# Opinion of the European Economic and Social Committee on the 'Proposal for a Regulation of the European Parliament and of the Council on European Long-term Investment Funds'

*COM(2013) 462 final — 2013/0214 (COD)*

(2014/C 67/13)

Rapporteur: **Michael SMYTH**

On 4 July 2013 and 17 July 2013 the European Parliament and the Council respectively decided to consult the European Economic and Social Committee, under Articles 114 and 304 of the Treaty on the Functioning of the European Union, on the

*Proposal for a Regulation of the European Parliament and of the Council on European Long-term Investment Funds*

COM(2013) 462 final — 2013/0214 (COD).

The Section for Economic and Monetary Union and Economic and Social Cohesion, which was responsible for preparing the Committee's work on the subject, adopted its opinion on 4 October 2013.

At its 493rd plenary session, held on 16 and 17 October 2013 (meeting of 16 October 2013), the European Economic and Social Committee adopted the following opinion by 150 votes to 2 with 1 abstention.

## 1. Conclusions and recommendations

1.1 The EESC welcomes the proposed regulation from the Commission to establish a cross-border product framework for a long-term investment. The introduction of European Long-Term Investment Funds (ELTIF) will help to stimulate investor demand for important long-term assets.

1.2 The fact that ELTIF's can only be offered under the Alternative Investment Fund Managers Directive (AIFMD) and must invest at least 70 % of funds in eligible long-term projects such as physical and social infrastructures and SMEs should ensure the emergence of stable investment products.

1.3 The EESC accepts most of the Commission's analysis of the expected demand for ELTIF's and of the regulatory barriers currently inhibiting institutional and retail investment in new cross-border infrastructure projects. The proposed regulation has the potential to stimulate a meaningful single investment market in long-term projects.

1.4 The Commission's proposal to introduce closed-ended funds open to both institutional and retail investors is probably the best approach especially given the likely emergence of the secondary market in units or shares in ELTIF's.

1.5 As the proposed regulation breaks new ground in European investment markets, there is a need to carefully monitor its implementation. The EESC welcomes the proposal to monitor of the development of the ELTIF market. In the event of the initiative failing to develop a long-term cross-border investment market then further evaluation, assessment and reform would be undertaken to address the failings and to further enhance the attractiveness of ELTIF's.

## 2. Background to the proposed Regulation

2.1 On 26 June 2013, the EU Commission published a proposal for a Regulation on European Long-term Investment Funds (ELTIF) together with a lengthy impact assessment [1]. The Commission states that the main purpose of creating a cross-border fund vehicle of this nature is to increase the amount of non-bank finance available for companies in the EU requiring access to long-term capital for the purposes of projects relating to:

- infrastructure such as in the fields of transport, communications, energy or education;
- investments in unlisted companies, mainly SMEs;
- investments in real estate assets, such as buildings or direct purchase of an infrastructure asset;
- investments in social infrastructure, innovation infrastructure and climate protection.

[1] SWD(2013) 231 final.

2.2 The Commission's proposals are consistent with the approach taken in the Green Paper on long term financing of the European economy ([2]) which was approved by the EESC in July 2013 ([3]). As the title of the regulation suggests, the focus is on the stimulation and facilitation of greater volumes of long-term investment across Europe. There is a need to make such long-term investments more widely available and attractive to investors.

2.3 It is necessary to take action at European level because the Commission's research highlights anomalies, inconsistencies and fragmentation in the provision of long-term investment vehicles across the Union. Annex 2 of the accompanying impact assessment sets out in great detail these inconsistencies in long-term fund regimes in Germany, UK, France, Ireland, Netherlands, Italy and Luxembourg. According to the Commission there is no agreed set of cross-border standards for what long-term assets and investments are, for whom they may be suitable and for how they function.

2.4 The existing cross-border framework for investments – the Undertakings in Collective Investment in Transferable Securities (UCITS) – relates to portfolios of liquid transferable securities such as bonds and shares. The asset classes that are excluded from UCITS, namely long-term real assets such as infrastructure and property, are essential for ensuring sustainable growth. Long-term investment instruments are generally non-transferable and illiquid with no secondary markets available and often require substantial upfront capital commitments. These factors can deter even the largest institutional investors.

2.5 The Commission identifies three sets of risks commonly associated with long-term asset investments:

— the risk of misleading investors as to the nature of the risks of long-term assets;

— the risk associated with the illiquidity of long-term assets; and

— the risk that existing long-term funds lack sufficient expertise in asset selection, project monitoring and matching return profiles to potential client needs.

2.5.1 Mainly due to these risks, long-term investment funds have not had an entirely successful history to date. They have not always lived up to their planned performance and investors have been misled about expected returns and there is some evidence of fund mis-selling. The Commission recognises the need for appropriate due diligence in and professional management of such long-term investment funds. Great emphasis is placed in the regulation on the drawing up of appropriate information and marketing materials. Retail ELTIFs will be a packaged retail investment product and will need to have a Packaged Retail Investment Product Key Information Document (PRIP KID) for marketing to retail investors. Prominent and clear warnings will be needed for retail investors in relation to the closed-ended nature of the vehicle, its investment horizon and the absence of any early redemption rights.

2.6 The Commission estimates that there is between 1 500 and 2 000 billion euro of infrastructure project finance required in Europe up to 2020 and that this is evidence of the need for large-scale financing. The consultation exercise in drawing up the Commission's impact assessment gathered substantial evidence of an appetite among investors (both institutional and retail) for such an ELTIF.

## 3. **Key features of the proposal**

3.1 The upshot of all this has been sub-optimal development and performance of the market for long-term investment vehicles right across the EU. Specifically, it is claimed that funds are smaller than they might otherwise be; management costs are higher than they should be and retail investors have very restricted choice of funds across Member States. Action at European level is required to address the situation and the Commission therefore proposes to create a single market for long-term investment funds.

3.2 Seven policy options are identified on the basis of their capacity to address these operational objectives. These options range from maintaining the status quo, a voluntary product label and code, expanding UCITS to include some long-term assets, the launch of a long-term closed-ended investment product modelled on UCITS open to institutional investors only, the same product but opened up to high net worth individuals, a new fund with stronger investor protection regulations and no redemption rights, open to all investors including retail investors and finally the same fund but with redemption rights after an initial lock-in period.

3.3 Of these seven options, option six, namely a new European long-term investment fund (ELTIF) open to all investors without redemption rights is the preferred option. This option is similar to the existing models in those member states that allow investments of retail investors.

3.4 Under the Commission's proposals ELTIFs will operate within the Alternative Investment Fund Managers Directive (AIFMD) regime as a new category of authorised closed-ended fund. As the legislative framework for ELTIFs takes the form of a regulation of the European Parliament and of the Council, it will be directly applicable in all EU Member States without the need for further transposition. There are also various aspects of the regime where the European Securities and Markets Authority (ESMA) will produce regulatory technical standards.

([2]) COM(2013) 150 final/2.
([3]) OJ C 327, 12.11.2013; p. 11-14.

3.5 ELTIFs are intended for investment in long-term assets appropriate to the life cycle of the fund. The overall design and orientation of the structure will be towards long-term assets such as infrastructure projects. The Commission sets out rules around how the portfolio of an ELTIF can be invested. At least 70 % must be invested in long-term assets and not more than 30 % in assets eligible for investment by a UCITS. The 70 % limit relating to portfolio composition does not apply over the first 5 years of the ELTIF, during the lifetime of the ELTIF for 12 months if the scheme looks to raise new capital, and approaching the end of its life cycle, once it begins to sell assets in accordance with its redemption policy.

3.6 ELTIFs must be closed-ended with a fixed term. Investors will not be permitted to ask for redemption of their investment before the end of that fixed term. The length of the fixed term will be determined by the nature of the assets the ELTIF targets to acquire and hold. So there is a correlation with the investment horizon of the long-term assets to be acquired and the redemption horizon of the ELTIF. ESMA is to develop regulatory technical standards to further outline the circumstances around matching the life-cycle of the ELTIF with the life cycle of each of its individual assets.

3.7 Article 17 of the proposed Regulation envisages the emergence of a secondary market for units or shares in an ELTIF. This would provide liquidity to investors who might wish to redeem all or part of their holdings and as such it would not affect the underlying financing of the projects within the ELTIF itself.

3.8 ELTIFs will be investment products within the meaning of the Markets in Financial Instruments Directive (MiFID) and therefore subject to all the requirements of that directive in relation to marketing, selling and disclosure.

3.9 ELTIFs appear to be a positive development in terms of both the creation of a new product label and retail passport for the long-term asset/closed-ended sector and as a potential source of funding for unlisted EU companies. The Commission's assessment is that there is an appetite from managers and investors for such a product and it will be of interest to those in the infrastructure sectors in terms of an alternative financing source.

3.10 Given the groundbreaking nature of the proposed regulation, the issues of monitoring and evaluation take on even greater importance. The Commission recognises this and proposes to monitor the growth or otherwise in the market for ELTIFs over an initial period of perhaps four years. Key performance indicators such as the number of funds established that operate cross-border, the average size of ELTIF's, the views of investors and the relative proportions of funding according to infrastructure, property, SMEs etc. will enable an assessment of the success or otherwise of this initiative. In the event of the initiative failing to develop a long-term cross-border investment market then further evaluation, assessment and reform would be undertaken to address the failings and to further enhance the attractiveness of ELTIF's.

Brussels, 16 October 2013.

*The President*
*of the European Economic and Social Committee*
Henri MALOSSE