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January 8, 2010

Via Email
Mr. Emil Paulis
Director, DG MARKT/G
Financial Services Policy & Financial Markets
European Commission
200 Rue de la Loi
B-1049 Brussels
emil.paulis@ec.europa.eu

Dear Mr. Paulis:

The Investment Company Institute[1] has followed closely the work of the Commission of the European Communities, the European Parliament, and the Swedish Presidency of the Council of the European Union on the proposed Directive on Alternative Investment Fund Managers (the "Directive").[2] We understand that the Spanish Presidency intends to make further progress on the Directive. We sympathize with and support these efforts to create a harmonized regime in the European Union ("EU") that will protect against the potential risks associated with certain types of alternative investment funds. Nonetheless, based on our review of the Directive in its original form and as proposed to be amended by the Swedish Presidency of the Council ("Swedish Presidency Draft") and

[1] The Investment Company Institute is the national association of US registered investment companies, including mutual funds, closed-end funds, exchange-traded funds (ETFs), and unit investment trusts (UITs). ICI seeks to encourage adherence to high ethical standards, promote public understanding, and otherwise advance the interests of funds, their shareholders, directors, and advisers. As of November 30, 2009, members of ICI managed total assets of $11.62 trillion and served almost 90 million shareholders.

[2] The text of the Directive on Alternative Investment Fund Managers issued by the Commission of the European Communities on April 30, 2009, is available at http://ec.europa.eu/internal_market/investment/docs/alternative_investments/fund_managers_proposal_en.pdf.

by the rapporteur of the Committee on Economic and Monetary Affairs, Jean-Paul Gauzés (the "Gauzés Draft Report),[3] we respectfully would urge a more tailored approach to meet this goal.[4] The current versions of the Directive are, in our view, unnecessarily broad. They will have significant, adverse and (we trust) unintended consequences for investors and investment managers alike – both in the EU and elsewhere. Our specific concerns include the following:

- The proposed Directive would preclude US investment companies registered under the Investment Company Act of 1940 and regulated by the US Securities and Exchange Commission (each, a "US RIC") from retaining an EU investment manager, to the detriment of US RICs and investors and EU managers.
- Contrary to sound and well-established global asset management practices, delegation of portfolio management to non-EU managers would be prohibited under the original form of the Directive and under the Gauzés Draft Report.
- Under the Gauzés Draft Report, sales of US RICs to EU investors under national law would require negotiated cooperation agreements among regulators, a process likely to be challenging and drawn-out, posing substantial disruption and adversely impacting investor access to US RICs and other non-EU funds.

We understand that other non-EU jurisdictions have similar concerns. To address these concerns, we respectfully suggest that the Directive be amended as follows:

- To exclude from the Directive's provisions non-EU funds that are neither marketed nor domiciled in the EU and that are subject to regulation in their own jurisdictions.
- To permit EU managers to delegate portfolio management of an alternative investment fund in a manner similar to that by which such functions are delegated under the UCITS Directive.

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[3] The Swedish Presidency Draft, dated December 15, 2009, is available at http://register.consilium.europa.eu/pdf/en/09/st17/st17330.en09.pdf. The Gauzés Draft Report, dated November 23, 2009, is available at http://www.europarleuropa.eu/sides/getDoc.do?pubRef=-//EP//NONSGML+COMPARL+PE-430.709+01+DOC+PDF+V0//EN&language=EN.

[4] The Institute sent a letter to the Commission and the Swedish Presidency on July 27, 2009, expressing its initial concerns with the Directive and proposing an exclusion of US RICs from the scope of the Directive, available at http://www.ici.org/pdf/23659.pdf.

- To permit Member States the continuing ability to prescribe the terms and conditions under which non-EU funds may be marketed and sold to professional investors in their own jurisdictions.

Appendix I sets forth these proposed amendments in further detail. We explain our concerns and the basis for our recommendations below.

1. *The Directive Should Permit US RICs to Retain EU Managers, to the Benefit of Investors and EU Managers Alike*

Under the proposed Directive, a US RIC would be considered an alternative investment fund ("AIF"). As a result, if a firm that is established in the EU provides investment management services to a US RIC, the Directive would apply to the manager's activities,[5] including its activities in connection with any other AIF that it manages. This presents a host of compliance and practical problems.

Certain provisions of the Directive are inconsistent or incompatible with well-established US regulations regarding, for example, custody, valuation, and shareholder disclosure and reports.[6] In some cases, the Directive would impose such divergent requirements as to be simply unworkable for US RICs.[7] The Gauzés Draft Report would make all of the provisions of the Directive applicable to all AIFs, including US RICs. As a result, it would no longer be possible for a US RIC to be managed by an EU AIFM, certainly not in a manner consistent with the Directive. We are aware that the Swedish Presidency Draft would relieve AIFs that are neither established nor marketed in the European

[5] A manager that is established in the European Community and manages an AIF, regardless whether the AIF is domiciled inside or outside of the European Community or sold to EU investors, would be considered a "manager of alternative investment funds" (an "AIFM") *See* Directive, Article 2; Gauzés Draft Report, Amendments 22 and 25; and Swedish Presidency Draft, Article 2 .

[6] *See, e.g.,* Directive, Article 17 (Depositary), Article 16 (Valuation), Article 19 (Annual Report), Article 20 (Disclosure to Investors), and Article 21 (Reporting Obligations to Competent Authorities) and analogous provisions in the Gauzés Draft Report and the Swedish Presidency Draft.

[7] For example, the provisions of Article 17 of the Directive regarding depositaries would be unworkable as US RICs do not employ an entity such as the depositary. Rather, US RICs have boards of directors/trustees that have overall responsibility for the management of the affairs of the fund, including the appointment of the fund's custodian, and custodians are appointed to safekeep a fund's assets. In addition, the Investment Company Act of 1940 also limits the entities that may serve as custodians to US RICs.

Community from complying with certain provisions of the Directive.[8] Nonetheless, under that Draft, other provisions of the Directive that would remain applicable to US RICs are incompatible with US rules. Accordingly, even under the Swedish Presidency Draft, an EU AIFM would be precluded from managing US RICs.

We hope that such a result is unintended. Certainly, it is not necessary and we respectfully submit that it will benefit neither investors nor the EU. As you know, investors today routinely seek to diversify their portfolios through exposure to securities markets in the US, EU and worldwide. Many investment managers have organized their businesses to assemble the expertise required to conduct such investment activity on behalf of their clients. To this end, many managers have established affiliates or other formal management relationships with advisers in the EU and elsewhere. These arrangements have served the interests of investors well. Regrettably, however, the proposed Directive would effectively preclude, or at a minimum significantly impede, non-EU investors gaining access to EU investment expertise. As discussed below, it will have a similar impact on EU investors seeking to access the expertise available in non-EU markets.

The implications for US RICs and EU investment advisers are not trivial. As of September 30, 2009, more than twelve percent of the assets of US mutual funds ($1.297 trillion out of $10.717 trillion) and more than two-thirds of the assets of US exchange-traded funds ($349.95 billion out of $515.13 billion) were advised by investment advisers that have a European parent entity.[9] Understandably, therefore, the potential adverse impact of the Directive is of utmost concern to US RICs, to their investors and to their EU managers. Our member funds are not alone, however. Other non-EU investment funds that fall under the definition of AIF may face similar obstacles to engaging or retaining EU managers.

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[8] *See* Swedish Presidency Draft, Article 2.1a, which provides that AIFM that manage AIF that are neither established nor marketed in the Community shall not be subject to Articles 17 (Depositary) and 19 (Annual Report) and Chapter VI (Rights of AIFM to Market and Manage AIF in the Community) in respect of those AIF.

[9] These figures are understated, in that they do not include US RIC assets that are sub-advised by investment managers with a European parent company. ICI does not track this information.

For all of these reasons, we respectfully recommend that any final Directive exclude from its coverage all funds that (1) are neither domiciled nor marketed in the EU and (2) are subject to regulation in their respective non-EU jurisdictions. Such exclusion would be consistent, we believe, with the stated objectives of the proposed Directive – *i.e.*, assuring appropriate regulation and oversight to entities that could pose significant risks.[10] In this regard, it is important to note that US RICs are comparable to the EU's UCITS, which the Directive expressly excludes from the definition of AIF. Like UCITS, US RICs are highly regulated investment vehicles. They disclose substantial information regarding their activities to regulators, investors and the market at large. The Investment Company Act of 1940 and other US securities laws impose stringent requirements on all US RICs. These requirements, which are designed to protect investors and mitigate risks, are in some respects even more detailed than those applicable to UCITS. They address, among other matters, custody, leverage, and transactions with affiliates, valuation, corporate governance, compliance policies and procedures, and the content of prospectuses, reports and other disclosure documents provided to prospective and current investors. We submit that US RICs simply do not raise the concerns about risk, lack of transparency and oversight that may well apply with respect to other investment funds that are less regulated or not regulated at all.

In addition, as you know, the US Securities and Exchange Commission ("SEC") has comprehensive authority to oversee, inspect and, if necessary, bring enforcement actions concerning the activities of US RICs. To enhance its oversight, the SEC has entered into formal memoranda of understanding with numerous foreign jurisdictions, including many EU Member States, concerning the exchange of information related to the enforcement of US and foreign securities laws.

In light of the comprehensive framework of regulation under which US RICs operate, we believe that excluding them and similarly regulated funds outside the EU would be fully consistent with the objectives of the Directive. It also would assure that US RICs and their investors continue to have access to EU managers and the unique expertise they offer.

2. *The Directive Should Permit Delegation of Portfolio Management to Non-EU Managers as Permitted under the UCITS Directive*

[10] *See* Proposal for a Directive of the European Parliament and of the Council on Alternative Investment Fund Managers (April 30, 2009), Explanatory Memorandum, page 2.

As noted above, in order to provide their clients with expertise in particular markets, investment managers often establish affiliates or formal relationships with other firms in various countries or regions around the world. Such arrangements serve investors' interests and also allow global managers to organize their businesses more effectively and efficiently. We are concerned that the Directive could call these legitimate and beneficial business arrangements into question. Under the Gauzés Draft Report, for example, the delegation of portfolio management is restricted to entities that are authorized as an AIFM.[11] Only EU entities, however, may be authorized as an AIFM. Accordingly, no AIFM would be permitted to engage any non-EU portfolio managers for the AIF they manage. The Swedish Presidency Draft, by contrast, allows the delegation of investment management functions in the same manner as permitted under the UCITS Directive.[12]

We support the Swedish Presidency Draft, which follows the well-established approach of the UCITS Directive. We respectfully urge that any final Directive allow an AIFM to delegate portfolio management functions in the same manner as is permitted under the UCITS Directive.[13] For many years, this approach has provided UCITS with appropriate flexibility to delegate investment management. For precisely these reasons that advisers to US RICs seek out EU investment management expertise, an AIFM should have the ability to access non-EU expertise. Denying them this flexibility, as it would appear the Gauzés Draft Report would do, will not benefit but rather harm EU investors.

3. *The Directive Should Preserve the National Private Placement Regimes for the Sale of Non-EU Funds*

We are concerned that the proposed Directive may have the practical effect of prohibiting EU investors under any circumstances from investing in US RICs. Under the Gauzés Draft Report, Member States may permit non-EU funds to be marketed under the respective Member State's national laws if: (1) the AIFM is established within the EU or (2) a cooperation agreement and an efficient exchange of all

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[11] *See* Gauzés Draft Report Amendment 84.

[12] *See* Swedish Presidency Draft, Article 18.

[13] In addition, since the MiFID provisions governing portfolio management outsourcing are similar to the UCITS Directive, adopting similar delegation provisions for the Directive would ensure consistency among these directives on the delegation of portfolio management, thereby reducing confusion and benefiting market participants.

relevant information for monitoring systemic risks exists between (i) the competent authorities of the Member State where the AIF is marketed and the non-EU competent authorities, (ii) the AIFM and its supervisors, and (iii) the AIFM's supervisor and the European Securities Markets Authority.[14] We strongly support the thrust of the Gauzés Draft Report in setting forth a procedure for permitting the sale of non-EU funds to EU investors under national law. Nonetheless, because a US RIC could not have an EU AIFM, it would be compelled to rely upon the second of the two conditions set forth. In our experience, negotiation and conclusion of the cooperation agreements among the governmental authorities contemplated by the Gauzés Draft Report would be a lengthy and drawn-out process. In the meantime, there would be substantial disruption affecting investor access to US RICs and other non-EU funds as well.

We respectfully recommend that any final Directive allow AIFM to sell AIF established in non-EU jurisdictions to professional investors subject to national law, as is contemplated in the Swedish Presidency Draft.[15] Alternatively, we recommend that pending the successful negotiation of the cooperation agreements between Member States and non-EU countries, Member State regulators be permitted to enter into information sharing agreements directly with non-EU managers so that ongoing business operations are not delayed or disrupted.

We submit that prohibiting access to US RICs is not in the best interest of institutional and other professional investors in the EU. US RICs are among the most-widely utilized investment vehicles in the world, owing in no small part to the comprehensive framework of regulation to which they are subject. Preserving the ability of EU Member States to continue to prescribe the terms and conditions of their national private placement regimes for professional investors – and under those regimes, permitting such investors to access US RICs – will not compromise the goals of the Directive.

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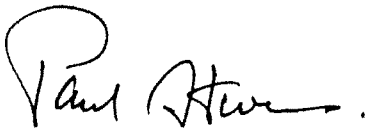
We are sensitive to the complexity of the issues under consideration in the proposed Directive, and we do appreciate the substantial work that the Commission, the Parliament and the Council are devoting to it. We share the common objective of establishing a framework for the regulation of non-UCITS funds that will mitigate systemic risks and protect investors. We are most grateful for this opportunity to convey our views and for your consideration of our recommendations. As noted above, we enclose as

[14] *See* Gauzés Draft Report, Amendment 118.

[15] *See* Swedish Presidency Draft, Article 31, paragraph 4a.

Appendix I specific language to address the concerns outlined in this letter. Should you wish to discuss our comments, or if we can be of any further information, please do not hesitate to contact me (paul.stevens@ici.org or 202-326-5901) or Susan Olson, the Institute's Senior Counsel (International Affairs) (solson@ici.org or 202-326-5813).

Sincerely,



Paul Schott Stevens
President and CEO
Investment Company Institute

cc: Honorable William E. Kennard
Representative of the United States of America to the European Union,
with the rank of Ambassador, Department of State

Andrew J. Donohue, Director
Division of Investment Management, US Securities and Exchange Commission

Ethiopis Tafara, Director
Office of International Affairs, US Securities and Exchange Commission

David Grim, Assistant Chief Counsel
Division of Investment Management, US Securities and Exchange Commission

David Vaughan, Attorney – Fellow
Division of Investment Management, US Securities and Exchange Commission

Peter De Proft, Director General
European Fund and Asset Management Association

APPENDIX I

ICI amendments to the proposed Directive on Alternative Investment Fund Managers

8 January 2010

Article 2 - paragraph 2 - point b

Text proposed by the Commission	*Amendment*
(b)AIFM established in the Community which do not provide management services to AIF domiciled in the Community and do not market AIF in the Community;	***(b) Management by an AIFM of AIF subject to regulation which are not domiciled in the Community and which are not marketed in the Community;***

Justification

By definition all third country funds (i.e., non-EU funds) are AIF, including US registered investment companies. If an EU AIFM provides portfolio management services to funds in third countries which are not marketed or domiciled in the EU and are subject to regulation in their own country, as is the case for US registered investment companies, there is no need to apply EU rules. Such funds are subject to their country's own regulatory regime. Application of the proposed Directive would lead to burdensome overlaps and, in some cases, inconsistencies or incompatibilities, precluding US registered investment companies from utilizing EU AIFM expertise absent an exemption from the Directive. US registered investment companies are subject to a robust regulatory regime similar to UCITS, are strongly and effectively regulated under the US securities laws and by the US Securities and Exchange Commission, and are not the type of fund that was intended to be included within the scope of the Directive. As of September 30, 2009, $1.297 trillion out of $10.717 trillion of the assets of open-ended US RICs (12.1%) and $349.95 billion out of $515.13 billion of the assets of US RICs that are exchange-traded funds (67.9%) were advised by investment advisers that have a European parent entity.

Article 18 – paragraph 1 – subparagraph 1

Text proposed by the Commission	*Amendment*
1. AIFM which intend to delegate to third parties the task of carrying out on their behalf one or more of their functions ***shall request prior authorisation from the competent authorities of the home Member State for each delegation.***	1. AIFM which intend to delegate to third parties the task of carrying out on their behalf one or more of their functions ***must inform the competent authorities of its home Member State in an appropriate manner.***

Justification

Given the global nature of securities markets and portfolio management, it is imperative that managers have appropriate flexibility to seek expertise outside the Community. The delegation framework for UCITS should be an appropriate framework for AIFM. Consequently, AIFM delegation should follow the requirements set forth in UCITS IV Art. 13(1)(a).

Article 18 – paragraph 1 - point b

Text proposed by the Commission	*Amendment*
(b)where the delegation concerns the portfolio management or the risk management, the third party must also be authorised as an AIFM to manage an AIF of the same type;	***(b)where the delegation concerns the investment management, the mandate must be given only to undertakings which are authorised or registered for the purpose of asset management and subject to prudential supervision: the delegation must be in accordance with investment-allocation criteria periodically laid down by the management companies; where the mandate concerns the investment management and is given to a third country undertaking, cooperation between the supervisory authorities concerned must be ensured;***

Justification

As described above, it is appropriate to allow the delegation of portfolio management in the same manner as permitted for UCITS.

Article 18 – paragraph 3

Text proposed by the Commission	*Amendment*
The third party may not sub-delegate any of the functions delegated to it.	***deleted***

Justification

As described above, the delegation provisions should be designed to align the Directive with the UCITS Directive.

Article 31 – paragraph 4a (new)

Text proposed by the Commission	*Amendment*
	Without prejudice to this Directive, Member States may allow or continue to allow marketing of third country alternative investment funds to professional investors on their territory subject to national law.

Justification

Member States should be able to prescribe the conditions under which professional investors domiciled in that Member State may invest in third country alternative investment funds.

Article 35 a (new)

Text proposed by the Commission	*Amendment*
	Member States may allow or continue to allow professional investors domiciled in the Member State to invest in third country alternative investment funds subject to national law.

Justification

Member States should be able to prescribe the conditions under which professional investors domiciled in that Member State may invest in third country alternative investment funds.