ASPIM ASSOCIATION FRANÇAISE DES SOCIÉTÉS DE PLACEMENT IMMOBILIER

17 January 2022

Making ELTIFs a true European Label

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ASPIM's Comments and Proposals

ASPIM welcomes the European Commission's draft proposal released on 25 November 2021 for the revision of the European Long-Term Investment Fund (ELTIF) Regulation, in particular improvements relating to the creation of a liquidity window mechanism, the introduction of differentiated rules for retail and professional investors, as well as the extension of the scope of eligible assets and the enhanced supervisory rules.

In this paper, we summarise the relevance and unique ways in which real estate fund managers can support the future success of ELTIFs in Europe, then set out our concrete comments and suggestions to further improve the proposed framework.

HOW REAL ESTATE FUND MANAGERS CAN HELP MAKE ELTIF A TRUE EUROPEAN SUCCESS

It is estimated that the EU real estate sector employs around 4 million people in Europe and contributes around 3% to Europe's GDP - the equivalent to both the automotive and telecom sectors combined[1]. An important portion of such contribution comes from the real estate fund management sector[2].

The contribution of real estate fund managers is not just an economic one. Unlike other asset managers, real estate fund managers directly manage "real", long-term assets in which a broad range of economic activities are carried out (offices, shops, maternity clinics, student and retirement homes, hotels, hospitals etc.). As such:

- They host a significant ecosystem of both small and large companies as well as of public-sector buildings which is relieved from administrative and other burdens (e.g. energy efficient renovations, adaptations etc.), so that it can focus on core business or public duties.

[1] Source/ Eurostats, EPRA/InRev data

[2] Around 40% of the EU real estate sector is held as an investment, of which unlisted real estate funds are the largest providers (Source/ Eurostats, EPRA/InRev data)

- They can have a very concrete positive impact on the transition towards more socially and environmentally responsible investing.

In doing so, real estate fund managers are rightly subject to a wide range of property, energy and financial services regulations, providing investors with a robust environment in which to generate higher than average returns for the long term.

Therefore, real estate fund managers are uniquely positioned to support one of the political goals underpinning the ELTIF review to better allocate private savings and capital into a more sustainable economy - and this in two ways:

- By providing a stable, long term alternative source of diversification from bank deposits - helping turn savers into investors, a crucial piece of the Capital Markets Union project.
- By enabling income derived from such investments to complement shrinking state supported pension systems - an additional source of retirement income.
- By proactively helping a sector that is the biggest energy consumer and third largest producer of CO_2 emissions transition towards the Paris Agreement climate change targets.

The COVID 19 crisis has tested the resiliency of the real estate funds sector. Yet, little is known about its robustness and potential, and the current EU regulatory framework is not conducive to its development at a time where real estate investing is taking place on an increasingly cross-border basis.

We believe that an improved ELTIF framework that recognises the important role real estate fund managers can play in the better allocation of savings and long-term investments in capital markets is a necessary complement to the highly successful EU UCITS label for traditional funds managing securities portfolios. ELTIF must become the natural home for diverse forms of patient investments, be they infrastructure, private equity or real estate.

ASPIM'S MAIN COMMENTS AND RECOMMENDATIONS

We believe there are 5 key structural barriers that have limited the use of ELTIFs and are very encouraged to see that the Commission is addressing most of them.

1. Differentiated rule for professional and retail investors

We fully support the differentiation introduced regarding the changes to the leverage, namely a maximum of 50% of the value of a retail fund versus 100% for a professional fund (Article16).

The distinction based on investor profile allows for a better adjustment of leverage depending on the level of risk that the investor will accept, and better protection for retail investors.

ASPIM Recommendations

However, the calculation should be based on the average of the entire portfolio, i.e. an LTV (Loan to Value) ratio, and not on the totality of the assets. The LTV ratio is the risk ratio used for Closed-ended real estate funds (eg SCPIs in France – *Sociétés Civiles de Placement Immobilier*) and Open-ended funds (eg. OPCIs in France – *Organismes de Placement Collectif* *en Immobilier*): it is the ratio between the fund's debt and the market value of its real estate assets.

2. Uniform rules for different types of investors

We welcome the many adjustments made to unify certain rules for investors, namely:

- **Lowering of the investment quota** to 60% (instead of 70%) (Art. 13, §1 as amended) - which is also in line with that used for many Open-ended funds (such as OPCIs in France)
- **Revision to the risk dispersion ratio** to a maximum of 20% of the fund per asset (Article 13, §2 as amended);
- **Deletion of the entry ticket** of €10,000 and the maximum 10% threshold if the retail investor's financial portfolio is less than €500,000 (Art. 30 amended by deletion of §3);
- **alignment of the suitability assessment with MiFID rules** to improve retail investors' access to ELTIFs (Article 30, §1 as amended);
- **facilitation of "fund of funds" investment strategies** through the possibility to invest in AIFs, ELTIFs, EuVECAs and EuSEFs, provided they invest in eligible assets (Art. 10, §1, d);
- **authorisation of co-investments** and in-house funds provided that adequate safeguards are in place to prevent and disclose any potential conflicts (amended Art. 12, §1 and §2).

These adjustments are real improvements which should be preserved in order to make ELTIFs more attractive to both retail and professional investors, and provide added necessary flexibility for portfolio managers.

3. Possibility of setting up redemptions before the end of the fund's life

We also welcome the possibility of setting up a **"liquidity window mechanism"** through the compensation of redemptions with new subscriptions (Art. 19).

Restrictions in the original ELTIF locked in investors for the entire duration of the ELTIF's. This could work for private equity funds which typically have a 3 to 5-year horizon. However, for real estate (as well as most infrastructure) funds comprising underlying real assets with a much more longer-term profile, it is essential to provide managers with equally longer-term liquidity management tools that recognize investors' potential needs for earlier redemption – keeping the fund closed-end, but giving investors reassurance that there is a carefully tailored liquidity mechanism in place to allow for a phased redemption process if need be.

By way of concrete example, under the new ELTIF rules as proposed, real estate fund managers would very usefully be able:

- During the ramp-up period, to honour redemptions via a "compensated withdrawal" mechanism (as is the case for open-ended SCPIs in France), or via a "deferred compensation" mechanism (compensating withdrawal requests made by fund holders with subscriptions made by "incoming" investors in previous months);

- then, during the period in which the risk diversification quotas are reached, to ensure liquidity through a redemption of units (leading to a reduction in the fund's assets within the 60% quota).

ASPIM Recommendations

- This additional flexibility **should be maintained**: for real estate (and infrastructure) funds, the possibility of offering these "evergreen" structures that match the much more longer-term profile of the underlying property asset is paramount, coupled with specific long-term liquidity management rules and tools that recognize investors' potential needs for earlier redemption.

- It would further **align the ELTIF liquidity management toolbox with that in the AIFMD** proposal, which is also welcome.

- Finally, the proposed establishment of a **secondary market liquidity mechanism** is also welcome - as is the case for the French, which functions very well. It is important that the mechanism adopted is suited to the inherently illiquid nature of real estate and infrastructure assets and not forced onto existing regulated market models.

4. Conditionality attached to qualifying as "eligible asset" and "real asset"

We welcome the recognition in Recital 7 that real estate such as commercial property, housing (senior residences and social housing) and public building infrastructure (eg schools, hospitals and prisons) should be deemed "eligible assets".

We further welcome the clarification by the Commission in its explanatory notes (para 1 on page 8) that changes to the definition of "real asset" in Article 2.6 also comprises investments in real estate assets listed above.

However, it would appear that the eligibility of real estate (as well as other real assets) remains subject to "*the ability of these assets to contribute to smart, sustainable and inclusive growth objectives"* (Recital 7).

These very legitimate objectives are nevertheless somewhat vague and subjective, and risk being interpreted differently between fund managers and Member states.

ASPIM Recommendations

To remove the risk of inconsistent interpretation and therefore implementation of ELTIF which could prevent its development, we believe there should be a coordinated EU process to ensure that consistent and sector specific criteria are developed at European level, for example through level 2 measures.

For example, in the real estate fund management sector, an important criterion would be existing compliance with sufficiently robust public norms and/or ESG type labels that exist in the real estate sector and meet certain societal needs (eg job creation, housing provisioning)

5. Taxation:

A likely game changer to ensure the development of a truly cross-border market in ELTIFs distribution would be to create a certain level playing field across Europe in the tax treatment of income and/or dividends.

Without a harmonised tax regime at EU level, managers will be able to arbitrate to locate their funds in a Member State that limits tax impacts (double taxation).

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