an appropriate and proportionate organisational structure.

France's regulatory framework is already in line with the AIFM Directive's provisions on risk management. That being said, it would be wise to develop an appropriate framework to deal with the separation of the risk control function from operational functions for private equity companies and real estate market participants in view of their size and the distinctive way they operate. Such a framework would make it possible to take a pragmatic approach designed to facilitate the establishment of the risk control function in small specialised asset management companies or in start-ups.

²³ Funds necessary to start a business

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Therefore, the AIFMD Stakeholders' Committee recommends applying the proportionality principle with regard to the separation of the risk control function, particularly in the case of private equity and real estate fund management companies.

It may also be worth considering having the risk control function of private equity companies report to the compliance and internal control function or to one of the senior managers. This would provide the risk control function with unrestricted access to the data it needs to perform its supervision duties.

When the internal control function is outsourced, in the case of small management companies or start-ups, where it is difficult to perform the function in-house from the very start, one needs to be vigilant about the quality of the control provided and about the independence of the external controller, given the contractual and business relationship between it and the management company. If the control function is outsourced, the scope of the tasks that can be delegated must be clarified to distinguish them from the ones that must be performed in-house by the compliance officer²⁴.

Recommendation 5	Maintain a single management company regime, which can be modulated through a specific programme of operations that matches the features of each type of investment strategy (innovative, private equity, real estate).
Recommendation 6	Where appropriate, apply the proportionality principle, particularly with regard to arrangements for the risk control function, for example, in the case of specialised asset management companies (private equity, real estate).

4.2. Allow management companies that are authorised under both the AIFM and UCITS directives to offer reception and transmission of orders (RTO)

The UCITS IV Directive does not include reception and transmission of orders (RTO) in the list of activities that management companies can carry out in addition to asset management. On the other hand, the AIFM Directive explicitly includes this function.

The single management company regime described above should allow an asset management company to be authorised as a UCITS management company and an AIFM, as provided for under Article 6(4) of the AIFM Directive²⁵, while maintaining the service of reception and transmission of orders, under a position proposed by ESMA in its Consultation Paper²⁶ of 23 February on the scope of the Directive with regard to AIFMs, which deems that the AIFM authorisation should prevail over the UCITS authorisation.

The AIFMD Stakeholders' Committee recommends maintaining the option that allows managers authorised under both the UCITS and AIFM directives to provide reception and transmission of orders for their customers with no restrictions. The other Member States' positions on this matter should also be considered to avoid any distortion of competition with other countries.

Recommendation 7	Allow management companies authorised under both the AIFM and UCITS directives to offer reception and transmission of orders (RTO).
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²⁴ *Responsable de la Conformité et du Contrôle Interne*

²⁵ "Article 6(4) of the AIFMD additionally allows AIFMs to be authorised to provide receipt and transmission of orders. This is not an additional activity that is permitted for UCITS management companies in the UCITS Directive. ESMA is of the view that AIFMs which are also UCITS management companies should be able to carry out this additional activity under their AIFMD authorisation, provided conflicts of interest are taken into account." (Key concepts of the Alternative Investment Fund Managers Directive and types of AIFM, point 51).

²⁶ ESMA's Consultation Paper "Key concepts on the AIFM Directive and types of AIFM" - 23 February 2012

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4.3. Allow portfolio management to be delegated to investment services providers²⁷ that are not management companies, while managing risks and conflicts of interest, but consider whether the restrictions allowed by the Directive, such as restrictions on AIFs marketed to retail investors, would enhance investor protection.

The AIFM Directive provides for delegation of the portfolio management function to:

- management companies governed by the UCITS Directive; or
- investment firms or credit institutions authorised to provide portfolio management services and governed by the Markets in Financial Instruments Directive; or
- third parties that are not necessarily subject to supervision (meaning entities that are not necessarily management companies, that are not necessarily regulated and may be located in countries outside of the EEA²⁸), but subject to the prior approval of the competent authority of the home member state of the AIFM and subject to cooperation between the authority of the AIFM and that of the delegate.

Three principles govern such delegation:

- the delegator does not transfer its responsibility to the delegate;
- the delegation must not entail conflicts of interest;
- the delegator must not delegate to the extent that it becomes a "letter-box entity".

In accordance with the core principle that the AIFMD Stakeholders' Committee has put forward on the faithful transposition of the Directive, this provision must be transposed into French law. However, the transposition of these rules would "liberalise" the rules on delegation of portfolio management to a certain extent, given that the doctrine applied in France up until now bans French funds from delegating portfolio management to an entity that is not authorised to provide collective investment management services in its home country.

This means that need to managed:

- the potential risks of opening up the delegation of AIFs marketed to retail investors, when the level of protection for such investors was the basis of the AMF's doctrine with regard to delegation of portfolio management; and
- the risks raised by delegates that may be entities without sufficient expertise or that are not subject to the same organisational constraints as asset management companies (e.g. a fund where the portfolio management function is delegated to a financial investment adviser²⁹ must be subject to the same organisational constraints as an asset management company). The risk related to the liberalisation of portfolio management delegation is very real when the delegate is not a regulated entity.

Consequently, the AIFMD Stakeholders' Committee recommends that, in keeping with the Directive, delegation of portfolio management be opened up to entities that are not authorised management companies, provided that such a delegation is restricted to regulated entities only. This raises the question of whether to use the option of restricting or banning the marketing of AIFs to retail investors in France, when management of the funds is delegated to entities that are not authorised for collective management or even subject to regulation.

Furthermore, in consideration of the European Commission's determination to tighten up the definition of "letter-box entities", the AIFMD Stakeholders' Committee also recommends opening up the delegation of portfolio management to investment services providers that are not management companies, but with strict vigilance against conflicts of interest and a more comprehensive list of controls that the AMF will implement in an appropriate manner.

This will liberalise the current system to a certain degree, while preserving an appropriately high level of protection for investors.

Recommendation 8	Allow portfolio management to be delegated to investment services providers that are not management companies, while managing risk and conflicts of interest, but consider whether the restrictions allowed by the Directive, such as restrictions on AIFs marketed to retail investors, would enhance investor protection.
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²⁷ ISPs

²⁸ European Economic Area

²⁹ Conseiller en Investissement Financier

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4.4. Align the manager's interests with those of investors through the managers' remuneration policy

The AIFM Directive requires management companies to establish remuneration policies. Annex II of the Directive sets out three main principles for remuneration designed to align the manager's interests with those of investors in the funds under management:

- variable remuneration must consider the overall results of the company and not only individual performances;
- the actual payment of the variable remuneration component must be deferred over time;
- at least 50% of the variable remuneration component must consist of units or shares in the AIF concerned, or related securities.

French management companies already comply with the first two principles, following the adoption of provisions relating to management companies' remuneration policies that were drafted by industry associations and approved by the AMF in November 2010.

The AIFMD Stakeholders' Committee notes that French industry players should be able to implement the provisions in the AIFM Directive on remuneration policies without difficulty and thus ensure that managers' and investors' interests are aligned.

The Committee also notes that the legal and tax rules applying to private equity are a major factor in the competitiveness of that sector. Consequently, the Committee proposes considering the establishment of provisions on managers' remuneration for all funds to ensure alignment of managers' and investors' interests, modelled notably on private equity industry practices.

The Committee also notes that ESMA's technical standards for managers' remuneration will have to be considered when defining these criteria, so as to avoid any distortion of competition with other Member States with regard to remuneration policies.

Recommendation 9	Allow the adoption of provisions governing fund managers' remuneration that promote alignment of the managers' interests with those of the investors.
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The AIFMD Stakeholders' Committee also recommended other changes concerning management companies which are described below.

- Allow private equity managers to continue performing valuation in-house

The AIFM Directive stipulates that an AIF's assets can be valued by the AIFM itself or by an external valuer.

The AIFMD Stakeholders' Committee brought up a number of specific issues concerning the valuation of private equity AIFs' assets.

First, the size of private equity management companies does not always allow them to consider the separation of functions stipulated by the Directive in cases where the AIFM decides to appoint an external valuer. Nor do their valuation procedures allow them to work with an external valuer who does not have the necessary knowledge.

Under the current procedure, before the private equity AIF manager makes an investment, it must carry out a large number of due diligence tasks and conduct comprehensive market research. This approach gives the manager a very sound grasp of the company, its sector and its competitors on the market. These factors are critical for a valuation.

In addition, the valuation of each asset in the portfolio is discussed by the management company according to the principles of a collegial and adversarial decision-making process, whereby discussions between the members of the management team and the senior managers of the management company ensure that the valuation is not determined by a single individual.

The use of statutory auditors is already based on the principle of oversight by an independent third party in practice. The final valuation of assets is based on a discussion between the valuer and the statutory auditor. Statutory auditors are also professionally liable for their certification of funds' financial statements, which makes them ensure that funds use robust methods and valuations of the companies in their portfolios.

In view of the very distinct characteristics of private equity in terms of asset valuations, which are based on knowledge of the activities of the companies in each portfolio and on the robust control systems already in place, the AIFMD Stakeholders' Committee recommends that the private equity industry players governed by the AIFM

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Directive should be allowed to continue performing their valuation tasks according to the existing internal practices, without being required to call on the services of an external expert.

Recommendation 10 Allow private equity managers to continue performing valuation in-house.

- Adapt requirements for asset valuation and supervision of depositaries to the specific characteristics of real estate funds ("SCPI"³⁰, "OPCI"³¹)

Existing practices regarding valuation methods are appropriate for French real estate fund managers. These managers hope that the transposition of the Directive does not undermine the effectiveness of these methods. Consequently, the AIFMD Stakeholders' Committee recommends that:

- real estate AIFs (French "OPCI" and "SCPI" funds) be allowed to continue the existing practice of using independent external valuers specialising in the valuation of real estate assets,
- that the cost of involving several experts be taken into consideration, along with the impact that these costs could ultimately have on the performance of French funds compared to analogous European funds,
- the liability of management companies for valuations be upheld since external valuations are very rarely disputed.

In the case of SCPI funds:

The existing regulations stipulate that each building owned by an SCPI fund should be appraised at least once every five years and that an appraiser must update the valuations each year.

The procedural rules for hiring appraisers provide that:

- real estate appraisers are independent. Once they have been "accepted" by the French regulator, they are appointed by the general meeting of the shareholders;
- any recently acquired building must be subjected to a full appraisal;
- the annual updates of appraisals are authentic valuations in that the appraisers may change the values on the basis of internally produced data provided by managers (changes in tenancy, improvements, changes in the environment of the property, etc.) or on the basis of external data analysed by appraisers (changes in real estate markets, interest rates, etc.)

The appraisers' work relies on increasingly comprehensive, accurate and rapid disclosures made possible by increasingly powerful market tools that make updates of appraisals even more accurate. The growing number of private and public databases also contributes to improving the quality of appraisers' work.

Therefore, there does not seem to be any need to increase the current frequency of valuation for SCPI funds. Such a move could even be harmful for end investors by generating substantial additional costs for the funds.

Consequently, the AIFMD Stakeholders' Committee feels that the five-year appraisal rule for SCPI funds, with annual updates, should be deemed "appropriate valuation" within the meaning of the AIFM Directive, subject to some amendments to fulfil the provisions of the Directive.

In the case of OPCI funds:

The existing rules for OPCI funds require two appraisers to be appointed and that each one values the assets every quarter. The transposition of the AIFM Directive into French law could be an opportunity to review these rules to ensure that the cost of compliance is warranted by the level of protection that the rules provide for investors.

Recommendation 11 Adapt valuation requirements to the specific characteristics of real estate funds (SCPI, OPCI).
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³⁰ Société Civile de Placement Immobilier

³¹ Organisme de Placement Collectif en Immobilier

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5. Third priority area: simplify and reshape the range of funds governed by the AIFM Directive

5.1. Reshape and simplify the range of French products into three fund categories by distinguishing between funds for professional investors, funds for retail investors and by accounting for the specific characteristics of specialised investment management

The AIFM Directive provides a better regulated and more secure framework for alternative investment fund management.

Currently, French and foreign investors have to choose investments from a wide and confusing range of products under current French regulations. Investors have no guidance for identifying the different strategies that fund managers use or in assessing risk levels.

The funds that could be deemed to be alternative investment funds under the terms of the AIFM Directive need to be rationalised to make them competitive and easier for investors to understand.

The names currently used for the different types of funds are not always easy to understand, particularly when translated into English for foreign investors. Consequently, the AIFMD Stakeholders' Committee recommends establishing a clear and easily understandable product range to improve the prospects of French alternative investment funds on export markets.

The existing product range could be rationalised into three distinct fund categories³². The trade names of these categories still need to be defined:

- "UCITS" (funds governed by the UCITS Directive);
- "retail alternative investment funds";
- "professional alternative investment funds".

Under this system, the "retail alternative investment funds" include UCITS-like funds, which are thus distinct from UCITS, along with other specialised retail funds (private equity, real estate, funds of hedge funds) and enable investors to diversify their investment into venture capital, real estate and alternative investment funds. On the whole, the regulatory provisions and, more specifically, the ratios that govern these funds are suited to their purposes. Since such retail funds could use investment strategies that are different from those used by UCITS, they could be more "tailored" on innovation to achieve higher returns and be marketed more easily to private wealth management customers, in addition to "retail" investors.

For "professional alternative investment funds", which would be marketed to qualified investors only ("professional" investors within the meaning of MiFID, or investors who invest more than €100,000), the Committee suggests choosing the existing "registered fund" format to bring together registered venture capital funds (FCPR contractuels), other registered funds (OPCVM contractuels), funds that are authorised but with streamlined investment rules (ARIA, FCPR à procédure allégée) and closed-end investment companies (SICAF).

Such professional funds could be either:

- authorised or registered,
- open or closed-end,
- listed or unlisted,
- identified by the planned strategy.

This measure could also promote the development of a range of "professional funds" to be broken down into different categories to meet the needs of both investors and the fund management company.

This new vehicle covering a wide variety of investment funds would have the characteristics of existing registered funds, thus making it one of the top ranking European vehicles in terms of efficiency.

To ensure a degree of continuity in marketing and to avoid confusing investors, it is important to make sure that the names used for these funds are changed only once in the coming years and do not have to be altered in the short term for the purposes of some other regulatory change.

³² The option being considered to rationalise the range of products that could be classified as AIFs within the meaning of the AIFM Directive is presented in Annex 2 to this report.

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Rationalising the product range will eliminate a number of fund names that are specific to the French market and often difficult for investors, especially foreign investors, to understand. Restructuring funds into a simplified and clearer vehicle should boost their growth.

Some members of the AIFMD Stakeholders' Committee suggested that exceptional arrangements could be made for a limited number of existing funds to maintain the benefits they provide and to avoid restricting access for certain categories of investors that could invest in them at no risk. According to these members, the straightforward transformation of closed-end investment companies (SICAFs³³) into registered funds would mean that they could be marketed only to professional investors in view of the higher minimum investment amount that would be applied. Yet according to the members in question, the current SICAF form, both in terms of investment horizon and tax treatment, meets the need to develop long-term savings products for retail investors. Consequently, they suggested making an arrangement to open up access to retail investors and to lower the minimum investment amount for this type of product subject to certain investor protection requirements to be defined.

In addition, to avoid hindering their distribution, institutional investors' investment rules could be reviewed, since they are required to invest in "UCITS" in the strictest sense of the current fund naming system.

Given the efforts to bring real-estate investment companies under the AIFM Directive for professional and retail investors, the AIFMD Stakeholders' Committee supports the idea put forward by real-estate alternative investment fund managers who want the rationalisation of the product range to be backed up by the following measures:

- Starting work on reviewing the management rules for real-estate investment companies as part of the drive to improve the competitiveness of alternative investment fund management,
- Realistic adaptation of the functions performed by the depositaries to the characteristics of the assets under management and real-estate alternative investment fund management, as well as the specific characteristics of real-estate investment companies (SCPI),
- Strong promotion of a coherent approach in the different Member States of the European Union to avoid creating competitive disadvantages for real-estate funds that are primarily intended for the domestic market, as is the case for real-estate investment companies (SCPI), which may incur additional costs related to the implementation of the AIFM Directive.

More generally, the Committee explained that a discussion on this topic would take place and give rise to a review of the investors' investment rules and an analysis of the changes in the product range and in the names of certain products. The purpose of this work is to modernise and simplify the existing product range, while preserving the specific features of certain product categories, particularly in terms of tax treatment.

Recommendation 12	Reshape and simplify the range of French products into three regulatory fund categories by distinguishing between funds for professional investors, funds for retail investors and by accounting for the specific characteristics of specialised investment strategies.
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- **Make "AIF" a brand for alternative investment funds**

AIFs will provide a perfectly suitable vehicle for alternative investment fund management. The amended MiFID will provide a clearer distinction between customer categories, which could be used to improve the structure of the asset management industry around the UCITS and AIFM Directives that now shape the industry, with UCITS being widely marketed to retail investors and AIFs being aimed more at a more knowledgeable customer base (professional investors and private wealth management customers).

This clarity about the investment product range will establish alternative investment funds as a recognised brand and help promote innovative investment strategies.

³³ Société d'Investissement à Capital Fixe

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- Explore the possibility of making real-estate AIFs eligible for employee savings plans (PEE-PERCO)

In addition to rationalising the product range with three fund categories, the AIFMD Stakeholders' Committee also recommends exploring a number of possible changes to employee savings plans to facilitate the marketing of real estate AIFs to a broader customer base. These vehicles provide investors with a more distant investment horizon than that usually offered by traditional investment strategies.

Some "retail" AIFs, including collective real-estate investment schemes, are not currently eligible investments for employee savings plans (PEE³⁴, PERCO³⁵). Consequently, the AIFMD Stakeholders' Committee suggests studying the possibility to extend the investment rules of employee savings plans to include collective real-estate investment schemes.

Recommendation 13	Explore the possibility of making real estate AIFs eligible for employee savings plans (PEE-PERCO).
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5.2. Harmonise the minimum investment amounts with one amount for retail investors and one for professional investors

The AIFMD Stakeholders' Committee recommends that the only subscription criterion for funds restricted to certain types of investors be to belong to the professional investor category as defined in MiFID.

The French regulations set five different minimum investment amounts, ranging from €0 to €500,000, depending on the type of fund. The AIFM Directive is an opportunity to simplify the rules considerably. Since the current minimum investment amounts do not really correspond to the scale of risks, the AIFMD Stakeholders' Committee recommends simplifying the system by having only two minimum investment amounts, as is the case in Luxembourg and Ireland:

- a minimum of €0 for retail products;
- a minimum of €100,000 for professional products.

Harmonising the minimum investment amounts at €100,000, instead of €250,000 at present for registered funds and €125,000 for authorised funds with streamlined investment rules (ARIA funds), will improve the competitiveness of French funds in Europe, without undermining protection for French investors.

However, care must be taken to ensure that the employees of private equity managers who co-invest in the funds under their management to align their interests with those of investors can still continue this sound practice, even when their investments are smaller than the minimum amount defined for professional investors.

Recommendation 14	Harmonise the minimum investment amounts with two distinct amounts: €0 for retail investors and €100,000 for professional investors.
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5.3. Explore the possibilities of new management techniques and new asset classes

- Bond issues: allowing certain French investment funds to issue bonds under very strictly regulated conditions at first

This possibility is advantageous in that the profile of the bonds issued by funds are more in line with the current wishes of investors, who are more interested in steady cash flows than in capital gains. Such bonds would also have a risk/return profile that is easier to understand.

However, bond issues backed by AIFs will need to be strictly regulated and restricted to certain types of AIF, such as registered funds, at first. Strict regulation should also govern leverage and structuring in order to avoid the problems seen in recent years with collateralised debt obligations (CDOs).

³⁴ Plan d'Epargne Entreprise

³⁵ Plan d'Epargne Retraite Collectif

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In order to explore the possibilities of this new technique, the AIFMD Stakeholders' Committee feels that the following questions need to be answered:

- What type of investors will be targeted by the marketing of these instruments?
- What are the provisions for issuer default (bankruptcy regime, etc.)?
- What measures regulate the structuring and leverage of these instruments?

- **New fund management techniques: exploring methods** for adjusting the net asset values used for subscriptions and redemptions, **while identifying the risks incurred and measures needed to regulate them.**

The AIFMD Stakeholders' Committee suggests exploring new methods for adjusting the net asset values of funds used for subscriptions and redemptions, such as "swing pricing" and "anti-dilution levy" techniques. The latter are designed to compensate long-term investors for the dilution of value and performance caused by frequent subscriptions and redemptions by certain investors, by making those investors pay for some of the resulting transaction and liquidity costs. This results in fairer treatment of investors who hold their investments over the long term.

Such adjustments are not allowed in France at present as funds are only allowed to charge fixed subscription and redemption fees. And yet, these adjustments would ensure fairer treatment of investors since they are already applied by many foreign funds, including some that are widely marketed in France.

The AIFMD Stakeholders' Committee is rather in favour of introducing new techniques to manage the liquidity of funds. However, to prevent such adjustments from hampering the marketing of the relevant funds by introducing uncertainty about redemption values for investors, the Committee recommends exploring the consequences of such adjustments before they are allowed and regulating them very strictly in any event.

Recommendation 15 Explore the possibilities of new management techniques, such as issuing bonds and adjusting the net asset values, subject to strict regulation.
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5.4. Review the AIFs' eligibility rules for institutional investors

The regulations governing some institutional investors do not allow them to invest in many AIFs for which the managers are covered by the AIFM Directive. For example, they are currently banned from investing in registered funds or registered venture capital funds ("FCPR³⁶").

Furthermore, a lack of clarity in the provisions on eligible asset classes for these institutional investors prevents them from investing in certain AIFs and certain UCITS. These potential obstacles to marketing AIFs could seriously impede their development by preventing them from reaching the critical mass needed to be competitive on international markets.

Therefore, the AIFMD Stakeholders' Committee feels that the regulations applying to the various institutional investors should be reordered to update the list of eligible investments. This work could be done as part of the transposition of the AIFM Directive into French law, given the level of the risks involved and institutional investors' ability to assess those risks.

On this point, the AIFMD Stakeholders' Committee feels that it would be more appropriate for institutional investors' investment rules not to be expressed in terms of fund classifications, but rather in terms of the levels of risk that the investor deems acceptable, given its liability constraints and its internal resources for assessing and monitoring risk. The AIFMD Stakeholders' Committee explains that these rules should be consistent with European legislation and regulations currently in preparation (Solvency Directive).

Recommendation 16 Review AIFs' eligibility rules for institutional investors.
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³⁶ Fond Commun de Placement à Risques

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The AIFMD Stakeholders' Committee also recommended other changes to reshape the product range, which are described below.

- Promoting the incorporation of investment funds

The AIFMD Stakeholders' Committee stresses that the development of incorporated AIFs, especially private equity funds, which already exist in other countries, could enhance governance and open up certain types of financial transactions that are not available to common funds (contractual funds) because of their tax treatment or investment procedures.

The main issues regarding the incorporation of funds relate to competition with other jurisdictions, where incorporated funds are very common, and to demand from certain institutional investors that have specific governance requirements that are met by incorporated funds.

In view of the competitive advantages involved, therefore, the AIFMD Stakeholders' Committee suggests that investment funds be allowed to incorporate and, more specifically, that they be allowed to incorporate as public limited companies (*société anonyme*, SA), simplified joint-stock companies (*société par actions simplifiée*, SAS), as provided for under current regulations, as well as limited equity partnerships (*société en commandite par actions*, SCA). Reservations were expressed about incorporation as SCAs however, in view of the governance rules applying to such partnerships.

Furthermore, incorporated private equity vehicles should benefit from the same tax treatment as current venture capital funds. This treatment provides incentives for investment in the national or local economy and would increase competitiveness with regard to foreign private equity vehicles.

Recommendation 17 Promote the incorporation of investment funds (SA, SAS, SCA)

- Allow the use of a language other than French in offering documents aimed at professional investors

The use of the French language provides a better understanding for investors and greater legal security for management companies, but the AIFMD Stakeholders' Committee still feels it is better to allow each management company to produce the constitutive documents and marketing literature of investment funds designed for professional investors in a language other than French, while requiring them to produce a French translation upon request.

This change is in line with current practices for certain categories of French funds that are already allowed to produce regulatory documents in another language commonly used in the financial sphere.

Recommendation 18 Allow constitutive documents and marketing literature for investment funds designed for professional investors to be written in a language other than French.
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6. Fourth priority area: Level the European playing field for French depositaries, for whom the impact of transposition is limited, in order to boost the attractiveness of the Paris financial centre, while giving due consideration to the specific characteristics of specialised investment management (private equity, real estate)

One of the strengths of the French asset management ecosystem is the organisation of the depositary function in France. Most of the measures in the AIFM Directive applying to depositaries are already in force in France. The challenges will be positioning French industry players on international markets, making sure rules regarding foreign service providers are fair and seizing the growth opportunities that the Directive opens up for depositaries, especially in the area of ancillary activities.

6.1. Maintain the current list of entities eligible to exercise depositary functions under French law for the sake of efficiency

The AIFMD Stakeholders' Committee feels that the list of entities authorised to exercise depositary functions in France is appropriate and does not wish to see it changed, other than to mention explicitly that branches of foreign investment services providers can be designated as depositaries for French funds. First, they shall make sure that they follow industry best practices that have the same effect as the general provisions of the AMF

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specifications applying to all French custodians in keeping with the principle of faithful transposition of the Directive.

In this respect, the two possibilities that the Directive offers to Member States to derogate from the eligibility criteria set out in Article 21(3) were discussed. The first possibility concerned authorising entities that are not subject to prudential regulation to be designated as depositaries under certain conditions, whereas the second possibility concerned allowing designation of a depositary that is not located in the same Member State as the AIF up until 2017.

- **Not taking up the option of allowing certain AIFs to entrust depositary functions to regulated professions**

Some European regulators wished to explore further the option of allowing regulated professions, such as lawyers or notaries, to exercise depositary functions for private equity funds or real estate funds under certain conditions.

Considering that commercial interest should not override the notions of investor protection and transparency, the AIFMD Stakeholders' Committee feels that the list of entities eligible to exercise depositary functions should not be extended during the transposition of the AIFM Directive into French law.

The Committee also feels that the derogations under the AIFM Directive constitute a risk in that regulated professions (notaries, lawyers) could be authorised to exercise depositary functions even though their skills are relatively distant from the expertise required, particularly in terms of supervision.

The Committee questioned the ability of these professions to comply, in practice, with the strict requirements of the AIFM Directive regarding supervision of cash flows and the custody of financial instruments. Nonetheless, the possibility for these professions to receive delegation from a depositary to perform recordkeeping was deemed to be desirable.

Furthermore, neither the management companies, which are accustomed to working with banks as depositaries, nor the representatives of the legal profession expressed any wish to see this arrangement changed.

It was also stressed that having regulated professions exercise depositary functions may not be less costly for AIFs and could ultimately create additional costs for investors compared to the present system.

Finally, it was felt that depositary tasks should be kept separate from the other tasks performed by the professions potentially concerned. For example, statutory auditors are in a regulated profession that would by nature be unable to exercise depositary functions. Exercising depositary functions would also mean that certain regulated professions would have to amend their own regulations. The delegation of some depositary functions would even be in contradiction with the initial activities of certain regulated professions.

The AIFMD Stakeholders' Committee recommends that, in light of these considerations, the present list of entities eligible to exercise depositary functions, as set out in the Decree of 6 December 1989, not be extended.

- **Do not take up the option under the transitional rules that would allow a French AIF to designate a depositary in another Member State up until 2017**

The option available to Member States of allowing fund managers to designate depositaries located in another Member State is not warranted in France, unlike countries where the depositary industry is undeveloped or where the selection of services is very restricted, and in view of the quality of the current players on the French depositary market. France's depositary industry has the talents, structures and tools necessary to meet the needs of French AIFs.

Given the strength of the French industry players, the AIFMD Stakeholders' Committee recommends that the option under the AIFM Directive that enables a regulator to allow an AIF to designate a depositary in another Member State should not be taken up.

Recommendation 19	Maintain the current list of entities eligible to exercise depositary functions and do not take up the option of allowing regulated professions to be designated as depositaries.
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- Ensure compliance with the professional practices required of French depositaries by branches of foreign investment services providers

Branches of foreign investment services providers must comply with the same operating rules as depositaries with their registered office in France in order to prevent any distortion of competition. This means that the principle of double-entry bookkeeping incumbent upon French depositaries acting as custodians must also apply to branches of foreign institutions.

The AIFMD Stakeholders' Committee therefore recommends that branches of foreign investment services providers seeking to do business as depositaries in France be required to comply with the provisions of the specifications for custodians applying to French depositaries with regard to asset protection, rules of conduct and organisational requirements.

Recommendation 20	Ensure compliance with the professional practices required of French depositaries by branches of foreign investment services providers.
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6.2. Bring the duties of UCITS depositaries into line with the AIFM rules

In view of the explanations that the AIFM Directive gives about the depositary function at the European level, the AIFMD Stakeholders' Committee considered the possibility of bringing the provisions about the tasks of depositaries appointed by UCITS into line with the requirements of the AIFM Directive. The discussions covered:

- a set of uniform rules for depositaries, regardless of the fund categories, acknowledging that the depositary's tasks depend primarily on the type of asset and not on the type of fund;
- a harmonisation that is critical for the competitiveness of the French industry;
- consideration of the very distinct characteristics of real estate and private equity, and, more generally, all assets that are not financial instruments;
- consideration of the distinct characteristics of employee savings schemes (particularly safe-keeping and ensuring the compliance of the managers' decisions with the decisions of the supervisory board);
- awareness of the risk of alignment on the lowest common denominator, which would undermine the acknowledged quality of French depositaries (which is a key element in the quality of French investment funds).

In view of the principles set out above, the AIFMD Stakeholders' Committee recommends that the duties of UCITS depositaries be brought into line with the requirements of the AIFM Directive, while ensuring that the distinct characteristics of real estate (and, more generally, assets that are not financial instruments) and employee savings schemes are given due consideration and while also ensuring that competition with other Member States is not distorted.

This alignment of the French system on the AIFM Directive will concern only the duties of depositaries at first. As to the potential changes to the liability rules applying to depositaries, the AIFMD Stakeholders' Committee recommends waiting for the texts on the revision of the UCITS Directive to be published before reviewing them at a later date.

Recommendation 21	Bring the tasks of UCITS depositaries into line with the requirements of the AIFM Directive while giving due consideration to the distinct characteristics of specialised management and wait for the publication of the texts relating to the revision of the UCITS Directive before starting work on any changes to the liability rules applying to depositaries.
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6.3. Allow depositaries to develop ancillary activities subject to compliance with the requirements in the Directive relating to the detection and management of conflicts of interest.

The AIFMD Stakeholders' Committee supports the faithful transposition of the Directive, with no national rules aimed at, for example, stopping a depositary from exercising the functions allowed under the Directive, which could distort the competition between French depositaries and other European depositaries.

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In addition, depositaries, like fund managers, administrators and accountants, have a role to play in enhancing the attractiveness of French financial markets by offering value-added services.

The "ancillary" services allowed by the Directive meet strong demand from management companies in an increasingly competitive European and international market that makes it critical to offer French depositaries the possibility of meeting the changing needs of their customers' multi-product and multi-country business.

The only service that the AIFM Directive deals with explicitly is the possibility for depositaries to be designated as an "external valuer", subject to a functional and hierarchical separation of this task from their depositary functions. This is seen as a real opportunity for depositaries, since they already have the expertise and organisational structure needed to provide this service to management companies. Therefore, the Committee favours registration of depositaries as external valuers, but it nonetheless recommends that the valuation business be clearly separated from the other services provided, such as calculating net asset values or pricing.

The AIFM Directive does not specify which other ancillary services depositaries can provide in addition to their duties as AIF depositaries. It merely requires appropriate management of conflicts of interest.

As part of its work, the AIFMD Stakeholders' Committee identified a number of complementary services that depositaries could provide, including:

- calculating net asset value,
- prime brokerage,
- cash administration,
- collateral administration.

However, it should be clarified that the possibility for depositaries to offer such value-added management services is subject to compliance with:

- the requirements of the AIFM Directive concerning identification and management of conflicts of interest;
- the principle that rules out making investment management decisions, which must remain the sole prerogative of the management company.

Recommendation 22	Allow depositaries to develop ancillary services and, more specifically, to be designated as external valuers, subject to compliance with the requirements of the Directive, including the functional and hierarchical separation of these services and the identification and management of conflicts of interest.
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6.4. Foster and support the industry players' efforts to promote the Paris financial centre

- Establish a common frame of reference for information flows between management companies and depositaries, with due consideration to the distinct characteristics of specialised investment strategies (private equity, real estate)

The industry associations and the depositaries met to develop a common frame of reference designed to implement contractual relationships between depositaries and management companies. This approach draws its inspiration from the standard "depository agreement" ("Convention dépositaires") implemented by French industry players and is intended to provide an incentive and support for industry players to standardise their procedures and information exchanges with depositaries, while giving due consideration to the distinct characteristics of certain aspects of non-traditional asset management.

This core set of standards will ensure a uniform approach to the disclosure requirements expected by depositaries and ensure that management companies monitor their constraints. It will also incorporate the adaptations needed to exercise the depositary functions for private equity AIFs and real estate AIFs.

This initiative will also enhance the transparency of the Paris financial centre and capitalise on the experience of its industry players with depositary functions by clarifying best practices for exchanges of information between depositaries and management companies, thereby making the market more attractive.

These informal rules are designed to provide a frame of reference that the relevant professionals can use to define an appropriate contractual arrangement. They will make the exchange of information more fluid and simpler, especially for real estate and private equity, based on a set of industry best practices. They will also ensure that these core standards do not interfere with the contractual relationship between management companies and depositaries in any way.

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Recommendation 23	Establish a common frame of reference for information flows between management companies and depositaries, with due consideration of the distinct characteristics of specialised investment strategies (private equity, real estate).
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- [Launch an industry initiative on fund administration to ease the rules on the marketing of funds registered in Euroclear France in other countries](#)

As part of the work to simplify the rules for direct orders to and promote the marketing of French funds in other countries, the Committee identified a number of obstacles to the distribution of funds with “bearer” units admitted to Euroclear France, the central depository.

- The hurdle to the marketing of French funds, especially funds admitted to Euroclear, lies in international practices that are different from French practices with regard to the subscription of securities. Foreign fund distributors are more familiar with the subscription of registered units;
- Some foreign distributors and custodians do not wish to open an account with a Euroclear member and would rather not disclose the identity of investors, which rules out administered bearer and registered units.

Consequently, the AIFMD Stakeholders' Committee recommends examining the possibility of facilitating the entry of foreign distributors and custodians into French funds' registers without having to disclose the identity of all of their investors as part of the transposition of the AIFM Directive.

In more general terms, the AIFMD Stakeholders' Committee recommends examining the different possibilities for removing obstacles to the distribution of funds admitted to a central depository.

The objective would be to facilitate transmission of orders concerning all funds admitted to the central depository (Euroclear France) from any French or foreign distributor or custodian, thus facilitating the distribution of French funds in other countries.

The associations representing asset management and the post trade industry in Paris are also conducting other discussions on the international distribution of French funds.

Recommendation 24	Launch an industry initiative on fund administration to facilitate the marketing of funds registered in Euroclear France in other countries.
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- [Management companies that fall below the threshold requiring them to designate a depository](#)

Companies that are not covered by the depository requirements of the AIFM Directive because they fall under the thresholds set out in Article 3 of the Directive raise the question of whether it is appropriate to let them choose whether or not to use a depository for vehicles that are currently unregulated and will become AIFs.

In these situations exclusively, this category of managers could be allowed to choose whether or not to use a depository.

However, the feasibility of such an arrangement needs to be examined in view of the problems it raises regarding the monitoring of the thresholds set out in the Directive, which apply to managers and not to funds. Furthermore, the wisdom of leaving the choice up to fund managers raises questions about investor protection, insofar as in certain cases, identical funds may or may not have depositaries, depending on the managers' choices.

Therefore, an examination of the possibility, at national level, to consider allowing management companies that fall below the thresholds in the Directive to decide whether they want funds that are not already required to have a depository to use a depository or not was recommended.

This option must be regulated to prevent it from being used to circumvent Article 21 of the AIFM Directive. This Article implements an external control system by designating a single depository. Such a system is critical for protecting investors' interests and fighting money laundering.

Recommendation 25	Examine the possibility of allowing management companies that fall below the threshold to choose whether to require funds that are not yet regulated to have a depository, while maintaining the possibility of converging on a single set of rules and ensuring investor protection.
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Part 3: The AIFMD Stakeholders' Committee's recommendations to the European Institutions

1. Funds that could be classified as AIFs within the meaning of the AIFM Directive: avoiding divergent interpretations by Member States

In the course of the work by the AIFMD Stakeholders' Committee, a number of issues concerning the interpretation of the AIFM Directive with regard to the level 1 text and the positions that other Member States might take came up and raised questions about the scope of the Directive.

The AIFM Directive defines alternative investment funds as "collective investment undertakings that raise capital from a number of investors, with a view to investing it in accordance with a defined investment policy for the benefit of those investors; and are not subject to the UCITS IV Directive."

Insofar as:

- the criteria used by the AIFM Directive to define an AIF are vague and do not define "Collective Investment Undertaking",
- the current French regulations³⁷ simply provide a list of collective investment undertakings and no definition,
- and, in theory, a wide variety of legal structures could be covered by the Directive;

it is necessary to ensure that the types of structures that could be deemed to be AIFs are the same in all Member States.

The questions concerning interpretation that come up with regard to the entities that could be deemed to be AIFs within the meaning of the Directive mainly involve the following structures:

- Unlisted holding companies;
- Listed real estate funds incorporated as SIC³⁸ in France (equivalent to REITs³⁹ in the UK);
- Others (agricultural groups, venture capital companies, financial innovation companies, etc.)

1.1 Unlisted holding companies

The Directive does not apply to holding companies. It defines a holding company as "a company with shareholdings in one or more other companies, the commercial purpose of which is to carry out a business strategy or strategies through its subsidiaries, associated companies or participations in order to contribute to their long-term value, and which is either a company:

- "operating on its own account and whose shares are admitted to trading on a regulated market in the Union; or
- "not established for the main purpose of generating returns for its investors by means of divestment of its subsidiaries or associated companies, as evidenced in its annual report or other official documents."

This exclusion only applies to certain holding companies, including:

- companies listed on a regulated market (e.g. Eurolist) that fit the definition of a holding company in the AIFM Directive;
- companies acting on their own account;
- holding companies for industrial or business groups, parent companies or passive holding companies, including LBO holding companies;
- personal holding companies, in keeping with the exclusions of family offices.

The issue of unlisted holding companies is still unresolved insofar as the Directive does not explicitly exclude them from the types of funds that can be deemed to be AIFs. The AIFMD Stakeholders' Committee urges ESMA to specify whether this type of entity should be excluded.

On the other hand, the list of excluded companies specifies that holding companies must be listed on a regulated market. This means that holding companies listed on a multilateral trading facility (MTF) cannot be excluded, according to a strict reading of the Directive. This issue must be resolved to prevent any distortions relating to interpretation.

³⁷ Article L-214-1 of the Monetary and Financial Code

³⁸ Société d'Investissement Immobilier Cotée

³⁹ Real Estate Investment Trust

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1.2 Listed real estate funds ("SIIC"/REITs)

The AIFMD Stakeholders' Committee also suggests that European institutions provide a clear and unambiguous answer to the matter of whether the AIFM Directive applies to certain real estate investment entities. Real estate fund professionals in France put forward some very sound arguments showing that most French listed real estate investment companies (SIIC) do not fit the definition of AIFs given in the AIFM Directive.

The AIFMD Stakeholders' Committee feels it would be highly desirable for the European institutions to clarify the issue of whether an entity that is explicitly excluded under the Directive, but has characteristics matching those defining an AIF in the AIFM Directive, would be deemed to be an AIF. If so, many provisions applying to "financial entities" (EMIR, Dodd-Frank Act, tax on financial transactions, etc.) would apply to it.

1.3 Other vehicles open to interpretation

There are also other types of joint stock companies that are tax vehicles, such as venture capital companies ("SCR⁴⁰"), financial innovation companies (SFI) and wealth tax and personal income tax holding companies that, according to the definition in the AIFM Directive, are likely to be covered by the Directive.

Clarification is needed about this type of entity, which, depending on how the AIFM Directive is interpreted, may or may not be funds covered by the directive.

Some categories of existing unregulated structures of this type are not explicitly excluded by the Directive and it could be a matter of interpretation whether they are to be deemed AIFs during the transposition. Consequently, a decision-tree methodology based on the purpose of the AIF (financial investment or exploitation of the underlying assets) that is used to qualify funds as AIFs or not could be promoted at the European level so that it is adopted by all of the Member States.

2. Agreements with third countries: can we agree to a third-country passport in 2015 without any reciprocal measures?

At the international level, the AIFMD Stakeholders' Committee suggests taking the offensive rather than using defensive measures, which would mean erecting barriers to the entry and thereby hindering the marketing of certain categories of foreign AIFs. However, the Committee stresses the risks involved, including the undermining of investor protection and the requirement of real reciprocity from third countries. The French authorities and the Paris financial centre brought up these risks with regard to the proposal for a third-country passport when the Directive was still in the negotiation phase, along with their reservations about the ultimately fairly loose framework chosen for this passport in the Directive now adopted.

This approach will require rapid action to convince European institutions, such as:

- stepping up the work already under way with regard to ESMA and the European Commission. This work is aimed at having ESMA come up with rigorous, specific and measurable criteria for evaluating the supervisory frameworks and prudential regulations of third countries, looking at whether a body of rules exists and how the local authorities and jurisdictions enforce them in practice. It is also aimed at the European Commission to ensure that the measures it then takes, acting on a mandate from the European Council, actually assess whether third countries actually have such a framework;
- establishing specific and measurable reciprocity clauses in the cooperation agreements with each of the third countries concerned (developed below in Part 3).

Nevertheless, given some of the extraterritorial US measures and barriers that some third countries have erected, it seems to be especially risky for Europe to allow a "third-country" passport to be introduced in 2015 without any reciprocity measures. So that French fund managers and the French asset management ecosystem can meet the challenges that competition from third-country industry players raise in Europe and, more specifically, in France, reciprocity should be encouraged, along with the notion of the "same effects" of regulations in word and deed, rather than building lines of defence. Rejecting the idea of establishing protectionist measures to cope with the risks raised by the entry into force of the international aspects of the Directive, which were sometimes negotiated and adopted in haste, will require convincing ESMA to ensure that all of the Member States interpret the AIFM Directive the same way and that they do not interpret it as allowing the marketing of products that are contrary to one of the core principles of the Directive, which is to improve investor protection.

⁴⁰ Société de Capital Risque

SUMMARY OF RECOMMENDATIONS

- Recommendation 1** Transpose the AIFM Directive faithfully into French law.
- Recommendation 2** Make the Paris financial centre more attractive to French and foreign managers and investors.
- Recommendation 3** Step up promotion of the French regulator's expertise and responsiveness.
- Recommendation 4** Promote French alternative investment fund management in international markets by stepping up the actions to promote the Paris financial centre initiated during the transposition of the UCITS IV Directive.
- Recommendation 5** Maintain a single management company regime, which can be modulated through a specific programme of operations that matches the features of each type of investment strategy (innovative, private equity, real estate).
- Recommendation 6** Where appropriate, apply the proportionality principle, particularly with regard to arrangements for the risk control function, for example, in the case of specialised asset management companies (private equity, real estate).
- Recommendation 7** Allow management companies authorised under both the AIFM and UCITS directives to offer reception and transmission of orders (RTO).
- Recommendation 8** Allow portfolio management to be delegated to investment services providers that are not management companies, while managing risk and conflicts of interest, but consider whether the restrictions allowed by the Directive, such as restrictions on AIFs marketed to retail investors, would enhance investor protection.
- Recommendation 9** Allow the adoption of provisions governing fund managers' remuneration that promote alignment of the managers' interests with those of the investors.
- Recommendation 10** Allow private equity managers to continue performing valuation in-house.
- Recommendation 11** Adapt valuation requirements to the specific characteristics of real estate funds (SCPI, OPCI).
- Recommendation 12** Reshape and simplify the range of French products into three regulatory fund categories by distinguishing between funds for professional investors, funds for retail investors and by accounting for the specific characteristics of specialised investment strategies.
- Recommendation 13** Explore the possibility of making real estate AIFs eligible for employee savings plans (PEE-PERCO).
- Recommendation 14** Harmonise the minimum investment amounts with two distinct amounts: €0 for retail investors and €100,000 for professional investors.
- Recommendation 15** Explore the possibilities of new management techniques, such as issuing bonds and adjusting the net asset values, subject to strict regulation.
- Recommendation 16** Review AIFs' eligibility rules for institutional investors.
- Recommendation 17** Promote the incorporation of investment funds (SA, SAS, SCA)
- Recommendation 18** Allow constitutive documents and marketing literature for investment funds designed for professional investors to be written in a language other than French.
- Recommendation 19** Maintain the current list of entities eligible to exercise depositary functions and do not take up the option of allowing regulated professions to be designated as depositaries.
- Recommendation 20** Ensure compliance with the professional practices required of French depositaries by branches of foreign investment services providers.
- Recommendation 21** Bring the tasks of UCITS depositaries into line with the requirements of the AIFM Directive while giving due consideration to the distinct characteristics of specialised management and wait for the publication of the texts relating to the revision of the UCITS Directive before starting work on any changes to the liability rules applying to depositaries.

Recommendation 22 Allow depositaries to develop ancillary services and, more specifically, to be designated as external valuers, subject to compliance with the requirements of the Directive, including the functional and hierarchical separation of these services and the identification and management of conflicts of interest.

Recommendation 23 Establish a common frame of reference for information flows between management companies and depositaries, with due consideration of the distinct characteristics of specialised investment strategies (private equity, real estate).

Recommendation 24 Launch an industry initiative on fund administration to facilitate the marketing of funds registered in Euroclear France in other countries.

Recommendation 25 Examine the possibility of allowing management companies that fall below the threshold to choose whether to require funds that are not yet regulated to have a depositary, while maintaining the possibility of converging on a single set of rules and ensuring investor protection.

Annex 1

Members of the AIFMD Stakeholders' Committee

Lead committee chaired by Monique Cohen and Jean-Luc Enguehard

- **Direction générale du Trésor**
Directorate General of the Treasury
- **Autorité de Contrôle Prudentiel (ACP)**
Prudential Supervision Authority
- **Direction de la législation fiscale Tax**
Legislation Directorate
- **Autorité des normes comptables**
Accounting Standards Authority
- **Association Française des Investisseurs Institutionnels (AF2i)**
French Association of Institutional Investors
Philippe Haudeville
- **Member of the Retail Investors Consultative Commission**
Jean Berthon
- **AFG**
French Asset Management Association
Paul-Henri de la Porte du Theil
Pierre Bollon
- **AFIC**
French Private Equity Association
Paul Perpère
France Vassaux d'Azemar de Fabregues
- **ASPIM**
French Association of Real Estate Funds
Patrick de Lataillade
Arnaud Dewachter
- **AFTI**
French Securities Industry Association
Karima Lachgar
- **FBF**
French Banking Federation
Jean Tricou
Jean-François Jondeau
- **Member of the Asset Management Consultative Commission**
Xavier Moreno
- **CMS Bureau Francis Lefebvre**
Jérôme Sutour
- **Paris Europlace**
Arnaud de Bresson

Group 1: Competitiveness

- **PAI Partners**
Blaise Duault
- **La Française AM**
Xavier Lépine
- **Quant Valley**
Arnaud Chrétien
- **Aviva Investors France**
Jean-François Boulier
- **Edrim**
Nicolas Dubourg/Emmanuel Courant
- **Allen & Overy**
Brice Henry
- **Rheinhold Partners**
Alain Rheinhold
Bertrand Gibeau
- **Member of the Retail Investors Consultative Commission**
Bernard Camblain
- **Members of the Asset Management Consultative Commission**
Etienne Stofer
Patrick Sellam
- **Direction générale du Trésor**
Directorate General of the Treasury
- **Autorité de Contrôle Prudentiel**
Prudential Supervision Authority
- **Direction de la législation fiscale**
Tax Legislation Directorate
- **Caisse d'Épargne d'Auvergne et du Limousin**
Claude Dupuy

Group 2: New Challenges

- **Amundi PE**
Corinne Ferriere
Bernard Arock
- **AEW Europe SGP**
Etienne Wagner
- **CIAM**
Frédérique Barnier-Bouchet
- **HDF Finance**
Christophe Jaubert / Christian Bartholin
- **BNP Paribas Investment Partners**
François Delooz
- **AXA IM**
Monique Diaz
- **Member of the Retail Investors Consultative Commission**
Jean Berthon
- **Member of the Asset Management Consultative Commission**
Bruno Prigent
- **Dechert**
Olivier Dumas
- **AGIRC**
Philippe Goubeault
- **Paris Europlace**
Arnaud de Bresson
- **Direction générale du Trésor**
Directorate General of the Treasury
- **Autorité de Contrôle Prudentiel**
Prudential Supervision Authority
- **Direction de la législation fiscale**
Tax Legislation Directorate

Group 3: Depositaries

- **Iris Capital**
Pierre de Fouquet
- **OFI Reim**
Brigitte Sagnes
- **Perial**
Eric Cosserat
- **Boussard & Gavaudan**
François Cornu
- **Amundi**
Frederic Bompaire
- **DNCA**
Philippe de Vecchi
- **CACEIS**
Anne Landier-Juglar
- **BPSS**
Anita Metzger
- **SGSS**
Michelle Besse
- **State Street**
Raphael Remond
- **Dexia**
Philippe Legrand
- **SJ Berwin**
Nathalie Duguay
- **Direction générale du Trésor**
Directorate General of the Treasury
- **Autorité de Contrôle Prudentiel**
Prudential Supervision Authority

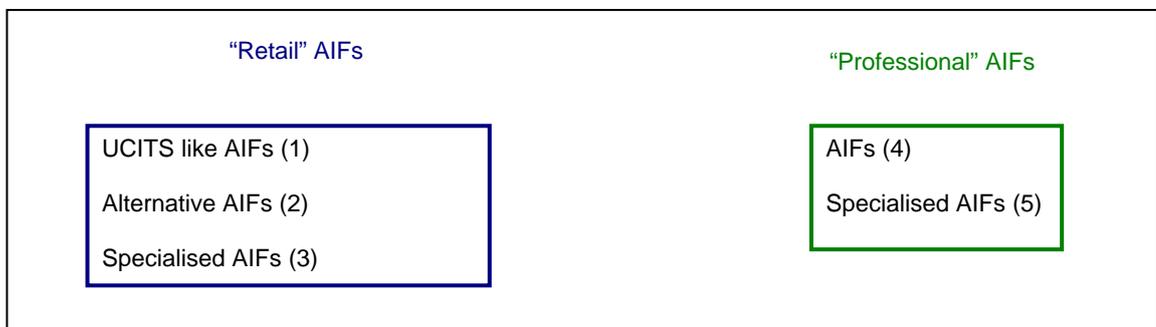
Group 4: Consistency of regulations

- **AXA Private Equity**
Karine Demonet
- **Viveris Reim**
Frédéric Bôl
- **Laffitte Gestion**
Arnaud Yvinec
- **Natixis AM**
Jean-Christophe Morandea
- **Ecofi Investissements**
Christophe Couturier
- **Member of the Investors
Consultative Commission**
Bernard Coupez
- **Gide Loyrette Nouel**
Stéphane Puel
- **Direction générale du Trésor**
Directorate General of the Treasury
- **Autorité de Contrôle Prudentiel**
Prudential Supervision Authority

Annex 2

Option considered to rationalise the range of products
that could be classified as AIFs within the meaning of the AIFM Directive

AIFs



"Retail" Alternative Investment Funds:

- (1) UCITS-like funds
- (2) Alternative "ARIA" funds (ARIA III)
- (3) Real-estate investment funds (OPCI), unleveraged real-estate investment funds with streamlined investment rules (OPCI RFA SEL)/real-estate investment companies (SCPI), venture capital funds (FCPR), forestry investment companies (SEF), closed-end investment companies (SICAF), etc.

"Professional" Alternative Investment Funds:

- (4) Leveraged authorised funds with streamlined investment rules (ARIA funds) and closed-end investment companies (SICAF)
- (5) Leveraged real-estate investment funds with streamlined investment rules (OCPI RFA EL), registered venture capital funds ("FCPR contractuel"), venture capital funds with streamlined investment rules ("FCPR procédure allégée")