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IRISH FUNDS
INDUSTRY
ASSOCIATION

Submitted via email to:
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Consultation on types of alternative investment funds under AIFMD and unit trust schemes under the Unit Trusts Act 1990 (including EUTs, REITs etc.)

Consultation Paper 68

Dear Sir / Madam,

As the representative body for the international investment funds industry in Ireland the Irish Funds Industry Association ('IFIA') represents custodians, administrators, managers, transfer agents and professional advisory firms. As you are aware Ireland is a leading centre for alternative investment funds ('AIFs'), with EUR 286 billion of assets in Irish domiciled non-UCITS funds, across 2,189 funds and sub funds as of August 2013. Accordingly, all developments in the alternative investment arena are of particular importance to the Irish industry.

The IFIA welcomes both the publication of, and the opportunity to comment on, the Central Bank of Ireland's 'Consultation on types of alternative investment funds under AIFMD and unit trust schemes under the Unit Trusts Act 1990 (including EUTs, REITs etc.)'.

As a general point we are concerned with possible unintended consequences of capturing Exempt Unit Trusts ('EUTs') within the Alternative Investment Fund Managers Directive ('AIFMD') regime and note that there may be particular issues arising around the classification of the investors in or the investment strategy of existing EUTs which are likely to have been established without the consideration of complying with the AIFMD. As such, we request that should the Central Bank decide that EUTs should fall within the AIFMD regime that there be not only a sufficient notification and transitional period before this would become effective but that a grandfathering provision would also apply for any existing EUTs established prior to this effective date.

Below are our responses to the specific questions posed in the Consultation Paper and other general comments. All responses and questions refer to the numbering used in the Consultation Paper.

QUESTION 1: For consideration: Do you believe that our brief summary on the organisation of EUTs as set out above is correct?

For reasons set out below, we do not believe that exempt unit trust schemes would necessarily fall within the scope of the Unit Trusts Act 1990 as it effectively only applies to those offering participation to the public. Please refer to our response to question 3 below.

QUESTION 2: Do you agree with our analysis that an EUT is an AIF?

We do not agree that just because a structure is an EUT that it is automatically an AIF for the purposes of the AIFMD and related regulatory provisions. It may well be that a number of EUTs are in fact AIFs which fall within the scope of the AIFMD but a case by case analysis would need to be undertaken in respect of each EUT to determine if that was the case. This is consistent with the Central Bank's AIFMD Questions and Answers document (4th Edition – 30 September 2013) and in particular Question ID 1016 which recommends that appropriate legal advice is taken in respect of each investment structure.

Based on our analysis of a variety of possible EUT structures, some would be considered AIFs but equally some would not or may otherwise fall outside the scope of the AIFMD. We understand that other industry bodies will similarly highlight that not all EUTs are AIFs in their submission. We believe that the analysis in relation to REITs, special purpose vehicles and other entities such as limited partnerships under the 1907 Act would need to be made on a case by case basis.

QUESTION 3: Do you agree that an EUT is subject to the UT Act?

No, we do not believe that an investment vehicle that is limited to investment by Revenue approved pension funds and charities should be a unit trust scheme for the purpose of the UT Act. Such a scheme is defined as "an arrangement made for the purpose, or having the effect, of providing facilities for the participation by the public, as beneficiaries under a trust, in profits or income arising from the acquisition, holding, management or disposal of securities or any other property whatsoever" on the basis that excluding all investors other than those that do not jeopardise the EUTs tax status results in the EUT in question not being capable of participation by the public.

In addition, even if a contrary view were to be taken by the Central Bank in respect of EUTs in general, it would be incorrect to state that all EUTs would automatically be subject to the UT Act. Once again, a case by case analysis would be required as an EUT may have further limited its investor base such that by anyone's analysis, it was not providing facilities for participation by the public.

We are of the opinion that if you want to achieve a position whereby all EUTs will be subject to the UT Act merely as a consequence of being an EUT, this would require an amendment to the Unit Trusts Act 1990 as it is clear that, even if one accepted the Central Bank's proposition as set out in this Consultation Paper (that EUTs were generally covered by the UT Act), an EUT can be structured to fall outside the UT Act.

QUESTION 4: Is there any reason why the Central Bank should not apply the same regulatory regime to EUTs which are AIFs as any other AIF?

As noted in our response Question 3 above, we do not believe that EUTs should be deemed subject to the Unit Trust Act 1990 and therefore be regulated. The Central Bank's AIFMD Q&A acknowledges at ID 1043 that there may be Irish AIFs not subject to Irish domestic AIF regulation much in the same way that under AIFMD, an Irish AIFM is permitted to manage a non-Irish AIF which may be a regulated or unregulated structure and we submit that EUTs ought to come within this category of AIFs. Accordingly the only applicable regime to fall for consideration ought to be the AIFMD requirements.

Without prejudice to the views expressed above, we believe that if a regulatory regime is to be applied to EUTs, it is not appropriate to subject EUTs to the QIAIF / RIAIF regulatory regime and that it would be important to develop a set of distinct rules which would reflect the particular nature of EUTs as long-term investments and allows for the differing investment and liquidity requirements of their investor base. Any such regulatory regime that is introduced would need to be proportionate and be mindful of additional costs that would arise for investors in the EUT who have been operating in a lower cost environment of an unregulated fund with adequate protections already in place with regard to custody, investment management and administration. One would expect that the investor base of many EUTs is reasonably static (since the investors are traditionally long term investors such as pension schemes and charities). It is therefore difficult to see any real merit in forcing regulation on these vehicles and their investors when the only apparent result is an increase in costs.

As noted in paragraph 22 of the consultation paper, if it was determined that an EUT required to be authorised under the Unit Trust Act 1990, the Rulebook would require it to be established as either a RIAIF or a QIAIF. The consultation paper notes that, on the basis of available information it is unlikely that these long-term investors in EUTs will meet with the QIAIF investor criteria or minimum subscription requirement. We agree with this conclusion and note that the minimum initial subscription requirements in particular may exclude many individual pension schemes which are likely to have an initial contribution below €100,000 which will only build over time to an amount in excess of this requirement.

However, we also believe that it would not be an appropriate response to conclude that all EUT strategies must therefore be adapted to comply with the RIAIF regime. The investment strategies currently used by EUT structures have evolved over time to reflect the particular circumstances and requirements of investors. In many cases, portfolio composition will reflect the fact that the investment strategy is intended as a long-term investment and may form part of a larger investment portfolio. The long-term nature of EUT structures and the fact that in many cases the portfolio is designed with the requirements of an individual investor or a relatively small pool of investors in mind, have meant that many of the protections found in a RIAIF structure in terms of liquidity, concentration limits and leverage requirements are not as relevant in an EUT structure. Furthermore, the fact that a EUT may have a relatively small initial subscription with growth coming through future contributions will mean that an EUT is likely to require a longer 'ramp-up' period in terms of concentration limits than would be the case in a typical RIAIF. The consultation paper notes that the RIAIF restrictions on investment of more than 30% of the net asset value of a real estate fund in a single property and a limit on borrowing of more than 25% of net asset value may be significant in the context of regulation of an EUT. We agree that would be the case and that an obligation to comply with these provisions, and certain other provisions of the Rulebook in respect of RIAIFs would require a significant recasting of existing EUTs and inhibit the launch of similar products in the future.

Accordingly, in the event that it was determined to regulate EUTs under domestic Irish legislation, we believe that a separate regulatory regime applicable to these entities should

be set out in the AIF Rulebook. It may be possible to align this regulatory regime with the recent European Long Term Investment Fund ("**ELTIFs**") proposals issued by the Commission, which introduce a long term investment product required to have an authorised AIFM, provided the rules on eligible assets, diversification and borrowing as set out in the proposed regulation are appropriate in the context of EUTs. However, in designing such regime, it would also be important to engage in further consultation in order to take account of investment policies that promoters and investors are currently pursuing under existing EUTs.

QUESTION 5: What transitional arrangements do you consider should be applied?

In light of the substantial increased costs for pension fund investors arising from authorisation requirements applicable to AIFM and the obligation to appoint independent depositaries, we agree with the proposed transitional deadline of July 2015 in relation to compliance with the AIFMD obligations, in the event that they are deemed applicable.

In the event that the Central Bank determines that it is appropriate to regulate EUTs in future under domestic legislation, we submit that grandfathering and transitional provisions should be put in place in order to avoid the imposition of excessive costs on investors.

In particular, we believe that any EUT in existence before the application of the new regulatory regime, including the relevant Rulebook provisions outlined above, should be grandfathered indefinitely. For the reasons outlined above in relation to the long-term nature of EUT investments, we believe a significant number (and possibly the majority) of existing EUTs have investment policies which are incapable of being accommodated within the RIAIF regulatory regime. Given that the purpose of the RIAIF requirements is the protection of the interests of retail investors, we believe it would run counter to the interests of investors in those EUTs to require the forced disposition of assets acquired in good faith under the existing rules (particularly in circumstances where such assets may be illiquid or trading below acquisition cost). Similarly, any proposals which require the recasting or amendment of existing investment policy and other fund documentation will all ultimately impact on the final amount available to investors at the end of the investment cycle. Accordingly, we believe that it would be appropriate to grant a derogation from the RIAIF rules for all EUTs in existence as at the date of introduction of any new regime.

In the case of any EUT established after the effective date of any new regulatory regime, we believe that it would be appropriate that such entity should have at least five years to apply any applicable portfolio composition and diversification rules (similar to the provisions applicable to ELTIFs).

Please do not hesitate to contact me should any aspect of our comments require further clarification."

Yours sincerely,

Pat Lardner
Chief Executive
Irish Funds Industry Association