NautaDutilh

AVOCATS LUXEMBOURG

5 things you need to know about Investment Funds in 2022

Intro

In the field of investment funds, we have identified the following five trends, which will shape your agenda in the coming year. By anticipating these developments, you can use them to your advantage and prepare for their impact. The five main trends are:

#1 increased importance of ESG

#2 retailisation of alternative investment funds

#3 investment by funds in virtual assets

#4 upcoming amendments to AIFMD

#5 upcoming amendments to the ELTIF regulation

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Adoption of delegated acts and RTS

Increased importance of ESG

A delegated act supplementing Article 8 of the Taxonomy Regulation (the "Disclosure Delegated Act") was formally adopted on 4 June 2021. The Disclosure Delegated Act establishes technical screening criteria to determine when an economic activity qualifies as contributing substantially to climate change mitigation or climate change adaptation, within the meaning of Article 9 of the Taxonomy Regulation, and that it does not cause significant harm to other environmental objectives. The Disclosure Delegated Act aims to increase market transparency and help prevent greenwashing by ensuring that investors are provided with information about the environmental performance of assets and the economic activities of financial and non-financial undertakings. A second delegated act on technical screening criteria for economic activities that make a significant contribution to the sustainable use and protection of water and marine resources, the transition to a circular economy, pollution prevention and control, or the protection and restoration of biodiversity and ecosystems (the "Environmental Delegated Act") is expected to be published in the course of 2022. Finally, the first quarter of 2022 should see the formal adoption by the European Commission of regulatory technical standards ("RTS") for the content and presentation of disclosures under the Taxonomy Regulation. The RTS are expected to be applicable as from 1 January 2023.

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Expansion of the investor base

Retailisation of alternative investment funds

The retailisation of alternative investment funds is an incontrovertible trend based on expected higher returns through exposure to non-traditional asset classes and a desire on the part of alternative asset managers ("AIFMs") to widen their investor base in order to obtain additional financing for the vehicles they manage. Although barriers still exist, we have noted that the EU legislature is actively considering how more funding can be channelled, including from retail investors, into the real economy. One possible solution is the establishment of a separate feeder fund for retail investors. The feeder then invests in a master fund, together with institutional and professional investors. This type of master-feeder structure can help to address the liquidity concerns of retail investors as additional liquidity can be created in the feeder fund through the organisation of enhanced redemption options or the facilitation of secondary transfers amongst retail investors.

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Authorisation extension and compliance requirements

Investment by funds in virtual assets

The recent launch of the first fund organised under Luxembourg law to invest in cryptocurrencies, digital assets, and funds and equity of fintech or blockchain-linked companies brought to the fore the possibilities for investment funds to invest in cryptoassets. The CSSF recently noted that virtual assets can be suitable for alternative investment funds (“AIFs”) marketed to professional investors and managed by an authorised alternative investment fund manager (“AIFM”) that has obtained a specific extension of its authorisation for this type of investment strategy. In addition to the authorisation extension requirement, AIFMs and service providers will need to reshape their business model, governance, organisation policies, risk assessment and procedures in order to comply with the CSSF’s best practices regarding investment in such risk-sensitive asset classes. From a regulatory standpoint, the forthcoming European Markets in Cryptoassets Regulation (“MiCA”) aims inter alia to limit the risks of fraud and illicit practices inherent in cryptomarkets by imposing compliance requirements on service providers.

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Improvements to the AIFMD framework

Upcoming amendments to AIFMD

On 25 November 2021, the Commission released a proposal to amend the directive on alternative investment fund managers (“AIFMD”). The main amendments regard delegation arrangements, liquidity risk management, supervisory reporting, the provision of depositary and custody services, and loan origination by AIFs. The Commission recognises the value of the delegation regime, which allows for the efficient management of investment portfolios. However, amendments are proposed to ensure that AIF managers retain core functions. For example, new Annex V, containing a list of liquidity management tools (“LMT”) available to AIFMs managing open-ended AIFs, is introduced. In order to better face redemption pressure under stressed market conditions, the managers of such AIFs should be required to choose at least one LMT from this list, in addition to the possibility of suspending redemptions. The Commission also concluded that there is a need to harmonise requirements for AIFMs of loan-originating AIFs. The amended directive is expected to be adopted in early 2023. Member States will then have 24 months to amend their national legislation accordingly.

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Increase in the use of ELTIFs across the EU

Upcoming amendments to the ELTIF regulation

The European long-term investment fund ("ELTIF") is an alternative investment fund for long-term investments, such as social and transport infrastructure projects, real estate and SMEs. The ELTIF regulatory framework is intended to facilitate long-term investments in these types of assets by institutional and retail investors and provide an alternative, non-bank source of financing for the real economy. Given the degree of overlap, the Commission is reviewing AIFMD and the ELTIF Regulation at the same time. The proposed amendments to the latter aim to increase the use of ELTIFs across the EU for the benefit of the European economy and investors. This especially entails broadening the scope of eligible assets and investments, allowing more flexible fund rules that include the facilitation of fund-of-fund strategies, and lowering unjustified barriers that prevent retail investors from accessing ELTIFs.

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