

European Commission adopts finalised Level 2 Measures for ELTIFs

July 2024

Background

European long-term investment funds (**ELTIFs**) are the only type of funds dedicated to long-term investments that can be distributed across borders in the EU to both professional and retail investors.

Under the ELTIF Regulation¹, ESMA is mandated to prepare draft regulatory technical standards (**RTS**) on various aspects of the ELTIF framework, including the specific rules which should be applied to open-ended ELTIFs which offer limited redemption rights to investors. The drafting of the RTS has now reached a conclusion, with the European Commission adopting a **finalised set of RTS** on 19 July 2024.

In this briefing, we provide a brief overview of some of the key provisions set down by the European Commission in the RTS.

¹ Regulation (EU) 2015/760 as amended





Maximum redemptions permitted by open-ended ELITFs

The European Commission has provided that the maximum percentage of liquid assets which can be redeemed on a given dealing day by an open-ended ELTIF can be calculated by the AIFM either (i) on the basis of the redemption frequency and maximum length of the notice period or (ii) on the basis of the redemption frequency and the minimum percentage of liquid assets held by the ELTIF. The calculation methodology should be selected by the AIFM taking into account the specific criteria set down in the RTS.

In both scenarios, the AIFM must apply the percentage of liquid assets that can be redeemed on a given dealing day to the sum of:

- (a) the assets categorised as “liquid assets” within the portfolio at that redemption date; and
- (b) the expected cash flow, forecasted on a prudent basis over 12 months.

For the purposes of point (b), the AIFM can only take into account those expected positive cash flows for which it can demonstrate that there is a high degree of certainty that these cash flows will materialise. It cannot consider as expected positive cash flows the possibility that the ELTIF can raise capital through new subscriptions.

Option A: Calculation based on redemption frequency and notice period

Under this calculation methodology, the percentage of liquid assets which can be redeemed on a given dealing day for an open-ended ELTIF is calculated based on the redemption frequency and the notice period of the relevant ELTIF, (including the extension of the notice, if any), depending on which of the criteria referred to in Annex I to the ELTIF Regulation is selected by the AIFM.

A copy of Annex I to the RTS which sets down this criteria is available [here](#).

This calculation methodology does not make it mandatory for the relevant ELTIF to hold a minimum percentage of liquid assets. Instead, the calculation methodology is based solely on the redemption frequency and applicable notice period imposed on redeeming investors in the relevant ELTIF.

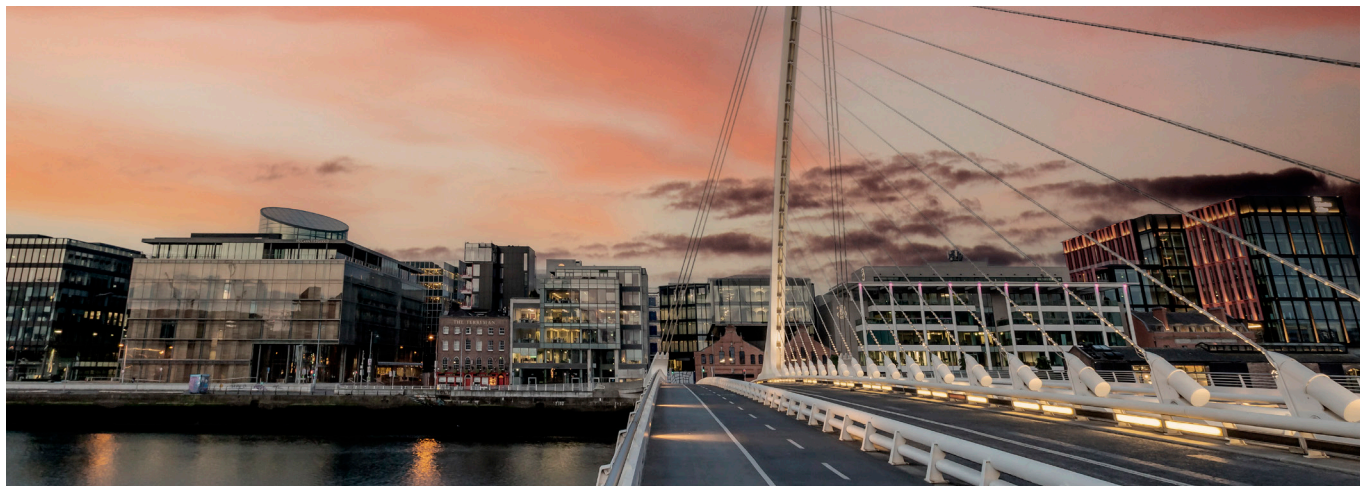
By way of example only, using the “baseline option”, an ELTIF which allows redemptions every 6 months and imposes a 1-month redemption notice period can redeem a maximum of 54.5% of the liquid assets held by the ELTIF on a given redemption day. However, in the case of an ELTIF which allows redemptions on a monthly basis and also imposes a 1-month redemption notice period, it is restricted under the RTS to redeeming a maximum of 9.1% of the liquid assets of the ELTIF on any redemption day.

Option B: Calculation based on redemption frequency and minimum percentage of liquid assets

The second of these options is to limit redemptions on any redemption day to the percentages outlined in the table in Annex II to the RTS, which are calibrated depending on the redemption frequency of the relevant fund and the level of liquid assets held by the ELTIF.

A copy of Annex II to the ELTIF Regulation is available [here](#).

By way of example only, under this calculation methodology an ELTIF which allows redemptions every 6 months is required to



maintain a minimum of 15% of liquid assets on an ongoing basis and is restricted under the RTS to redeeming a maximum of 67% of the liquid assets of the ELTIF on any one redemption day. In the case of an ELTIF which allows redemptions on a monthly (or more frequent) basis, the ELTIF must maintain a minimum of 25% of liquid assets on an ongoing basis and is restricted under the RTS to redeeming a maximum of 20%² of the liquid assets of the ELTIF on any one redemption day.

Other liquidity management requirements

As well as the requirements outlined above relating to the maximum percentage of liquid assets that can be used for redemption requests in an open-ended ELTIF, the RTS also set down other specific liquidity management provisions.

Compatibility of life of the ELTIF with the life-cycle of each of its individual assets

The RTS set down the criteria which must be considered by the AIFM when assessing whether the life of the ELTIF is compatible to the life-cycles of each of the individual assets of the ELTIF.

Minimum holding period applicable to open-ended ELTIFs

In contrast to ESMA's earlier recommendations³, the RTS suggest that a mandatory minimum holding period is not required for an open-ended ELTIF. However, if such a minimum holding period is applied by the AIFM, it should satisfy the criteria set down in the finalised rules.

Provision of information of redemption policy and liquidity management tools to the national competent authority of the ELTIF (NCA)

The RTS set down prescriptive information which must be provided by any AIFM managing an open-ended ELTIF to the ELTIF's NCA at the time of authorisation of the relevant ELTIF. This includes for example information on the redemption policy of the ELTIF, how assets and liabilities will be managed to meet redemption requests and the results of liquidity stress testing demonstrating how the ELTIF can deal with redemption requests in severe but plausible scenarios. Any material changes to the information provided to the NCA at authorisation must be notified to the NCA at least 1 month in advance where possible.

Separately where an ELTIF will redeem more frequently than on a quarterly basis, the AIFM must be in a position to justify to the NCA of the ELTIF the appropriateness of that redemption frequency.

Liquidity management tools (LMTs)

Under the RTS, the AIFM may, at its discretion choose to select and implement at least one LMT from a list of anti-dilution levies, swing pricing and redemption fees. However, it is also afforded the flexibility to select and implement other LMTs where it can justify this decision to the ELTIF's NCA.

² Applied on a monthly aggregated basis

³ Accessible from https://finance.ec.europa.eu/document/download/b882433c-2da9-48ce-a57a-e34b59c51600_en?filename=240419-opinion-eltif-rts_en.pdf



Other measures addressed in the RTS

Matching mechanism

An ELTIF may, subject to satisfying specific criteria, choose to provide for a matching mechanism under which transfer requests of shares of an ELTIF from an exiting investor can be “matched” with transfer requests by potential investors.

The RTS finalise the rules applicable to this matching mechanism, setting down:

- the minimum content requirements which must be satisfied if full or partial matching of transfer requests are facilitated;
- the requirements for determining the execution price and pro-ratio conditions where transfers are matched under the matching mechanism;
- the level of fees, costs and charges, if any, related to the transfer of shares of the ELTIF; and
- the minimum information that the ELTIF must disclose to investors when transfers are matched.

Circumstances in which the use of financial derivative instruments (FDI) for hedging purposes can be used by an ELTIF

An ELTIF can only use FDI where the use of such instruments “solely serves the purpose of hedging the risks inherent to other investments of the ELTIF”. The RTS set down the circumstances in which the use of FDI for hedging purposes is considered to meet this test.

Calculation of costs and presentation of costs borne by the ELTIF

The RTS set down the prescriptive rules on the specific costs, whether directly or indirectly borne by investors, which are associated with investing into an ELTIF which must be disclosed to potential investors.

Next steps

The application date of the RTS, subject to any objections being raised by the European Parliament or the Council of the EU during the three-month scrutiny period, is expected to be towards the end of October 2024.

Conclusion

The adoption of the RTS by the European Commission is an important and welcome step towards the finalising of the regulatory framework for open-ended ELTIFs. This is expected to democratise access for retail investors to long-term investments financing energy, social and transport infrastructure projects (amongst others) while still providing them with some liquidity if needed.

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