Via electronic submission: www.esma.europa.eu

Institutional Limited Partners Association

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8 January 2015

To European Securities and Markets Authority
103 Rue de Grenelle
75007 Paris
France

Response to the ESMA call for evidence on the AIFMD Passport and Third Country AIFMs

Dear Sir/Madam

The Institutional Limited Partners Association (ILPA) appreciates the opportunity to respond to the call for evidence issued by ESMA, on 7 November, on the functioning of the AIFMD Passport, the national private placement regimes and the question of the proposed extension of the Passport to third country Alterative Investment Fund Managers (AIFM) and non-EU Alternative Investment Funds (AIF).

ILPA is a global organization dedicated to the interests of institutional investors into private equity funds worldwide (known as Limited Partners). ILPA's membership comprises more than 3,000 investment professionals from 32 countries around the world across 316 organizations, ranging from insurance companies, pension funds, public sector funds, foundations and endowments, collectively representing more than €1 trillion in private equity assets under management globally. More than 15% of ILPA's member organizations are headquartered in Europe, including a number of well-known European pension plans, insurance companies and endowments across 11 countries. In addition, 17 of ILPA's non-EU member organizations operate European investment portfolios managed or advised by satellite offices in the EU.

ILPA supports the important work of its colleagues at the European Venture Capital and Private Equity Association (EVCA), in their role as the industry's interlocutor in Europe, representing both investors and fund managers, and ILPA shares many of the observations outlined in EVCA's response to this consultation. Through this submission, we seek to provide a supporting and complementary response, with a particular emphasis on the impact on investment opportunities for EU investors and the attractiveness of Europe for internationally active fund managers seeking to raise capital in Europe.

Our perspective is distinct, in that our observations reflect the views of those making investment decisions into private equity on behalf of the European pensions and other beneficiaries that the AIFMD is intended to protect, and who would benefit most from a globally diversified, high performing investment portfolio. We also take a global point of view: Limited Partners worldwide welcome the enhanced oversight and disclosure that comes with regulation of the private equity industry but believe that such regulation must be consistently applied and evenly enforced, and must strike a considered balance between investor and consumer protections and the commercially sensitive and valuable aspects of this asset class.

This response focuses on a number of initial observations about how we perceive investors have coped during these initial months of the transition to the new EU AIFMD regime, perceptions of how some member states have implemented rules locally in respect of national private placement conditions and our members' experiences with fund managers seeking to market their funds to our members in Europe. However, we believe that more time is needed to truly assess the AIFMD Passport regime and its functioning. While we note that the AIFMD Level 1 obliges ESMA to provide its opinion on the functioning of the Passport by 22 July 2015, the practical experience with the Passport regime has been limited due to delayed/incomplete transposition of the AIFMD. These observations are grounded in a survey of ILPA's members on specific elements of ESMA's call for evidence, select findings from which are summarized in the appendix.[1]

We conclude that ensuring the workability of the AIFM Directive for the industry and the attractiveness of the EU for non-EU AIFMs is key and should be the ultimate objective during this review. It is important to ensure that Europe is open and accessible to non-EU AIFMs and non-EU AIFs, allowing EU investors to have access to a wide range of investments to meet their long-term obligations. We also consider it crucial that EU investors can compete with their non-EU counterparts on a level-playing field.

ILPA welcomes ESMA's work evaluating the current marketing rules that apply to non-EU AIFMs seeking to market AIFs to EU investors, and we would be very pleased to elaborate on the views set out below, given the importance of this issue to our members. We look forward to the opportunity to play a constructive role in this process going forward and to discussing ILPA's submission in greater detail.

Kind regards,

Jennifer Choi

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[1] Survey of ILPA members conducted in December 2014, reflecting the input of 42 individual respondents across 35 investor organizations in Europe.

Executive Summary

- As background, ILPA's members seek to generate the maximum risk-adjusted return possible in order to fulfil their fiduciary obligations to their beneficiaries—pensioners, insurance savers, research or academic institutions, etc. Private equity as an asset class has been shown to consistently offer investors higher returns net of fees over the long-term than other investment options. According to the latest ILPA performance data, private equity globally produced net rates of return to Limited Partners of 13.17% over a ten-year horizon, compared with 7.42% and 8.99% from the MSCI Europe index and the S&P 500, respectively, over the same period.[2] Each year, from hundreds of possibilities, investors must select a small number of high performing private equity fund managers (irrespective of their location) to help them achieve their overall portfolio investment objectives. As private equity funds are closed-ended and privately offered, however, investor interest alone does not guarantee access—Limited Partners must be invited into these vehicles, fundraising for which is capped at a maximum amount within a delimited period of time.

- In our members' experiences, there can be significant dispersion in returns between the highest performing managers and their peers within the same asset class. Several European investors, particularly smaller institutions, report lower levels of access to top performing PE funds attributable to the functioning of the AIFMD Passport or the National Private Placement Regimes. This is a serious concern as our members rely on the performance available from investments into private equity to meet beneficiaries' or members' target returns, whether for retirement planning or meeting other liabilities as they fall due. This is even more important in a low interest rate, and potentially deflationary economic environment. ILPA's members are concerned that a poorly functioning Passport and National Private Placement Regimes **hinder investor access** to the highest performing managers available, thus resulting in **lower returns to EU investors** and a potentially **elevated risk profile due to unintended geographic concentration** within their portfolios.

- AIMFD implementation at the national level (and in some instances its lack of implementation) has in several areas added to **further fragmentation of the EU internal** market for private equity. In particular, variance around the **definition of marketing** has raised barriers to investment rather than facilitate capital flows. ILPA's members caution that the **uneven requirements that have manifested within the current AIFMD Passport regime should not be allowed to persist** if the Passport regime is extended to non-EU AIFMs.

- Our members' experiences with several National Private Placement Regimes have been on balance negative. **European investors have observed a decrease in marketing activity of non-EU AIFs.** Having multiple and different rules in place across the EU deters managers from seeking to raise capital from some markets, due to complexity and cost, especially for markets where there are comparatively fewer institutional investors. As a result, our European members believe that they are **missing out on good quality investment opportunities as well as valuable market intelligence** on other geographies and sectors, and smaller institutions and investors in smaller countries in particular are at a stark

[2] Sources: ILPA Private Markets Benchmark (All Funds) as of June 30, 2014, reflective of pooled end-to-end returns net of fees, expenses and carried interest; Cambridge Associates Modified Public Market Equivalent (mPME), which replicates private investment performance under public market conditions.

competitive disadvantage to their peers outside Europe. The complexity of the National Private Placement Regimes also causes some of our members to devote more time and personnel cost to proactively identifying and engaging non-EU AIFMs who are otherwise deterred from marketing in certain European countries. **In some instances, processing delays by national regulators have resulted in investors missing the window to invest with their preferred managers altogether**.

- Our members believe that a well-proportioned marketing Passport, introduced in an efficient, consistent and commercially sensitive manner, could increase the attractiveness of European capital and thereby increase investor choice by addressing the complexity and regulatory uncertainty impeding many non-EU AIFMs from approaching EU-based investors. This would ultimately benefit European pensioners and other beneficiaries by ensuring that their funds are being invested at the highest rate of return available globally. ILPA would also welcome a detailed evaluation of the degree to which a harmonised EU private placement regime could simplify fund raising in Europe, improving access for investors to a broader and better range of investment opportunities.

APPENDIX – Questions & Survey Results

The following responses reflect input collected anonymously in December 2014 from 42 individual investors across 35 investor organizations in Europe.

FUNCTIONING OF THE PASSPORT FOR EU AIFMS

Q1: Please describe your experience using the AIFMD Passport, indicating your home Member State, Number of funds marketed in other Member States (please provide a breakdown by host Member State), Number of funds managed in other Member States (please provide a breakdown by host Member State).

ILPA's members are institutional investors (known as Limited Partners) investing into private equity funds managed by AIFMs taking advantage of the Passport; they do not have direct experience with the Passport themselves but can comment on the Passport's impact on investor protections, competition and investor choice.

ILPA's membership comprises more than 316 organizations across 32 countries, with 15% of member organizations headquartered in 11 European countries and 17 non-EU member organizations operating European investments through satellite offices in the EU. Our members range from insurance companies, pension funds, public sector funds, foundations and endowments, collectively representing more than €1 trillion in private equity assets under management globally.

ILPA's European members invest broadly both within and beyond the EU and for many investors, non-EU markets comprise a meaningful portion of their private equity investments. Among European investors we surveyed, 88% indicated that 40% or more of the AIFMs they currently invest with are non-EU AIFMs. 77% of respondents claim they will invest at least 40% of their private equity capital into non-EU AIFMs in 2015, most of which will be either US-based or global funds that include exposure to the US and/or Asian markets.

A number of AIFs that invest in European companies are managed by non-EU AIFMs. Nearly all European investors we surveyed (93%) indicated that some portion of their non-EU AIFMs invest into Europe, with 64% of respondents estimating that at least 20% of their non-EU AIFMs are investing in European companies.

Q3: What is your overall experience of using the passport of the AIFMD? Please explain.

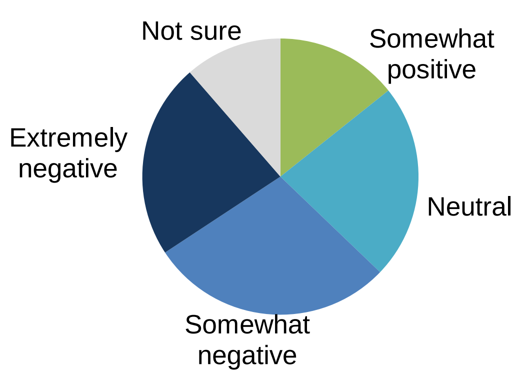
As institutional investors, ILPA's members do not have direct experience with using the marketing Passport but can comment on its impact on investor protections, which was among the intended objectives of the AIFMD. On balance, ILPA's members believe that the AIFMD Passport and the registration requirements associated with it have not resulted in enhanced investor protections. Among those surveyed, 52% of respondents believe that AIFMD registration requirements have in fact had a somewhat or very negative impact on European Limited Partners, due to uneven implementation of the AIFMD and the additional requirements posed by certain national regulators.

It is worth noting that members' views on the functioning of the Passport are preliminary, informed by limited experience in these initial months since the end of the AIFMD's transition period and their observations would benefit from more time and study of these issues:

> *"The regulation might make sense if fund managers were addressing retail investors, which is, however, not the case. We feel the regulation is restricting our access to top fund managers rather than providing us with any benefit."*

> *"[We] do not see any positive impact, only a potential delay in coming to market because of a lack of registration capacity by authorities."*

What impact have AIFMD registration requirements had on investor protections for European limited partners?



Q4: What difficulties have you encountered when trying to use the passport?

As ILPA represents institutional investors who do not themselves use the Passport, we refer ESMA to the more detailed responses to this question provided in the submissions of EVCA and individual AIFMs.

FUNCTIONING OF THE NATIONAL PRIVATE PLACEMENT REGIMES

Q7: Please describe the activity of your organization in the EU, identifying whether your organisation operates under Articles 36 or 42 of the AIFMD.

ILPA's members are institutional investors and therefore do not market or manage AIFs.

Q15: What have been the benefits of the National Private Placement Regimes (NPPR) to you?

As indicated in Q1, ILPA's European members invest globally and non-EU markets comprise a meaningful portion of the private equity investments of many European investors. Among European investors we surveyed, 88% indicated that 40% or more of the AIFMs they currently invest with are non-EU AIFMs. 77% of respondents claim they will invest at least 40% of their private equity capital into non-EU AIFMs in 2015, most of which will be either US-based or global funds that include exposure to the US and/or Asian markets.

Since the end of the transition period of the AIFMD, the continued availability of the National Private Placement Regimes for non-EU AIFMs without access to the Passport has been an important, and often EU investors' only channel for information about investment opportunities beyond Europe, particularly when an investor has no pre-existing relationship or awareness of the non-EU AIFM. Investors' ability to access these opportunities is critical to their ability to select best in class managers that will help them achieve their overall investment objectives and fulfil their fiduciary obligations to their ultimate beneficiaries, i.e., pensioners, savers, research and academic institutions, etc.

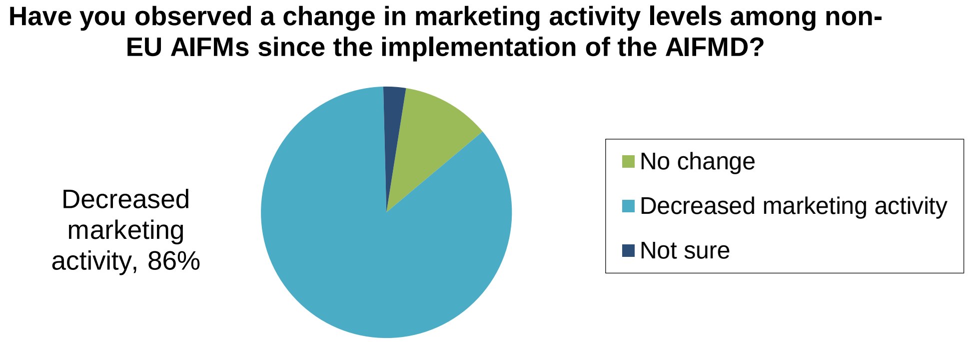
Q16: What have been the obstacles or barriers to entry of the NPPR to you?

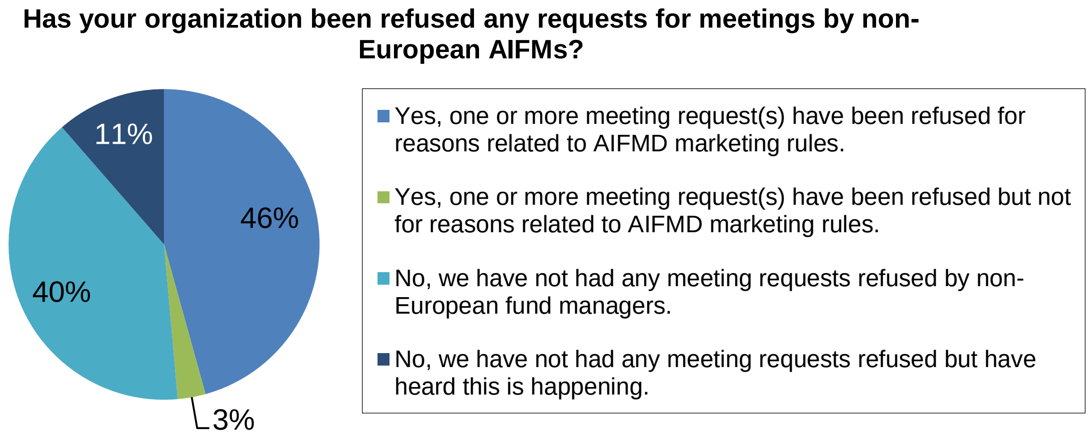
National Private Placement Regimes have been an important mechanism for preserving investors' access to non-EU opportunities but are generally viewed as having changed for the worse since the implementation of the AIFMD. Non-EU AIFMs are reportedly deterred from marketing in certain countries due to registration requirements or costs perceived as excessively onerous relative to the pool of investor capital available, resulting in decreased investor access to potentially attractive investment opportunities. Among ILPA members surveyed, 52% report that changes to national private placement regimes have been somewhat or very negative. Additionally, the introduction of additional processing time has been the source of delays that have hurt investors' ability to secure preferential fee discounts or to invest in their top choice AIFMs.

> *"[Local rules and requirements have] prevented us from participating in the first close of the fund and thus [we] lost some early bird discounts because of the slow processing by the regulator."*

The majority (86%) of European investors surveyed report that marketing activity among non-EU AIFMs has decreased since the implementation of the AIFMD. Many investors (46% of respondents) also report that efforts to initiate contact with non-EU AIFMs have been rebuffed due to compliance concerns.

"[High performing] non-EU AIFMs are oversubscribed already. They do not need EU money that comes with burdensome compliance and corresponding costs."



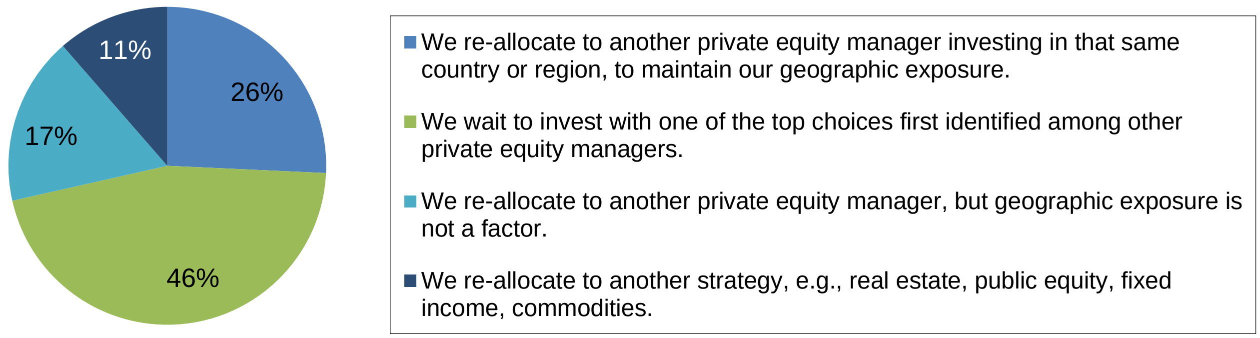


When unable to invest into their top choice of AIFMs, European investors most often prefer to wait until one of their first choice AIFMs becomes available (46% of respondents). European investors confronted by narrowed manager choice are being forced to rethink how to achieve the diversification necessary to meet their investment objectives, as increased allocations within Europe may pose geographic concentration risk that is sub-optimal for the overall portfolio.

"As a France-based LP, AIFM has been extremely negative for our investment program as it makes contact very difficult with non-French GPs (US but also Europe); it forces to make use of various techniques to adjust, probably not in the intent of the initial legislation."

"It forces us to allocate more to Europe, which is definitely not in the interest of the pension savers."

If you are unable to invest with your top choices among private equity managers, how will your organization proceed?



Investors also report that the diversity and quality of AIFMs from which they can choose has diminished. While large, well-established AIFMs have the infrastructure to either apply for a Passport, or register across multiple national private placement regimes, smaller niche players offering sometimes very compelling investment strategies are less available to investors.

> *"The quality of the funds stays the same, we just need to do more work to be in contact with them. The risk of missing out on a good quality investment opportunity has increased a lot."*

> *"It is more challenging to find a large enough non-European group of managers to evaluate and after due diligence to invest with. The risk is that you miss someone interesting because it is more difficult for them to contact a European investor."*

Q17: What obstacles did you encounter when trying to register through the NPPR?

We refer EMSA to the specific points raised by EVCA and others on the obstacles encountered by AIFMs seeking to register through the different National Private Placement Regimes related to the cost, time and complexity resulting from divergence in fees, informational and other requirements.

Worth noting from an investor's perspective, delays in processing registrations may cause EU investors to miss the window to invest with a first choice manager altogether and the additional direct costs to AIFMs of compliance with national private placement regimes may ultimately be passed on to investors.

FUNCTIONING OF BOTH REGIMES

Q21: What is the possible impact of an eventual extension of the Passport to non-EU AIFMs on competition?

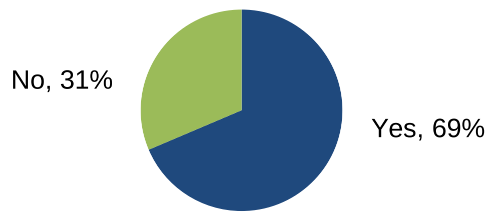
In principle, it is anticipated that the eventual extension of a Passport to non-EU AIFMs will be beneficial to competition. Decreased marketing activity among non-EU AIFMs due to the lack of a Passport has been damaging to European investors, who feel the sharp decrease in deal flow and the narrowed choice in managers puts them at a competitive disadvantage to their peers outside of Europe.

> *"Our investment program is facing a critical challenge; we used to have 400 to 500 opportunities per annum in deal flow, of which half were from non-EU GPs but now this has literally gone away."*

"Deal flow is reduced and access to information is significantly delayed, which has led us to be too late in the fundraising process and missing out on funds."

"Bigger [European] LPs can avoid this disadvantage by incorporating a subsidiary in USA but smaller [European] investors lack this opportunity."

Do you consider your PE program to be at a competitive disadvantage to your non-EU counterparts in terms of access to managers as a result of the AIFM Directive?



The availability of a Passport would benefit EU investors insofar as it results in a broader and better array of investment options. That said, should an extended Passport regime be disproportionately structured or unevenly applied, and should national private placement regimes be eliminated entirely, non-EU AIFMs targeting only a small number of European investors or countries will direct their marketing efforts to jurisdictions outside Europe where the compliance burden is commensurate with the pool of potential investors or capital available. This would undermine the very benefits to market efficiency, competition and investor choice that the introduction of a marketing passport for non-EU AIFMs should create.

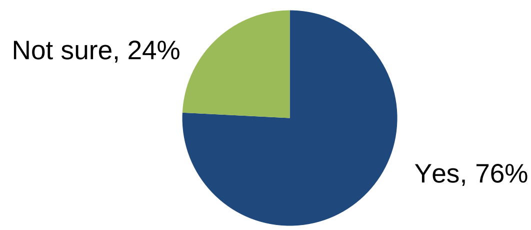
Q22: What are the risks of an eventual extension of the Passport to non-EU AIFMs in relation to market disruptions and investor protection?

ILPA's members do not anticipate that extending the Passport should pose any additional risks related to market disruptions or investor protections, as in many cases this would simply be a restoration of communication with managers that investors had identified as high quality prior to the implementation of the AIFMD. They do, however, caution that the uneven requirements that have manifested within the implementation of the AIFMD Passport regime should not be allowed to persist if the Passport regime is extended to non-EU AIFMs.

"European investors are best served by having a wider range of potential investment opportunities, as long as those AIFMs are properly vetted and the screening process is consistent across the EU."

"[There must be] a uniform application of the requirements under the AIFMD across all member states so as to prevent "forum shopping" and maintain the agreed level of requirements on AIFMs."

Should the European marketing passport under AIFMD be made available to non-EU AIFMs?



ILPA's members strongly favour the extension of the marketing Passport to non-EU AIFMs, provided such a regime is introduced in an efficient way and is constructed to be proportionate to the role that European investors play in the funding base for non-EU AIFMs, and is consistently applied. ILPA members also believe that the review process should be no more and no less stringent than for EEA AIFMs, as "*making the review too stringent for non-EU AIFMs will reduce the range of investment options available to EU-based investors*," thus negating the envisioned benefits of extending the Passport regime to non-EU AIFMs in the first instance. Many European investors believe that AIFMs that are already subject to robust regulation in their home markets, such as registration with the SEC in the United States, should be able to easily demonstrate their credentials to the satisfaction of European authorities.

We refer ESMA to the detailed analysis presented in the submissions by our colleagues at EVCA and others around some of the specific impediments to be addressed and issues to be considered in the event of the extension of the Passport regime.