

The European Long-Term Investment Fund ("ELTIF") Regulation: A new European Label Success Story for Luxembourg?

Olivia Moessner

Counsel, Elvinger Hoss & Prussen

On 20 April 2015, the Council formally approved a regulation which was published in the Official Journal of the European Union (the "EU") on 19 May 2015 (the "Regulation")¹ aiming at increasing the pool of capital available for long-term financing in the European real economy by creating a new European investment fund vehicle available to retail investors but also appealing to other investors such as insurance companies or pension funds which need steady income streams or long-term capital growth. The ELTIF project was announced by the EU Commission back in October 2012 in the Single Market Act II communication and in the Green Paper on Long-Term Financing of the European Economy.

The idea of giving retail investors access to long-term investments was initiated in the UCITS² environment and more particularly in the so-called UCITS VI³ project which has since been aborted. In its UCITS VI Consultation, the EU Commission assessed the potential need for measures to promote long-term investments and the possible form of such measures.

In its UCITS VI Consultation, the EU Commission was seeking feedback on whether long-term investments could be part of the UCITS label or whether a brand new label should be created for that purpose. Access to retail investors through a passport would of course entail high standards of investor protection, as is already the case for UCITS.

Finally, with ELTIF it was decided to go the route of a brand new European label besides the successful UCITS label. Throughout this article, which analyses the main characteristics of the new ELTIF label, the reader will notice that ELTIF rules are, consequently, broadly inspired from UCITS rules.

TABLE OF CONTENT

1.	An New Alternative European Label Safely Regulated	3
2.	A Straightforward and Harmonised Authorisation Process	4
2.1.	Authorisation as an externally managed ELTIF	4
2.2.	Authorisation for internally managed ELTIFs	5
2.3.	Refusal of authorisation	5
2.4.	ELTIF register	5
3.	Investment Rules: a UCITS Inspiration for a Long-Term Investment Vehicle	5
3.1.	Authorised investments: A mix of eligible assets	5
3.2.	A non-speculative investment vehicle going beyond UCITS rules: prohibited investments and restriction on leverage	6
3.3.	UCITS-like risk diversification rules and investment restrictions	7
4.	Legal Structuring: Multiple Possibilities in Luxembourg?	7
4.1.	Legal forms	7
4.2.	Free distribution of proceeds and capital and issue of new units	8
5.	A Counterparty to Investment in Long-Term Assets: Limited Redemption Facilities and Pre-Determined Life-Time of the ELTIF	8
6.	High Transparency Standards	9
7.	ELTIFs: A Gateway to Alternative Investments for European Retail Investors	9
8.	Specific Provisions concerning ELTIFs Marketed to Retail Investors	10
9.	Will Luxembourg become the new hub for ELTIFs?	11

1. An New Alternative European Label Safely Regulated

An ELTIF is a "hybrid" concept lying somewhere between the AIFM⁴ and the UCITS worlds as it can invest in illiquid assets but also offers an EU passport to AIFMs for marketing to retail investors and is subject to stringent rules inspired by UCITS rules as mentioned above.

The ELTIF Regulation complements the European

1. Regulation (EU) 2015/760 of the European Parliament and of the Council of 29 April 2015 on European long-term investment funds.

2. UCITS is an acronym for "Undertaking for Collective Investments in Transferable Securities" within the meaning of Directive 2009/65/EC of the European Parliament and of the Council of 13 July 2009 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (the "UCITS Directive").

3. Consultation Document "UCITS, product rules, liquidity management, depositary, MMF, long-term investments", European Commission.

4. AIFM is an acronym for "Alternative Investment Fund Manager" within the meaning of Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011 on Alternative Investment Fund Managers and amending Directives 2003/41/EC and 2009/65/EC and Regulations (EC) No 1060/2009 and (EU) No 1095/2010 (the "AIFMD").

venture capital funds (EuVECA) and the European social entrepreneurship funds (EuSEF) which have been applicable throughout the EU since July 2013. Those labels have been established to facilitate capital-raising for start-ups and for companies which develop social business by introducing a European marketing passport for EuVECA and EuSEF managers.

The ELTIF label is exclusive. The designation "ELTIF" or "European long-term investment fund" in relation to an EU AIF⁵ or the units⁶ it issues may only be used where the EU AIF has been authorised in accordance with this Regulation. Also once the ELTIF label has been obtained, they are prohibited from transforming themselves into UCIs outside the sphere of ELTIFs.

ELTIFs will be subject to two-layer regulatory approval and two-layer supervision. Firstly, the AIF must be approved by its national competent authority as an ELTIF (internally managed or externally managed). Secondly, if the ELTIF is externally managed, the manager shall be a full-scope AIFM specifically authorised to manage the ELTIF.

Only EU managers authorised⁷ as AIFMs under the AIFMD may manage and market ELTIFs. Similarly, only EU AIFs can qualify for the ELTIF label. Therefore an ELTIF and its AIFM will need to comply with the AIFMD requirements (such as the appointment of a depositary).

As a result of the above and based on the EU mutual recognition principle, an AIFM based in Luxembourg or in another member state of the EU (a "Member State") may create a Luxembourg ELTIF and market it in several other Member States and potentially in jurisdictions outside the EU as is currently the case for UCITS.

2. A Straightforward and Harmonised Authorisation Process

An ELTIF may only be marketed in the Union once it has been authorised in accordance with the Regulation.⁸ In Luxembourg, the competent authority for delivering the ELTIF label to an AIF (regulated or non-regulated by a legislation on investment funds⁹), will be the *Commission de Surveillance du Secteur Financier* (CSSF). In addition, in that scenario, to the extent that the ELTIF is externally managed, the CSSF will also be competent to approve the EU AIFM specifically to manage the ELTIF.

2.1. Authorisation as an externally managed ELTIF

Firstly, the application for authorisation as an ELTIF filed with the CSSF shall include the following basic and easily available information¹⁰ and documentation regarding the Luxembourg AIF/ELTIF including (i) the ELTIF rules or instruments of incorporation (the "Constitutional Documents") (ii) information on the identity of the proposed manager of the ELTIF and its current and previous fund management experience and history (iii) information on the identity of the depositary and (iv) a description of the information to be made available to investors, including a description of the arrangements for dealing with complaints submitted by retail investors (if applicable).

The CSSF may request clarification and information as regards the documentation and information provided.

Secondly, the application will need to include information and documentation relating to the ELTIF's AIFM:

As mentioned above, only an EU authorised AIFM may apply to the CSSF for approval to manage a Luxembourg-based ELTIF. If the CSSF is also the competent authority of the EU AIFM, such an application for approval shall refer to the documentation submitted for authorisation under AIFMD. Otherwise, the application with the CSSF for approval of the AIFM to manage the ELTIF shall include certain information (i) the written agreement with the depositary (ii) information on delegation arrangements regarding portfolio and risk management and administration with regard to the ELTIF and (iii) information about the investment strategies, the risk profile and other characteristics of AIFs that the EU AIFM is authorised to manage.

To the extent both authorities are different, the CSSF as the competent authority of the ELTIF may ask the competent authority of the EU AIFM for clarification and information as regards the documentation filed or an attestation as to whether the ELTIF fall within the scope of the EU AIFM's authorisation to manage AIFs. The competent authority of the EU AIFM shall provide an answer within 10 working days from the date on which it received the request submitted by the CSSF.

Applicants shall be informed within two months from

5. AIF is an acronym for "Alternative Investment Fund" within the meaning of AIFMD.
6. When the term "unit" is used in this article, it refers to both units and shares of ELTIFs or other UCIs.
7. It may be a cause for regret, however, that AIFMs of AIFs below the threshold which may market AIFs qualifying as EuVECA or EuSEF will not be able to manage and market ELTIFs.

8. Article 3 of the Regulation.
9. As in accordance with Article 1 of the Regulation, the Regulation is applicable to any EU AIF, the author has taken the view that (as no gold plating is allowed) a Luxembourg AIF could be labelled as ELTIF when created under a Luxembourg regulated fund regime but also where it is non-regulated.
10. Article 5 of the Regulation.

the date of submission of a complete application with the CSSF whether authorisation as an ELTIF, including approval for the EU AIFM to manage the ELTIF, has been granted.

Any subsequent changes to the documentation referred to above shall be immediately notified to the CSSF.

2.2. Authorisation for internally managed ELTIFs

An EU AIF the legal form of which permits internal management and the governing body of which chooses not to appoint an external AIFM shall apply simultaneously for authorisation as an ELTIF under this Regulation and as an AIFM under AIFMD.¹¹

Without prejudice to Article 7 of AIFMD, the application for authorisation as an internally managed ELTIF shall include the following: (i) its Constitutional Documents and (ii) a description of the information to be made available to investors, including a description of the arrangements for dealing with complaints submitted by retail investors, if applicable.

An internally managed EU AIF shall be informed within three months from the date of submission of a complete application whether authorisation as an ELTIF has been granted.

2.3. Refusal of authorisation

The CSSF may refuse to approve the application of an EU AIFM to manage an ELTIF only where the EU AIFM¹² (i) does not comply with this Regulation, (ii) does not comply with AIFMD (iii) is not authorised by its competent authority to manage AIFs that follow the ELTIF's investment strategies; or (iv) has not provided the relevant information, clarification and/or documentation referred to above.

Before refusing an authorisation of the ELTIF label the CSSF should consult the competent authority of the EU AIFM (if different).

2.4. ELTIF register

The CSSF as the competent authority to authorise ELTIFs shall, on a quarterly basis, inform ESMA of authorisations granted or withdrawn pursuant to the

Regulation. ESMA will maintain a central public register (available in electronic format) identifying each ELTIF authorised under the Regulation, the manager of the ELTIF and the competent authority of the ELTIF.¹³

3. Investment Rules: a UCITS Inspiration for a Long-Term Investment Vehicle

3.1. Authorised investments: A mix of eligible assets

3.1.1. Eligible investment assets

At least 70 % of the ELTIF's capital¹⁴ has to be invested in "eligible investment assets" although ELTIFs will have up to five years after their authorisation as ELTIF to reach this target or half the life of the ELTIF, whichever is the earlier.

The following are eligible investment assets:

- equity/quasi-equity instruments, debt instruments issued by a qualifying portfolio undertakings¹⁵;
- loans granted to qualifying portfolio undertakings not exceeding the life of the ELTIF under certain restrictive conditions;
- direct or indirect holdings of real assets with a value of at least EUR 10 million that generate an economic and social benefit. These assets include (i) infrastructure (ii);
- intellectual property (iii) vessels and aircraft, (iv) equipment and machinery and (v) others such as rolling stock or immovable property meeting certain criteria;
- units of ELTIFs, EuSEFs and EuVECAs which do not themselves invest more than 10 % of their capital in ELTIFs.

As long-term investments in projects, undertakings, and infrastructure in third countries can also bring capital to ELTIFs and thereby benefit the European economy¹⁶, the assets do not necessarily have to be European as originally envisaged in the draft Regulation (see footnote 15 above item (iii)).

3.1.2. Long-term investment only

There is no specific definition of "long-term" in the Regulation even though the recitals of the Regulation¹⁷

11. Article 5.5 of the Regulation.

12. Article 6.3 of the Regulation.

13. Article 3 of the Regulation.

14. As defined by Article 2 (1) of the Regulation "capital" means aggregate capital contributions and uncalled committed capital, calculated on the basis of amounts investable after deduction of all fees, charges and expenses that are directly or indirectly borne by investors. Usually, investment restrictions of investment funds are expressed as a percentage of their net assets.

15. A qualifying portfolio undertaking must fulfil certain criteria: among other things (i) it must not be a financial institution (ii) it must not be admitted to trading on a regulated market or on a multilateral trading facility except if

at the same time it has a market capitalisation of less than EUR 500 million (iii) it is established in a Member State or in a third country which is not a high-risk and non-cooperative jurisdiction identified by the financial task force and it has signed an agreement with the home Member State of the AIFM of the ELTIF and in Member States where the units or shares (hereafter referred to as "units") of the ELTIF are intended to be marketed to ensure that this third country fully complies with the standards of Article 26 of the OECD Model Tax Convention on Income and on Capital and ensures an effective exchange of information.

16. Recital 4 of the Regulation.

17. Recital 15 of the Regulation.

recognise that the economic cycle of the investment sought by ELTIFs is essentially of a long-term nature due to the high capital commitments and the length of time required producing return. However, as a result of the analysis of the EU Commission preparatory works, the EU Commission struggled to find a satisfactory definition and this probably explains why there is no definition in the final version of the Regulation.

In its staff working document¹⁸, the Commission tried to define it through a precise period of time stating that "*the definition of what constitutes a long-term asset is very broad, in general comprising all asset classes that generate steady cash returns over periods ranging from 10 to up to 50 years*". And then in its proposal¹⁹ the Commission finally notes that "*the mere fact that an asset is not traded on a regulated market will qualify it as a long-term asset*" giving up any concept of a time period.

In the recitals of the Regulation, it is provided that "*the definition of what constitutes a long-term investment is broad. Eligible investment assets are generally illiquid, require commitments for a certain period of time, and have an economic profile of a long-term nature*".²⁰ There is no reference at all of a time period.

The only reference to a time period that we can find in the Regulation to define this concept by deduction is related to the life of the ELTIF. The Regulation provides that where the life of an ELTIF that is offered to retail investors exceeds 10 years a clear written alert that the ELTIF product may not be suitable for retail investors that are unable to sustain such a long-term and illiquid commitment should be made.²¹ *A contrario* an ELTIF could be set up for fewer than 10 years.

3.1.3. "Ancillary" UCITS-eligible liquid assets

Up to 30 % of the capital of the ELTIF can be held in assets that would be eligible investments for a UCITS²² (with the exception of financial derivatives which can only be used for hedging purposes) but only as long as this is consistent with the ELTIF's long-term investment strategy.²³

3.2. A non-speculative investment vehicle going beyond UCITS rules: prohibited investments and restriction on leverage

To limit speculative activities, ELTIFs are prohibited from using various types of investment techniques, in particular those creating leverage. Hence, they cannot (i) enter into short selling, (ii) take direct and indirect exposure to commodities, (iii) enter into financial techniques and instruments (such as securities lending, securities borrowing or repurchase transactions) if they affect more than 10 % of the ELTIF's assets and (iv) use financial derivatives that do not serve the purpose of hedging risks inherent in other investments of the ELTIF.

ESMA has to specify the circumstances in which financial derivatives are considered as being used for hedging purposes. ESMA, in its Consultation Paper²⁴ is of the view that the general definitions of hedging mentioned in the IFRS Standard 9²⁵ and in the CESR guidelines on Risk Measurement and the Calculation of Global Exposure and Counterparty Risk for UCITS²⁶ might be considered as a basis for defining the circumstances where derivative contracts solely serve the purpose of hedging the risks inherent to the investments of the ELTIFs. In that context, it seems that the identified risks to be hedged for an ELTIF are mainly fluctuation of interest rates, inflation rates, foreign exchange rates or credit risk.

However, the broad range of assets that might fall within the scope of the eligible investment assets of an ELTIF, including physical assets of the ELTIF Regulation, must be taken into account and ESMA concludes that consequently the scope of those risks is difficult to assess and to limit *ex-ante* and should be as broad as under the approach of IFRS.

Borrowing of cash above 30 % of the value of the capital of the ELTIF is also prohibited.²⁷ In addition, it shall (i) be limited to the purpose of acquiring eligible investment assets (ii) be denominated in the same currency as the acquired eligible investment assets (iii) have a maturity which does not exceed the life of the ELTIF and (iv) be adequately disclosed as part of the ELTIF's investment strategy. This restriction regarding borrowing may be difficult to comply with for certain ELTIFs like those investing in infrastructure as infrastructure investments are generally debt inten-

18. Ref. SWD (2013) 230 final.

19. Ref. COM (2013) 462.

20. Recital 15 of the Regulation.

21. Recital 28 (2) of the Regulation.

22. Articles 9 and 13 of the Regulation.

23. Recital 16 of the Regulation.

24. Consultation Paper, Draft Regulatory technical standards under the ELTIF Regulation, 31 July 2015/ESMA/2015/1239, ESMA. In accordance with some provisions of the ELTIF Regulation, ESMA must develop its technical standards, after its consultation, on several aspects of the Regulation such as (i)

use of financial derivatives for hedging purposes, (ii) redemption policy and life of ELTIFs, (iii) disposal of assets, (iv) cost disclosure and (v) facilities available to investors. ESMA shall submit its technical standards to the European Commission by 9 September 2015.

25. International Financial Reporting Standard (IFRS) 9 Financial Instruments (July 2014, as well as IFRS adopted in accordance with Article 3 of Regulation (EC) No 1606/2002).

26. Guidelines on Risk Measurement and the Calculation of Global Exposure and Counterparty Risk for UCITS, CESR, 28 July 2010/CESR/10-788.

27. Article 14 of the Regulation.

sive (70 % to 90 % of project financing).²⁸

3.3. UCITS-like risk diversification rules and investment restrictions

3.3.1. Diversification rules

Stringent diversification rules are applicable to ELTIFs which are similar to UCITS rules in order to limit risk-taking by ELTIFs. Similarly to UCITS with the so-called 5-10-40 rule²⁹, ELTIFs shall not invest more than 10 % of their capital in instruments issued by or loans granted to any single qualifying portfolio undertaking or in a single real asset, provided such limits may be raised to 20 % where the aggregate value of such assets in which it invests more than 10 % of its capital does not exceed 40 % of the value of its capital.

In addition, the Regulation provides for a prohibition of ELTIF fund of funds. ELTIFs may invest in other ELTIFs, EuvECAs or EuSEFs only to the extent that those funds have not themselves invested more than 10 % of their capital in ELTIFs³⁰, they do not invest more than 10 % of their capital in any single ELTIF, EuvECAs or EuSEFs³¹ and the aggregate value of other ELTIFs, EuvECAs or EuSEFs in its portfolio does not exceed 20 % of its capital.³²

More strictly than UCITS rules³³, the aggregate exposure to a single counterparty that an ELTIF may have, as a result of OTC derivative transactions and repurchase and reverse repurchase agreement, shall not exceed 5 % of its capital. In addition, no more than 5 % of its capital may be invested in UCITS eligible assets issued by one single body³⁴ but this may be increased under certain conditions to 25 % of the ELTIF’s capital.

Where the diversification requirements are infringed and where the breach is beyond the ELTIF manager’s control, the manager shall, within an appropriate period of time, take the necessary measures to remedy the situation, taking into account the interests of the investors in the ELTIFs.

Tolerance for the risk diversification requirements is provided for in the Regulation which allows a suspension for a maximum of 12 months if the ELTIF raises additional capital or reduces its existing capital.

This risk diversification rules may be difficult to meet for certain types of funds like infrastructure funds which may usually have only two different infrastructure investments in their portfolios. This will require managers to re-think their infrastructure portfolios.

3.3.2. Concentration rules

An ELTIF may not acquire more than 25 % of the units of a single ELTIF, EuVECA or EuSEF. Regarding the ancillary UCITS eligible assets, they will be subject to the rules laid down in Article 56.2. of the UCITS Directive.

4. Legal Structuring: Multiple Possibilities in Luxembourg?

Luxembourg will offer a favorable environment for the creation of ELTIFs offering a great diversity in structuring and by exploiting the various combinations offered by the Regulation. Unlike in the UCITS environment, multiple legal forms and features will be available for ELTIFs.

4.1. Legal forms

According to the Regulation, ELTIFs may adopt any legal form available to an AIF as defined under AIFMD in its home jurisdiction. The Regulation allows the creation of stand-alone or umbrella ELTIFs³⁵ (one single legal entity) where there are several sub-funds (with segregated assets and liabilities) which may have different investment strategies or be restricted to certain investors. One single sub-fund of an umbrella AIF may also apply for the ELTIF label and co-exist with non-ELTIF sub-funds.

ELTIFs can have any of the legal forms available in Luxembourg for regulated or unregulated AIFs and may include (without limitation) corporations with fixed or variable capital (SICAV³⁶ or SICAF³⁷) or mutual funds (FCP³⁸), partnerships (SCS³⁹, SCA⁴⁰ or SCSp⁴¹).

Any vehicle regulated by Part II of the 2010 Law⁴² could apply to be granted the ELTIF label at the umbrella or sub-fund level and can be available to all retail investors subject to the ELTIF’s requirements.

28. Source, Guidelines Luxembourg Infrastructure Investment Vehicles, Alfi (Association Luxembourgeoise des Fonds d’Investissement).

29. Article 52.2 of the UCITS Directive.

30. Article 10 d) of the Regulation.

31. Article 13 1. c) of the Regulation.

32. Article 13 3. of the Regulation.

33. Article 52.1 of the UCITS Directive.

34. Whereas UCITS are subject to the 5-10-40 % rule.

35. Article 8 of the Regulation.

36. Means *société d’investissement à capital variable*, which is an investment company with variable share capital, i.e. the share capital is at all times equal

to its net asset value. The share capital of the SICAV is automatically increased or reduced upon issue or redemption of shares.

37. Means *société d’investissement à capital fixe*, which is an investment company with a fixed capital, which capital may only vary in accordance with legal requirements.

38. Means *fonds commun de placement*.

39. Means *société en commandite simple*.

40. Means *société en commandite par actions*.

41. Means *société en commandite spéciale*.

42. Part II of the Law of 17 December 2010 on undertakings for collective investment (which regulates non-UCITS retail funds).

The flexibility offered under the regime of specialised investment funds subject to the amended Law of 13 February 2007 on specialised investment funds (the "SIF Law"), whose base of eligible investors is restricted to certain sophisticated investors, can also be considered as a tailor-made product by those sponsors willing to develop their ELTIFs across the EU.

Provided that the capital risk element is complied with, the SICAR⁴³ (supervised investment company in capital risk) regime could be available.⁴⁴ As the Regulation provides that ELTIFs must be AIFs, one might consider that a securitisation vehicle qualifying as an AIF could also benefit from the ELTIF label.

The recent and successful Luxembourg Special Limited Partnership, the SLP (or *SCSp* as defined above), will certainly constitute a vehicle of choice for ELTIFs. The SLP is a partnership entered into by one or more general partner(s) (GP) with one or more limited partners (LPs) contributing a specific amount pursuant to the provisions of the limited partnership agreement (LPA). The SLP does not constitute a legal person separate from that of its partners and, an ELTIF may use the SLP under a regulated regime (the Part II of the 2010, the SICAR or the SIF Laws) or set up an SLP as a non-regulated entity. This structure offers a great amount of flexibility. It contains a few mandatory rules, including the keeping and content of a register of partners, the information to be published and other formalities regarding the SLP's assets. The other features can be determined in the LPA further to the agreement between the GP and the LPs. Maximum flexibility is thus given to organise the rules that will govern distributions, claw back, political rights or redemption of partnership interests.

The legal form of an ELTIF marketed to retail investors shall not lead to any further liability for the retail investor or require any additional commitments on behalf of such an investor, apart from the original capital commitment (see Additional requirements for marketing ELTIFs to retail investors).

4.2. Free distribution of proceeds and capital and issue of new units

ELTIFs may regularly distribute to their investors the proceeds generated by the assets contained in their portfolio which comprise proceeds that assets are regularly producing and capital appreciation realised after the disposal of assets.⁴⁵

An ELTIF can issue new units in accordance with its Constitutional Documents. If they are issued below the

net asset value they must be proposed to the current investors of the ELTIF in priority.

5. A Counterparty to Investment in Long-Term Assets: Limited Redemption Facilities and Pre-Determined Life-Time of the ELTIF

In accordance with the legal framework of ELTIFs, investors do not, in principle, have the freedom to request the redemption of their units before the end of the ELTIF's life.⁴⁶ The redemption of ELTIF's units is only possible during the liquidating phase of the ELTIF.

The Constitutional Documents must specify a date for the end of the life of the ELTIF. The Regulation does not prescribe the lifetime of the ELTIF which has to be determined by the ELTIF's manager provided that its life has to be consistent with its long-term nature and shall be sufficient in length to cover the life cycle of each of its individual assets, measured according to the illiquidity profile and economic life cycle of each asset and its investment objective.⁴⁷ Assets in which an ELTIF invests may have different maturity profiles. Whenever an ELTIF invests in assets that all have the same maturity profile, the life cycle of the ELTIF may be easily set with reference to the life cycle of these assets. However, in situations where an ELTIF invests in assets that have different maturity profiles, ESMA considers it is important to ensure that the life of an ELTIF is set in a manner that ensures that the assets with the longer maturity are appropriately taken into account. By the time an application for authorisation as an ELTIF is made, the life of the ELTIF has to be determined. While at the time of authorisation an ELTIF may not have defined the full range of assets in which it envisages investing, and the investment positions in which the ELTIF is invested during the course of its life may change, given the aforementioned requirements, ESMA considers that the assets which the ELTIF needs to look at when determining its life are those in which it envisages investing at the time of the submission of the application for authorisation. For any investments made at a later stage (i.e. after the length of the life of the ELTIF is set), the manager of the ELTIF should ensure that such investments do not have a residual life cycle that exceeds the residual time period before the end of the life of the ELTIF. However, it is important to note that the Constitutional Documents may provide for the right to extend temporarily the life of the ELTIF and the condition for exercising this right.

43. Means *société d'investissement en capital risque*.

44. The amended Law of 15 June 2004 on *société d'investissement en capital risqué*.

45. Article 21 of the Regulation.

46. Article 18 of the Regulation.

47. ESMA is developing in its Consultation Paper the draft regulatory technical standards specifying the circumstances in which the life of an ELTIF is considered sufficient to cover the life cycle of each of its individual assets.

The European Long-Term Investment Fund (“ELTIF”) Regulation

The Constitutional Documents and disclosures to investors shall lay down the procedures for the redemption of units and the disposal of assets and state clearly that redemptions to investors shall commence on the day following the date of the life of their ELTIF.

The ELTIF⁴⁸ has to adopt an itemised schedule for the orderly disposal of its assets in order to redeem its units after its end of life which shall be disclosed to the CSSF at the latest one year before the date of the end of life. Among other elements, this schedule needs to include, according to ESMA regarding "eligible investment assets" only, an assessment of the market for potential buyers. ESMA considers that in making this assessment there are a number of market risks to be taken into account such as the risk of illiquidity of the assets, the risks associated with legislative changes and the risk of deterioration of the economic situation.

In the context of the disposal of its "eligible investment assets"⁴⁹ an ELTIF should ensure that an *ad hoc* valuation is carried out in advance and no more than 6 months before the schedule for the orderly disposal is disclosed to the CSSF. If the 6-month condition is complied with a valuation in accordance with Article 19 of AIFMD is acceptable.

Therefore, the ELTIF would run for a limited period of time during which investors will not, in principle, have the right to redeem their holding.

However, by way of derogation and probably in view of marketing ELTIFs to retail investors, redemptions may be allowed before the end of the life of the ELTIF to the extent that the liquidity of the assets of the portfolio (i) is in line with the redemption policy and (ii) is adequately managed.

The redemption policy of the ELTIF must ensure that (i) the overall amount of redemptions within any given period is limited to a percentage of its UCITS-eligible assets and that (ii) investors are treated fairly and redemptions are granted on a pro rata basis if the total requests for redemption within any given period of time exceed the percentage of its UCITS-eligible assets.

Investors must always have the option to be repaid in cash.

Redemptions are not granted before the date on which

the diversification requirements start to apply (as set out above).

In order to allow ELTIFs to create liquidity on the secondary market, its Constitutional Documents cannot prevent units of an ELTIF from being admitted to trading on a regulated market or on a multilateral trading facility or prevent investors from freely transferring their units to third parties other than the manager of the ELTIF.⁵⁰ In the event that there is a material change in the value of an asset, the manager of the ELTIF must disclose this to investors in its periodical reports.

6. High Transparency Standards

A prospectus, which shall include all information necessary to enable investors to make an informed assessment regarding the proposed investment and the risks attached thereto, must be published by ELTIFs before they can market their units. This prospectus must contain the minimum listed information⁵¹ and in particular the information which must be disclosed by closed-ended funds in accordance with the Prospectus Directive⁵² and the information which must be disclosed under Article 23 of the AIFMD (if not already covered under the Prospectus Directive). In addition, ELTIFs must publish annual reports.

7. ELTIFs: A Gateway to Alternative Investments for European Retail Investors

ELTIFs may be marketed in the EU to professional investors, but also to retail investors (subject to specific requirements described in section "Specific provisions concerning ELTIFs marketed to retail investors" below) in compliance with Articles 31 and 32 of the AIFMD. The Regulation thus goes far beyond the fundraising scope of AIFMD.

Contrary to what is envisaged in the EuVECA or EuSEF Regulations which target retail investors committing an investment of at least EUR 100 000, ELTIFs are open broadly to retail investors with an entry ticket of at least EUR 10 000 in one or more ELTIF(s). The result of this requirement is that, when assessing the possibility for a retail investor to subscribe in an ELTIF, the AIFM or any distributor may need to take into account similar investments made by this retail

48. Article 21 of the Regulation.

49. ESMA Consultation Paper.

50. Article 19 of the Regulation.

51. Article 23, 24 and 25 of the Regulation include prescriptive disclosures to be inserted in the prospectus. In particular, Article 25 provides for a cost disclosure. ESMA in its consultation has given further guidelines based on the existing framework on costs disclosure under the UCITS Directive and ac-

knowledge that it may be necessary to re-assess these technical standards once the future technical shareholders on the PRIIPS Regulation have been finalised.

52. Directive 2003/71/EC on the prospectus to be published when securities are offered to the public or admitted to trading and amending Directive 2001/34/EC.

investor in other ELTIFs managed by their competitors.

However, if the financial instrument portfolio (as defined in the Regulation) of a potential retail investor does not exceed EUR 500 000 the AIFM or any distributor shall ensure that this investor does not invest an aggregate amount exceeding 10 % of that investor's financial instrument portfolio in ELTIFs. Retail investors are responsible for providing accurate information on their patrimonial situations.

If this new passport to retail investors in the sphere of long-term investments offers great opportunities to managers, these managers will need to become familiar with this vehicle which creates brand new rules regarding product management but also retail distributions.

We may expect retail investors' reluctance to block their assets in long-term investment vehicles in the absence of any tax incentive. We may, however, expect certain EU jurisdictions to create a favorable tax environment for investments in ELTIFs to support this project to channel the European savings to the real economy.

ELTIFs may also be viewed by many institutional investors as an attractive way to diversify their portfolios. The EU Commission anticipates that pension funds and insurance companies will invest in ELTIFs. Pension funds are expected to invest in ELTIFs as their long-term investments will potentially match long-term pension liabilities and provide diversification. However, special treatment should be given to ELTIFs to prevent regulatory capital requirements such as solvency II rules from deterring prudent capital.

In addition, ELTIFs will benefit potentially from European public financing. Firstly, they are conceived as investment vehicles through which the European Investment Bank (EIB) Group can channel its European infrastructure or SME financing. Secondly, in its Communication⁵³, the EU Commission recognises that ELTIFs may play a role in providing a complementary vehicle for delivering public or private/public investments in the real economy and consider that the European Fund for Strategic Investments may support private fund structures such as ELTIFs set up by private investors and National Promotional Banks.

8. Specific Provisions concerning ELTIFs Marketed to Retail Investors

ELTIFs marketed to retail investors will benefit from additional protection features and additional conditions are applicable to the AIFM and the depositaries which, amongst others, are the following:

- the AIFM shall put in place facilities available to investors for making subscriptions, repurchasing or redeeming units of the ELTIF and providing them with relevant information. This requirement is inspired by the similar provisions in Article 92 of the UCITS Directive. As a consequence, ESMA in its Consultation Paper suggests taking the existing practice under the UCITS Directive when developing the specifications on the facilities to investors under ELTIF⁵⁴;
- the AIFM may directly offer or place units of the ELTIF to retail investors only if it is authorised to provide discretionary management services (i.e. it has the so-called MIFID extension licence) in accordance with Article 6.4 of the AIFMD;
- retail investors are provided with appropriate investment advice from the AIFM (provided it has the extension licence mentioned above) or the distributor;
- the AIFM shall have performed a suitability test for each retail investor in accordance with the Regulation;
- a depositary compliant with Article 23.2. of UCITS Directive (as it will be amended by the so-called UCITS V Directive⁵⁵) must be appointed. It means *inter alia* that the depositary will not benefit from the liability discharge it has under AIFMD and will not be in a position to re-use the ELTIF assets;
- no right to re-use the ELTIF assets (e.g. transfer, pledge, sale or lending of assets) must be granted unless it is for the account and benefit of the ELTIF;
- the depositaries will have no right to discharge or limit their liability in the event of a loss of financial instruments held in custody by a third party or for all other losses in the event of negligent or intentional failure to fulfil their obligations;
- the legal form of ELTIFs should not lead to any further liability for the investors or require any additional commitments on behalf of such investors apart from the original capital commitment;
- retail investors benefit from a cancellation right during the subscription period and at least two weeks after the date of their subscription, without penalty;
- additional information will need to be given to re-

53. Communication from the Commission to the European Parliament, the Council, the European Central Bank, the European Economic and Social Committee, the Committee of the Regions and the European Investment Bank An Investment Plan for Europe /* Com/2014/0903 final */.

54. Based on the requirements existing at national level under the UCITS Directive, ESMA proposes to set out the following main requirements:

1) the ELTIF entity itself should act as a contact point for investors and facilitate the handling of any issues that retail investors have relating to the ELTIF;

2) the facilities should include the possibility to directly subscribe for the units or shares of the ELTIF and to make repurchase and redemption requests;

3) the facilities should ensure payments to retail investors, including in relation to any distribution of proceeds and capital;

4) the rules or instruments of incorporation of the ELTIF, its sales document and its latest annual reports should be made available to retail investors through the facilities.

55. The Directive 2014/91/EU amending the UCITS Directive.

tail investors and preferential treatment or specific economic benefits granted to investors or groups of investors are prohibited;

- AIFMs of ELTIFs must implement a complaint handling policy;
- a PRIPs⁵⁶-compliant KID will need to be issued;
- a clear written alert if the life of an ELTIF exceeds 10 years that the product may not be suitable for retail investors which are unable to sustain such a long-term and illiquid commitment.⁵⁷

Although the implementation of additional protection measures for retail investors is welcomed, the question arises whether these additional burdens will not prevent institutional and professional investors from investing together with retail investors in ELTIF structures, knowing that they have generally a limited appetite for being mixed with retail investors. However, as demonstrated above, ELTIF managers have the opportunity to create different sub-funds or share classes to gather investors according to their status, as is already the case in UCITS funds, for instance.

9. Will Luxembourg become the new hub for ELTIFs?

The Regulation will be directly applicable in all the Member States, including Luxembourg, on 9 Decem-

ber 2015 without the need for any implementing provisions⁵⁸. No gold-plating is allowed and Member States cannot add or remove any requirement in the Regulation.

In Luxembourg there are currently discussions on whether a law, decree, regulation or other type of publication should be put in place to position this new type of vehicle in the existing legal and regulatory UCL, AIFM and AIF framework. In the absence of a clear outcome for the time being, the CSSF has already published a new page on its website to host ELTIF-related information.

As ELTIFs may have any legal form available in their home jurisdiction and with Luxembourg positioning itself as one of the world's leading financial centres for investment funds and companies, the Regulation can be considered as a new opportunity for the further development of a new product label with a world-recognised brand, as Luxembourg has done over the past 27 years for UCITS funds.

The Regulation will permit Luxembourg to continue to develop its fast-growing private equity, venture capital, and infrastructure funds industry.

56. PRIPs is an acronym for “Packaged Retail Investment Product” in accordance with EU Regulation 1286/2014.

57. Article 28 (2) of the Regulation.

58. ESMA will also develop its technical standards, after its consultation released on 31 July 2015, on the various aspects described in this Article (i) use of financial derivatives for hedging purposes, (ii) redemption policy and life of ELTIFs, (iii) disposal of assets, (iv) cost disclosure and (v) facilities avail-

able to investors. Further developments may also stem from the Capital Market Union Green Paper published by the EU Commission on 18 February 2015 and the consultation on the Prospectus Directive published the same day, in which the EU Commission encourages measures to boost the development of ELTIFs and to assess the relevance of the information to be published in their prospectuses.