**Alt\_Investment**

**ID:** 104 **Code:** COM (2009) 207 **Type:** Directive **Proposal** **Date:** 15.6.09  **Status:** Agreed 8.6.11

**Title:** Proposal for a Directive of the European Parliament and of the Council on Alternative Investment Fund Managers and amending Directives 2004/39/EC and 2009/…/EC

**Identified Commission Official:** DG Internal Market

**Objective:** This proposal is part of a wider programme to increase the level of regulation and supervision across financial markets. The key concern is that market failure in one sector can have severe consequences/risks for the entire financial system. The specific aim of this proposal is to impose harmonised requirements for entities engaged in the management and administration (this distinction is important as often these functions take place within different jurisdictions) of alternative investment funds (AIFM). Essentially these are all funds not otherwise defined as UCITS (Undertakings for Collective Investment in Transferable Securities), which are subject to a parallel directive. They include hedge funds and private equity funds, but also real estate and infrastructure funds.

**Background:** There had been a growing focus on the potential risks posed by alternative investments to both investors and the financial system as a whole. A focus of concern was the macro-prudential risks associated with leverage, which is a key feature of hedge funds. In December 2005 the Commission set up an expert group to ‘find ways to improve the efficiency of the EU investment fund market’. Here we have two reports from 2006 (see archive), which point towards the need for regulation in both the AIFM and UCITS sectors.

However, it seems that the financial crisis prompted a consensus for action, and to a significant extent redefined the nature and potential severity of the problem. The debate becomes sharply focussed on the role of AIFM’s in the crisis and the potential for this sector to cause a further crisis.

But throughout the debate, an important consideration/problem is that the nature and intensity of financial risk varies widely between business models within the AIFM sector. This is in contrast to UCITS, which is relatively cohesive. This has had the effect of creating a highly fragmented regulatory structure that is largely supervised under national regulation, with no EU regulation directly targeting AIFM. This situation posed particular challenges for policy makers, as there were significant variations between national regimes with regard to registration, authorisation, reporting, disclosure, and risk management. It seems likely that the further effect of the crisis was to make some of these differences easier to reconcile.

**Consultation:** The report implies that extensive consultation took place, with the details apparently available in the impact assessment. However, this document doesn’t seem to be available (strange). Not amongst the Institutional docs in dropbox or on Lexus. The 60 or so submissions that we have are from the 2006 period, which predates the crisis, and as such are not directly related to this proposal. However, it seems possible that these along with the 2005 consultation have been called upon to imply that a more relevant post crisis consultation has occurred. I think the explanation for this is that at the time of the proposal there was a real sense of urgency, which began to dissipate.

**Issues:** The issues are likely to focus on the relevance of regulation to specific types of funds, and the extent to which they should be regulated. In addition with functions within funds often split between regulatory regimes, often outside the EU, there will be issues of third party oversight. Likely issues: 1. should all business models be subject to regulation, ie all funds outside of UCITS; 2.Will the regime be open to all third parties (non-EU domiciled), through a passport system; 3. Strong or weak role for depositories.

**Frames:** Several options seem possible: 1. Shielding consumers and institutional investors from high risk; 2. Ensuring the stability of the financial system.