

INCEPTION IMPACT ASSESSMENT

Inception Impact Assessments aim to inform citizens and stakeholders about the Commission's plans in order to allow them to provide feedback on the intended initiative and to participate effectively in future consultation activities. Citizens and stakeholders are in particular invited to provide views on the Commission's understanding of the problem and possible solutions and to make available any relevant information that they may have, including on possible impacts of the different options.

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| TITLE OF THE INITIATIVE | Proposal for a Regulation amending Regulation (EU) 2015/760 of the European Parliament and of the Council of 29 April 2015 on European long-term investment funds |
| LEAD DG (RESPONSIBLE UNIT) | FISMA - Unit C4 |
| LIKELY TYPE OF INITIATIVE | Legislative proposal |
| INDICATIVE PLANNING | Q3 2021 |
| ADDITIONAL INFORMATION | A public consultation on the ELTIF review will be launched around four weeks following the publication of the Inception Impact Assessment |

The Inception Impact Assessment is provided for information purposes only. It does not prejudice the final decision of the Commission on whether this initiative will be pursued or on its final content. All elements of the initiative described by the Inception impact assessment, including its timing, are subject to change.

A. Context, Problem definition and Subsidiarity Check

Context

The European Long-Term Investment Funds Regulation (ELTIF) is a pan-European framework for Alternative Investment Funds (AIFs) that invest in longer term real economy investments such as infrastructural projects, real estate, listed and unlisted SMEs. The ELTIF regime is intended to facilitate investment in these assets by pension funds, insurance companies, professional and retail investors providing an alternative non-banking source of finance. Such long-term finance is critical for the Capital Markets Union (CMU), the EU climate action and the European Green Deal, as well as the EU Energy Union and the Digital Single Market. It is important for the development of the European economy on the path of smart, sustainable and inclusive growth, while supporting job creation and improving overall economic competitiveness and resilience to systemic shocks. The ELTIF Regulation lays down uniform rules on the authorisation, investment policies and operating conditions of EU AIFs and marketed in the Union as ELTIFs. ELTIFs may also, under certain conditions, be marketed to retail investors under a pan-European passport.

Since the adoption of the ELTIF legal framework in April 2015, only a small number of ELTIFs have launched with a relatively small amount of net assets under management (total AuM below ~EUR 2 billion). There are currently approximately 27 ELTIFs in the EU, however a number of Member States have no ELTIFs. The fact that market acceptance has not met expectations highlights the need to better understand the reasons for the low take-up and develop potential measures to address any issues identified.

By reviewing the legal and policy elements of the ELTIF framework, the Commission aims to increase the number of ELTIF funds and overall investment in the real economy. In June 2020, the High Level Forum (HLF) on the CMU has made a set of specific recommendations calling for a review of the ELTIF Regulation broadening the scope of eligible assets and reducing potential barriers to investment. The Commission is currently assessing the recommendations from the HLF as part of the overall ELTIF review and the CMU Action Plan.

Under Article 37 of the ELTIF Regulation, the Commission is also required to review the framework and submit a report to the co-legislators assessing the contribution of the ELTIF Regulation and of ELTIFs to the development of the Capital Markets Union and smart, sustainable and inclusive economic growth.

Problem the initiative aims to tackle

The EU has been suffering from a chronic lack of long-term financing for SMEs, notably compared to other major economies. Tools are therefore needed to ensure that more investments go into companies and long-term investment projects. A proper functioning regime for ELTIFs would have the potential to boost investors' ability to invest, among others, in unlisted equities and bonds with longer-term maturities, as well as transport and social infrastructure projects and other long-term sustainable investments. The ELTIF can connect sophisticated investor capital directly with these investments and drive greater professional investor demand.

European companies and in particular SMEs, would benefit from increased access to alternative sources of finance and a broadened investor base. The ELTIF passport is also an established basis on which to grow increased cross-border investment in the Union. While the current investor base is both institutional and retail, the ELTIF can be a suitable vehicle to promote the European cross-border retail investment fund market.

The current challenge with the ELTIF regime is that, to date, the initial take-up of ELTIFs by the market has been slow, with only a limited number of ELTIFs launched. While some delay can be expected in the case of a new product/fund label, there may also be other reasons as to why the ELTIF market has not developed to a larger scale. The preliminary feedback of stakeholders has focused on three main areas:

- i. **removing limitations on the supply side** by improving the fund structuring and eligible assets related aspects of the ELTIF framework;
- ii. **reducing the demand side barriers to investment** (with a focus on retail investors but also including the institutional investor base); and,
- iii. **the introduction of incentives** by Member States to promote ELTIF investment.

The ELTIF review should contribute to the further development of the market by examining the following issues:

The **first category of supply side issues** are mainly related to the eligible assets and investments with stakeholders calling for the inclusion of additional asset types including “financial undertakings”, investments in funds other than ELTIFs, EuVECAs or EuSEFs. Stakeholders also called for the clarification of some aspects of asset eligibility such as the meaning of “real assets” while also addressing other legal provisions that may cause uncertainty among market participants. Additional proposals included modifying borrowing limits, targeted amendments to improve the attractiveness of the ELTIF regime for institutional investors that will assist them in meeting conditions around investment strategy, governance, investor base and oversight.

The **second category of barriers to investment** are primarily focused on aligning national measures related to the retail passport for ELTIFs by reducing national discretions, clarifying the ELTIF requirements for the assessment of retail investor's knowledge and experience, introducing more flexibility for investors to redeem their investment “at a mid-point” or more frequent redemptions optionality, while reinforcing, where appropriate, liquidity requirements. Other proposals include encouraging participation from a wider range of investors, such as lowering the minimum entry ticket or finding ways to encourage the development of listed ELTIFs, encouraging the use of the ELTIF in unit-linked insurance products and targeted amendments to increase manager flexibility when executing investor centric investment strategies.

The **third category of the possible Member State incentives** such as tax reliefs are outside the mandate of the European Commission due to the powers stemming from the EU Treaties, and will hence not be addressed in the present initiative.

Basis for EU intervention (legal basis and subsidiarity check)

The Treaty on the Functioning of the European Union (TFEU) confers upon the European institutions the competence to lay down appropriate provisions that have as their object the establishment and functioning of the internal market (Article 114 TFEU). Depending on the policy option chosen and the specific design of the rules, the appropriate legal base could also be Article 53(1) TFEU on the taking-up and pursuing of activities by self-employed persons, which is used to regulate financial intermediaries, their investment services and activities.

Some Member States have put in place (or are considering) bespoke national regimes to regulate long-term investment funds. These national regimes can follow different approaches and create barriers to the cross-border provision of services in relation to long-term investments. This proliferation in national approaches also poses risks to the level playing field in the Single Market in terms of investor/consumer protection, market integrity and competition.

In the recognition of the basis for the EU intervention, Recital (52) of the ELTIF Regulation sets out “since the objectives of this Regulation, namely to ensure uniform requirements on the investments and operating conditions for ELTIFs throughout the Union, while taking full account of the need to balance safety and reliability of ELTIFs with the efficient operation of the market for long-term financing and the cost for its various stakeholders, cannot be sufficiently achieved by the Member States but can rather, by reason of their scale and effects, be better achieved at Union level, the Union may adopt measures in accordance with the principle of subsidiarity as set out in Article 5 of the Treaty on European Union.” The ELTIF Regulation also explicitly recognises ELTIFs as a conduit for supporting the CMU. EU action in the ELTIF sector, will add value by preventing market fragmentation through national regimes, addressing deficiencies identified in the framework and promoting further market growth and liquidity.

B. Objectives and Policy options

The overall objective of the initiative is to evaluate the effectiveness of the ELTIF framework and to identify the reasons for the markets failure to develop in line with expectations. In particular, the low uptake of ELTIFs and improving the EU ELTIF framework to ensure that it addresses the challenges identified in relation to directing

increased financing towards long-term investments in the real economy. These objectives will also complement the ongoing work on the Capital Markets Union and increasing the capital available for longer-term investments in the real economy.

Policy options will be structured to identify the most appropriate and proportionate approach that would fulfil these objectives without creating undue administrative burdens. In the absence of EU action, the most likely outcome is continued under-performance of the ELTIF sector and increasing market fragmentation impairing the effective functioning and development of the market.

The impact assessment will analyse also several policy options, ranging from soft-law measures (e.g. a ESMA's interpretative communication and/or Guidelines and/or Questions and Answers) to further clarify the applicability of existing EU ELTIF legislation to the introduction of targeted amendments to the ELTIF legal framework to ensure that the ELTIFs structure is an effective vehicle for channelling long-term investments while addressing the challenges of the ELTIF regime. The analysis of policy options, including their combinations, will focus on the alleged limitations of the ELTIF regime for professional investors (such as those pertaining to the eligible assets, investment objectives, leverage, redemption requirements and others), as well as those demand-side limitations for retail investors (such as appropriateness test, further lowering entry threshold, leverage, etc.) in combination with appropriate investor protection safeguards.

This process will also support the completion of the report under Article 37 of the ELTIF Regulation.

C. Preliminary Assessment of Expected Impacts

Likely economic impacts

ELTIFs provide long-term financing to infrastructure projects, unlisted companies, or listed small and medium-sized enterprises (SMEs) that issue equity or debt instruments for which there is no readily identifiable buyer. Clarifications on the scope of eligible assets could be considered to broaden the scope of the investment universe set out in the ELTIF framework. ELTIFs can complement or replace bank financing in addition to other investment funds (such as AIFs, EuSEFs and EuVECAs, as well as UCITS). The cost of funding is fundamental for undertaking new development projects. If the cost of funding decreases, companies will be able to undertake new projects and grow the real economy more readily. While ELTIFs alone cannot address all of the financing challenges, developing the market will complement the CMU Action Plan and support further development of this sector.

Since ELTIF eligible investment assets, such as infrastructure, intellectual property, vessels, equipment, machinery, aircraft or rolling stock, and immovable property, generate an economic and social benefit, higher investments in commercial property or housing are expected to contribute to smart, sustainable and inclusive growth and to the Union's energy, regional and cohesion policies.

In terms of the economic segments, regardless of whether ELTIFs target or specialise in infrastructure investment, investments in unlisted SMEs or in airplane or marine financing, the ELTIF regime has a broad range of applications. For example, the envisaged rules on investment policies (portfolio composition and diversification, concentration limits, limits on cash borrowing) or the envisaged rules on redemption policies are designed to apply to all categories of ELTIFs, whether they specialise in providing equity participations for infrastructure or whether they invest in real assets directly (airplane or ship finance). In light of the above, ELTIFs provide a useful investment structure with well-regulated fund rules that facilitate and complement existing funding sources and strategies and the achievement of the CMU objectives.

Likely social impacts

The review of the ELTIF legal framework is unlikely to have a direct impact on social issues. An indirect impact might however relate to the financing of long-term investments, such as social housing projects or infrastructure spending. Social housing, for instance, is included in the scope of eligible assets as part of the real estate category. Investment funds can provide financing to social housing projects or associations responsible for managing social housing properties. Investment funds appear to be well-placed to offer solutions to substitute or complement bank financing. Another indirect impact might be on the employment in the companies that attract investment from ELTIFs. By providing financing to these companies, they could secure existing jobs or create new employment opportunities, as well as promote regional development. Measuring precise social impacts might prove difficult due to substitution effects (understanding the origins of investment inflows and a recourse to an alternative fund structures).

Likely environmental impacts

The ELTIF framework has potential to contribute to and support the EU climate action and the sustainable finance work, as well as promote the green and resilient energy transition in the Union. Increasing funding options for long-term projects can be expected to aid the development of environmental projects and sustainable growth given the inclusion of sustainable criteria for some eligible assets. This would complement the investments in green, smart and sustainable growth. A wider range of financing may benefit marginal (more risky from a pure

financial perspective) projects more than core (less risky from a pure financial perspective) projects, though this would be a secondary impact depending on the nature of the projects targeted by ELTIFs. It is difficult to measure the exact impact that ELTIFs could have but as an example the ELTIFs could represent an added value for helping to finance environmental projects where, for example, bonds issuance or bank financing are excessively costly or impracticable.

Likely impacts on fundamental rights

The ELTIF Regulation respects the fundamental rights and observes the principles of the Charter of Fundamental Rights of the European Union and notably consumer protection, the freedom to conduct a business, the right to remedy and to a fair trial, and the protection of personal data as well as access to services of general economic interest. The ELTIF framework would be applied in accordance with those rights and principles, and the targeted amendments in the ELTIF regime would not have any consequences or adverse effects on the exercise of fundamental rights.

Likely impacts on simplification and/or administrative burden

The initiative aims to provide legal clarity regarding certain provisions of the current ELTIF framework. This should lead to simplifications for ELTIFs and their managers and may result in a reduction of the administrative burden and compliance costs. The review of the ELTIF Regulation is also aimed at recalibrating the product to potentially extend the basket of eligible assets, adjust leverage levels, clarify a few legal definitions where necessary and assess the appropriate size of the investment ticket.

This exercise will involve the recalibration of the product and fund structure related rules bearing in mind, among others, the interest of simplification and reducing the administrative burden, as well as adjusting the parameters of ELTIFs to meet the needs of the market and the investors in view of the recommendations of the High Level Forum of the CMU in order to facilitate increased uptake of ELTIFs among investors. More specifically, the analysis will propose a range of amendments, including those pertaining to the list of eligible assets and investments, as well as the diversification rules, portfolio composition and limits regarding the borrowing of cash. Further, amending, for instance, leverage limits and the minimum investment threshold will likely result in a change of investor protection safeguards.

The review should not lead to an increase in regulatory or administrative burdens. On the contrary, while there is a possibility that the compliance costs might potentially marginally increase at the initial stage, the revised ELTIF legal framework will avoid fragmented regulatory approaches across Member States in the future and should lead to a more efficient regulatory regime with lower administrative burdens. As such, compliance costs and regulatory burdens are ultimately expected to be lower. The review of the ELTIF framework will not have any material impact on public administrations.

D. Evidence Base, Data collection and Better Regulation Instruments

Impact assessment

An impact assessment is being prepared to support the preparation of this initiative and to inform the Commission's decision. The impact assessment will be accompanied by the report of the European Commission to the European Parliament and the Council on the functioning of the ELTIF regime.

Evidence base and data collection

In line with the general principles in the Better Regulation guidelines on the need for evidence-based impact assessments the Commission will gather evidence through several sources and will, *inter alia*, rely on:

- [“A New Vision for Europe’s Capital Markets: Final Report of the High Level Forum on the Capital Markets Union”](#), dated 10 June 2020, which has called for a targeted review of the ELTIF Regulation with a view to strengthen the ELTIF passport, encourage more participation from retail investors through more flexibility in redemptions or tax incentives, as well as broaden the scope of eligible assets and investments while taking into due account investor protection.
- Analysis of the existing legislative framework, in particular the ELTIF Regulation, the Commission Delegated Regulation (EU) 2018/480, Directive 2011/61/EU on Alternative Investment Fund Managers (AIFMD), the Prospectus Regulation (EU) 2017/1129 and the PRIIPS Regulation (EU) 1286/2014 (where marketing of the ELTIFs also to retail investors within the meaning of the ELTIF Regulation takes place), as well as ESMA’s work in [developing draft RTS](#) to determine the costs disclosure requirements applicable to ELTIF managers.
- Stakeholders’ colloquium on European long-term investment funds (ELTIFs) entitled “ELTIF - Challenges and Opportunities in 2020” held on 4 February 2020.
- The content, feedback and the respective documentation surrounding the [public consultation on cross-border distribution of investment funds](#) (UCITS, AIF, ELTIF, EuVECA and EuSEF) across the European Union, as well as follow-up legislative proposals and policy actions.
- Excerpt from the ESMA fact-finding questionnaire on EU ELTIFs, with breakdowns on the name of the National Competent Authorities (NCAs), name of the ELTIF manager, name of the ELTIF, Member State of the domicile and Member States in which ELTIFs are marketed.

- Analysis of the ESMA [alternative investment funds register](#), ESMA central database of [European Social Entrepreneurship Funds \(EuSEF\) managers](#) and ESMA central database of [European Venture Capital Funds \(EuVECA\) managers](#).
- European Commission's [report dated 10 June 2020 assessing the scope and the functioning of the AIFMD \(COM\(2020\) 232 final\)](#) and respective [Commission Staff Working Document \(SWD\(2020\) 110 final\)](#) assessing the application and the scope of the AIFMD.
- Analysis of the scope of the [European Green Deal](#) (Communication, COM(2019) 640 final, dated 11 December 2019) and the extent to which ELTIF structure and financial tools could be employed as a pass-through vehicle to facilitate the funding in the green transition in the public and the private sector.
- Documentation surrounding the CMU Action Plan, including the Communication from the Commission on ["Capital Markets Union: Progress on Building a Single Market for Capital for a Strong Economic and Monetary Union"](#) dated 15 March 2019.
- Publications and position papers by the EIB and EIF in the area of SME funding and long-term growth.
- Publicly available documentation on some existing ELTIFs, such as prospectuses, Key Investment Documents (KID), annual reports and other related documents.
- Analysis of academic and commercial publications on the topic of the practical issues pertaining to the functioning of the ELTIF framework, long-term investments in the EU, and policy aspects in the area of SME, infrastructure financing, real estate and lending.
- Analysis of policy and regulatory approaches to facilitate growth and long-term investments, including the legislation put in place in other jurisdictions, such as the UK Investment Trust legislation and the U.S. Business Development Company (BDC) model to finance small business.
- Market data on the size, asset flows and respective stakeholders in the field of long-term investments by using Morningstar and Refinitiv databases.
- Publicly available reports, studies, surveys, position papers and other relevant documents drawn up by private and public stakeholders;
- Input from relevant workshops, bilateral meetings and consultation with Member States and industry stakeholders, including asset managers, product manufacturers, retail investors representatives and investment funds active in the field of long-term investments;
- The results of the public consultation targeting all interested parties.

Consultation strategy

The Commission will launch an open public consultation related to this initiative. The consultation is an opportunity for all stakeholders (EU citizens, Member States, ESAs, NCAs, financial institutions, asset managers, investors etc.) to provide their views on the risks and opportunities related to the review of the ELTIF framework and the need for action. It will also present a range of possible solutions to address the issues raised by stakeholders.

The public consultation will be published on the [EUSurvey](#) portal. The Commission will consult the Expert Group of the European Securities Committee (EGESC), and will continue to liaise with stakeholders to further substantiate the analysis of the available policy options in line with the Better Regulation guidelines. The Commission will also liaise with the EIB and the EIF given the role of ELTIFs as an investment vehicle through which the EIB Group may channel its European infrastructure or SME financing. The Commission will continue to consult with NCAs both directly and through the ESMA Investment Management Standing Committee.

Will an Implementation plan be established?

Article 37(2) of the ELTIF Regulation mandates that the Commission's report to the European Parliament and to the Council should be accompanied, where appropriate, by a legislative proposal. Since the ELTIF Regulation is a directly applicable and legally binding piece of secondary EU legislation, an amended ELTIF Regulation and respective Level 2 regulations would not *per se* require implementation beyond those implementation measures (i.e. mainly competences of NCAs and sanctions) already being put in place.