8 July 2024
ESMA34-1985693317-1095

Consultation Paper

Draft Regulatory Technical Standards on Liquidity Management Tools under the AIFMD and UCITS Directive

Responding to this paper

ESMA invites comments on all matters in this paper and in particular on the specific questions summarised in Annex 1. Comments are most helpful if they:

1. respond to the question stated;
2. indicate the specific question to which the comment relates;
3. contain a clear rationale; and
4. describe any alternatives ESMA should consider.

ESMA will consider all comments received by **8 October 2024.**

All contributions should be submitted online at www.esma.europa.eu under the heading 'Your input - Consultations'.

Publication of responses

All contributions received will be published following the close of the consultation, unless you request otherwise. Please clearly and prominently indicate in your submission any part you do not wish to be publicly disclosed. A standard confidentiality statement in an email message will not be treated as a request for non-disclosure. A confidential response may be requested from us in accordance with ESMA's rules on access to documents. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by ESMA's Board of Appeal and the European Ombudsman.

Data protection

Information on data protection can be found at www.esma.europa.eu under the heading 'Data protection'.

Who should read this paper?

This document will be of interest to alternative investment fund managers, AIFs, management companies, UCITS, and their trade associations, depositories and their trade associations, as well as professional and retail investors investing into UCITS and AIFs and their associations.

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1 Executive Summary

Reasons for publication

The revised AIFMD and UCITS Directive[1] provide that ESMA shall develop draft regulatory technical standards (RTS) to determine the characteristics of liquidity management tools (LMTs)[2] available to AIFMs managing open-ended AIFs and to UCITS.

This Consultation Paper (CP) represents the first stage in the development of the draft RTS and sets out proposals for their content on which ESMA is seeking the views of external stakeholders.

Contents

Section 2 explains the background and gives detailed explanations on the content of the proposals and seeks stakeholders' input through specific questions.

Annex I sets out the list of questions contained in this paper.

Annex II contains the legislative mandate to develop draft RTS.

Annex III provides for the cost-benefit analysis related to the draft RTS.

Annex IV contains the full text of the draft RTS under the AIFMD.

Annex V contains the full text of the draft RTS under the UCITS Directive.

Next Steps

ESMA will consider the feedback it received to this consultation and expects to publish a final report and submit the draft technical standards to the European Commission for endorsement by 16 April 2025.

[1] Directive (EU) 2024/927 of the European Parliament and of the Council of 13 March 2024 amending Directives 2011/61/EU and 2009/65/EC as regards delegation arrangements, liquidity risk management, supervisory reporting, the provision of depositary and custody services and loan origination by alternative investment funds (europa.eu)
[2] The lists of LMTs are set out in Annex V of AIFMD and in Annex IIA of the UCITS Directive

2 Background

1. Directive (EU) 2024/927[3] (hereafter referred to as 'the amending Directive') amending Directives 2011/61/EU (AIFMD) and 2009/65/EC (UCITS Directive) was published in the Official Journal on 25 March 2024.

2. This amending Directive modifies the AIFMD and the UCITS Directive in the area of, inter alia, LMTs, supervisory reporting and depositaries. It also amends the AIFMD in relation to loan-originating alternative investment funds.

3. The amending Directive introduces new provisions on LMTs: according to Article 16(2)(b) of the AIFMD and Article 18a(2) of the UCITS Directive, AIFMs and UCITS[4] shall select at least two appropriate LMTs from those referred to in Annex V[5] of AIFMD and Annex IIA of the UCITS Directive, points 2 to 8 (in both Annexes), after assessing the suitability of those tools in relation to the pursued investment strategy, the liquidity profile and the redemption policy of the fund (for AIFs, only in the case these are open-ended).

4. AIFMs and UCITS shall include those tools in the fund rules or instruments of incorporation for possible use in the interest of investors. It shall not be possible for that selection to include only dual pricing and swing pricing. Funds that are established under the AIFMD and the UCITS Directive as MMFs may decide to select only one LMT instead of two from those referred to in Annex V (for AIFMD) and Annex IIA (for UCITS Directive), points 2 to 8.

5. In addition, AIFMs and UCITS shall implement detailed policies and procedures for the activation and deactivation of any selected LMT and the operational and administrative arrangements for the use of such tool. The selection of the LMTs and the detailed policies and procedures for their activation and deactivation shall be communicated to the competent authorities of the home Member State of the AIFM and to the competent authorities of the home Member State of the UCITS.

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[3] Directive (EU) 2024/927 of the European Parliament and of the Council of 13 March 2024 amending Directives 2011/61/EU and 2009/65/EC as regards delegation arrangements, liquidity risk management, supervisory reporting, the provision of depositary and custody services and loan origination by alternative investment funds (europa.eu)

[4] The obligation is on the UCITS and not on the management company.

[5] The list of LMTs is:

1. suspension of subscriptions, redemptions and repurchases
2. redemption gates
3. extension of notice periods
4. redemption fees
5. swing pricing
6. dual pricing
7. anti-dilution levy
8. redemption in kind
9. side pockets

6. In that context, ESMA shall, by 16 April 2025, develop draft RTS to specify the characteristics of the LMTs[6].

7. When developing those draft regulatory technical standards, ESMA shall take account of the diversity of investment strategies and underlying assets of AIFs/UCITS. Those standards shall not restrict the ability of AIFMs/UCITS to use any appropriate liquidity management tool for all asset classes, jurisdictions and market conditions.

8. It should be noted that the list of LMTs and their definitions are identical in the AIFMD and in the UCITS Directive. Since the empowerments are identical in the AIFMD and the UCITS Directive, ESMA is issuing a single CP for both sets of draft RTS, but ultimately ESMA will issue two different sets of draft RTS because the empowerments stem from two different sectoral legislations.

9. In addition, ESMA shall, by 16 April 2025, develop guidelines on the selection and calibration of LMTs[7]. ESMA is consulting at the same time on these draft guidelines[8] (hereafter referred to as 'CP on guidelines on LMTs').

10. Therefore, the future RTS on the characteristics of LMTs will have to be read in conjunction with the ESMA Guidelines on selection and calibration of LMTs.

11. Finally, under Article 16(2)(f) of AIFMD ESMA shall develop, by 16 April 2025, draft RTS to determine the requirements with which loan-originating AIFs are to comply to maintain an open-ended structure. ESMA will consult on these RTS separately at a later stage.

2.1 Regulatory Technical Standards

12. For ease of reference, in this CP references to 'funds' should be understood as references to both UCITS and AIFs. Similarly, references to 'fund managers' should be understood as references to both AIFMs and Management Companies. In the case of provisions applying to one type of funds or fund managers only, then this CP specifically refers to UCITS, AIFs, AIFMs or Management Companies.

13. According to Article 16(2)(g) of AIFMD and Article 18a (3) of the UCITS Directive, ESMA shall develop draft RTS to specify the characteristics of all the LMTs set out in the relevant Annexes of the Directives. When developing those draft RTS, ESMA shall take account of the diversity of investment strategies and underlying assets of AIFs/UCITS. Those standards shall not restrict the ability of AIFMs/UCITS to use any appropriate liquidity management tool for all asset classes, jurisdictions and market conditions.

[6] See Article 16(2)(g) of AIFMD and Article 18a(3) of the UCITS Directive
[7] See Article 16(2)(h) of AIFMD and Article 18a(4) of the UCITS Directive
[8] https://www.esma.europa.eu/sites/default/files/2024-07/ESMA34-1985693317-1097_CP_on_LMTs_of_UCITS_and_open-ended_AIFs.pdf

14. Importantly, the draft RTS do not address the conditions under which the LMTs selected by fund managers shall be activated because the scope of the RTS is limited to the characteristics of each LMT and there is no empowerment for ESMA to determine the circumstances according to which the selected LMTs shall be activated (except for side pockets for which ESMA is tasked with determining the circumstances where side pockets may be activated in the context of the Guidelines on LMT for UCITS and open-ended AIFs[9]).

2.2 Characteristics of LMTs

2.2.1 General considerations

- Use of other tools to manage the liquidity of the funds

15. In addition to the two LMTs (only one for MMFs) that fund managers shall at least select under Article 16(2)(b) of the AIFMD and Article 18a(2) of the UCITS Directive, fund managers may also decide to use other tools than the ones referred to in the AIFMD and UCITS Directive to manage the liquidity of the fund they manage. However, when doing so, these other tools shall not be considered as LMTs for the purpose of complying with Article 16(2)(b) of AIFMD and Article 18a(2) of the UCITS Directive.

16. One example of these other tools would be a so-called "soft closure", where the fund is closed to new subscriptions when the size of the fund exceeds a pre-determined level, while still allowing investors to redeem. These types of tools may be appropriate for funds pursuing investment strategies where the size of the underlying markets in which the funds invest is limited and it would not be in the best interest of investors to continue to accept new subscriptions.

- International work on liquidity management tools

17. In 2023, IOSCO published its Guidance on anti-dilution tools. The anti-dilution tools listed in the IOSCO Guidance are redemptions/subscription fees, swing pricing, anti-dilution levy, valuation at bid or ask price and dual pricing.

18. According to the IOSCO Guidance, these tools should impose on subscribing and redeeming investors the estimated cost of liquidity, i.e., explicit and implicit transaction costs of subscriptions or redemptions, including any significant market impact of asset purchases or sales to meet those subscriptions or redemptions.

19. ESMA is of the view that these are important characteristics that should be considered in the context of the RTS and also in the CP on the Guidelines on LMTs.

[9] See Section 6.5.5 of the draft Guidelines on LMTs

- Difference between AIFs and UCITS

20. ESMA believes that in most instances, the characteristics of the LMTs should be the same under both legal frameworks and that only in limited circumstances these characteristics would differ. Similarly, ESMA has not identified so far, any investment strategies that would require tailored characteristics of LMTs. However, if ESMA concluded that there is a need to differentiate further between UCITS and AIFs, this would be reflected in the draft RTS. For the time being, the only differences that ESMA has identified between UCITS and AIFs relate to one of the characteristics of redemption gates and the provisions on side pockets (see sections 2.2.3 and 2.2.10 thereafter).

2.2.2 Suspension of subscriptions, repurchases and redemptions

21. According to the revised AIFMD and UCITS Directive, suspension of subscriptions, repurchases and redemptions means *"temporarily disallowing the subscription, repurchase and redemption of the fund's units or shares".*

22. Suspension of subscriptions, repurchases and redemptions are not part of the two LMTs that AIFMs and UCITS shall at least select. These are universal tools that fund managers should be able to use in addition to the ones they have to select. They shall be activated only in exceptional circumstances and where justified having regard to the interests of the fund's investors.

- Characteristics of suspension of subscriptions, repurchases and redemptions

23. In case of activation of this LMT, the fund manager shall not process any request for subscription, repurchase and redemption. Therefore, the fund cannot be closed for redemptions and repurchases and continue to accept subscriptions (and vice versa). The suspension shall apply simultaneously to, subscriptions, repurchases and redemptions.

24. According to ESMA, when fund managers decide to suspend the subscriptions, repurchases and redemptions, such a decision shall be accompanied by a plan for the future of the fund. After the activation of a suspension, there could be a number of possible outcomes, including:

    - The fund is reopened for subscriptions, repurchases and redemptions after a certain period of time and the fund is managed according to the fund's rules.
    - The fund manager creates a side pocket[10].

[10] For side pockets different provisions would apply depending on whether the fund is a UCITS or an AIF as explained in Section 2.2.10 of this consultation paper.

- The fund is put into liquidation if the fund manager comes to the conclusion that it is in the best interest of shareholders or unit-holders as a whole.

25. ESMA understands that repurchases of units/shares refers to situations where the fund decides at its own initiative to buy back its own units/shares and not at the requests of investors. Despite this difference, ESMA is of the view that all the characteristics below shall apply in the same manner to suspension of redemptions and suspension of repurchases.

26. The characteristics of suspension of subscriptions, repurchases and redemptions would therefore be the following:

    - The triggering event shall consist of exceptional circumstances and the decision shall be made in the best interests of investors.
    - The fund is simultaneously and temporarily closed for subscriptions, repurchases and redemptions.
    - Subscription, repurchase and redemption orders that have been placed but not executed before the fund manager suspends shall not be executed before the suspension of subscriptions, redemptions and repurchases is lifted.
    - The fund is reopened simultaneously for subscriptions, redemptions and repurchases.

27. ESMA believes that the RTS for suspension of subscriptions, repurchases and redemptions shall be the same between the AIFMD and the UCITS Directive.

Q1. Do you agree with the proposed characteristics of suspension of subscriptions, repurchases and redemptions? If not, please justify your position.

Q2. Do you agree that orders that have been placed but not executed before the fund manager suspends shall not be executed until the suspension is lifted? If not, please explain why these orders shall be executed.

Q3. Once the fund is reopened for subscriptions, repurchases and redemptions, what would be your approach to redemption orders that have not been executed before the fund was suspended?

Q4. Do you think there are circumstances where subscriptions, repurchases and redemptions may not be reopened simultaneously? If yes, what are these circumstances?

Q5. Can you think of any further characteristics of suspension of subscriptions, repurchases and redemptions?

Q6. Do you think there is merit for the characteristics of suspension of subscriptions, repurchases and redemptions gates to differ between different investment strategies and between AIFs and UCITS? If yes, how?

2.2.3 Redemption gates

28. According to the revised AIFMD and UCITS Directive, a redemption gate means a temporary and partial restriction of the right of unit-holders or shareholders to redeem their units or shares, so that investors can only redeem a certain portion of their units or shares.

- Characteristics of redemption gates

29. Contrary to suspensions of redemptions and subscriptions, a fund that applies redemption gates could still be open for subscriptions and the restriction only applies to the redemptions.

30. Redemption gates are composed of an activation threshold which is the threshold that triggers the activation of redemption gates. This threshold shall be determined, for a given dealing day, as the net redemption orders expressed as a percentage of the Net Asset Value ('NAV') of the fund.

31. ESMA has identified another method for determining the activation threshold which would consist in applying the activation threshold at the level of individual redemption orders. With such mechanism, redeeming investors placing redemption orders below the redemption threshold would get their redemption orders fully executed, while redeeming investors placing redemption orders above the threshold would get their redemption orders partially executed in the case the redemption gate is activated. ESMA is of the view that this type of redemption gate threshold should not be allowed as some investors would be treated more favourably than others.

32. In addition, there is a need to avoid any possible conflict between these draft RTS and the ELTIF Regulation and, in particular the future ELTIF Delegated Regulation. In that context, the characteristic on the redemption gate threshold set out in paragraph 31, should not apply to ELTIF for which the characteristics of gates, if put in place by the manager of the ELTIF, are set out in Article 18(2)(d) of the ELTIF Regulation and in its upcoming Delegated Regulation[11].

33. When the activation threshold is exceeded, either the redemption gate is automatically activated, or the fund manager/fund Board shall decide to activate the redemption gate or not. This means that the fund manager/fund Board may decide to execute in full the redemption orders, having regard the liquidity of the fund and provided that the full execution of the redemption orders is in the best interest of investors (both redeeming and

[11] At the time this consultation paper was drafted, the Delegated Regulation on the ELTIF Regulation was not available yet.

remaining investors). The fund manager/fund Board may also decide to activate the gate but to satisfy redemption requests above the pre-set activation threshold, depending on the underlying liquidity of the fund. This means that the fund manager/Fund Board has the option to activate redemption gates at a higher level than the pre-set activation threshold but never below the activation threshold.

34. Therefore, redemption gates are also composed of a redemption gate level which corresponds to the exact level of the redemption gate applied in case of activation of the redemption gate (see example below for further details).

35. For a given dealing date, if a redemption gate is activated, the same level of redemption gate shall apply to all redeeming investors in proportion of their redemption orders. In the case of activation of redemption gates, the non-executed part of redemption orders shall either be carried forward to the next dealing date or cancelled at the initiative of investors.

36. The fund manager/fund Board shall specify in advance, whether the part of redemption orders that have not been executed, as a result of the activation of the redemption gate, and that have been carried forward to the next dealing date, shall have any priority or not over redemption orders submitted for execution at the next dealing date.

Example:

37. For example, a fund manager sets an activation threshold at 10% of the NAV of the fund. The fund receives net redemption requests for 15% of NAV of the fund. The fund manager/fund Board may decide to satisfy redemption requests up to 12.5% of net assets. Therefore, the fund manager would execute 83.3% of all redemption requests on a pro-rata basis instead of 66.66% if it had strictly applied the gate at 10%.

38. In this example, the activation threshold is 10% of the NAV and the actual redemption gate level applied is 83.3%. Also, all redeeming investors shall get 83.3% of their redemption orders executed (i.e. it shall not be possible to execute 83.3% of redemption orders of some investors and 100% of redemption orders of others investors).

39. Therefore, the characteristics of redemption gates would include:

    - The activation threshold, which triggers the possibility to temporarily activate this LMT. The activation threshold shall be expressed as percentage of the NAV of the fund for a given dealing day and determined as the net redemption orders at the level of the fund (except for ELTIF for which the activation threshold is determined in Article 18(2)(d) of the ELTIF Regulation as a maximum percentage of asset referred to in Article 50(1) of the UCITS Directive and in the upcoming Delegated Regulation).
    - Investors have a temporary and partial restriction on their ability to redeem their units or shares from the fund.

- The redemption gate level, which corresponds to the actual proportion of redemption orders executed for a given dealing date. The redemption gate level shall not be below the activation threshold.
- When activated, the same redemption gate level shall apply to all redeeming investors on pro rata basis of their redemption orders. In the case of funds with multiple share classes, the level of redemption gate shall be the same for all share classes.
- When the activation threshold is exceeded, the redemption gate may be either automatically activated or the fund manager/the responsible fund Board may decide whether or not to activate the redemption gate.
- The non-executed part of the redemption orders shall be carried forward to the next dealing date or may be cancelled at the initiative of investors.
- The fund manager/fund Board shall specify in advance whether the part of redemption orders that have not been executed and that have been carried forward to the next dealing date shall have any priority over new redemption orders submitted for execution at the next dealing date.
- The fund may still be open for subscriptions.

40. ESMA believes that the RTS for redemption gates shall be the same between the AIFMD and the UCITS Directive.

Q7. Do you agree with the description of redemption gates and their characteristics? If not, please justify your position.

Q8. The draft RTS provides that the redemption gate threshold shall be expressed as a percentage of the NAV of the fund considering the net redemption orders for a given dealing day. Are you aware of any other method that ESMA should consider in the RTS? If yes, please explain.

Q9. Do you agree that redemption gates may be either activated automatically when the activation threshold is exceeded or that the fund manager/ fund Boards may decide whether or not to activate the redemption gate? Do you believe that automatic activation of redemption gates could create a first mover advantage?

Q10. Do you think that the automatic activation of redemption gates shall not be permitted for some types of funds? If yes, please explain your position.

Q11. Do you agree that the activation threshold shall not be expressed at the level of the single redemption order? If not, please justify your position.

Q12. In the case of activation of redemption gates, do you agree that investors should have the right to cancel the non-executed part of their redemption orders? In particular, should there be a different approach between UCITS and AIFs?

Q13. Do you think there is merit in having different characteristics of redemption gates for different investment strategies and between AIFs and UCITS? If yes, how?

Q14. In the case of funds with multiple share classes, do you agree that the same redemption gate shall apply to all share classes? If not, please justify your position.

Q15. Can you think of any further characteristics of redemption gates?

2.2.4 Extension of notice periods

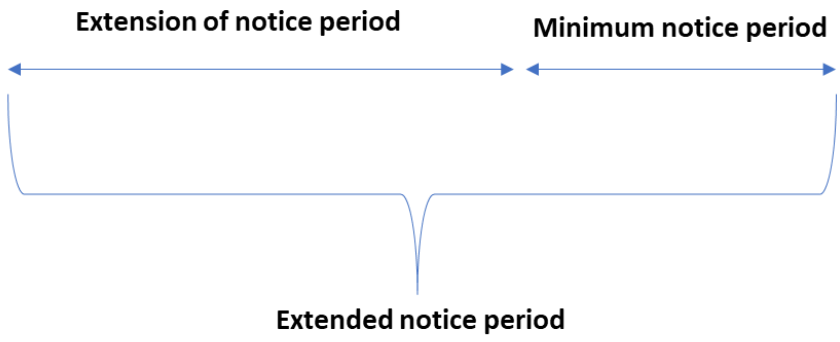
41. According to the revised AIFMD and UCITS Directive, the extension of notice periods means extending the period of notice that unit-holders or shareholders must give to fund managers, beyond a minimum period which is appropriate to the fund, when redeeming their units or shares.

    - Characteristics of extension of notice periods

42. The extension of the notice period shall not have any impact on the dealing frequency of the fund and shall not include the settlement period. This means that if the notice period of a fund is extended, the dealing frequency of the fund shall not be modified. In particular, UCITS that would extend their notice period, shall continue to make public in an appropriate manner the issue, sale, repurchase or redemption price of their units each time they issue, sell, repurchase or redeem them, and at least twice a month as per Article 76 of the UCITS Directive. The extension of the notice period shall not change the nature of the fund.

43. The extended notice period shall be understood as the notice period that results from the sum of the minimum notice period, as defined in the funds rules, and the additional period of notice before the next possible redemption dates that investors shall respect when placing their redemption order.

44. For example, a fund calculates its NAV once a week with an original notice period of two days. The fund manager/fund responsible Board decides to extend the notice period by 3 additional days. This means that the new notice period (i.e. the extended notice period) that investors must give to the fund manager before the next dealing date is now 5 days and no longer 2 days (i.e. 2 days of original notification period + 3 additional days as per the extension).



45. When extending the notice period, fund managers shall apply the same extension to all unit-holders or shareholders of the fund. In the case of funds with multiple share classes, the extension of the notice period shall be the same for all share classes.

46. Therefore, the characteristics of the extension of notice periods would include:

- The extension of the notice period that shall be the period of time that is added to the minimum notice period that investors shall respect when placing their redemption order. The sum of the extension of the notice period and the minimum notice shall be considered as the 'extended notice period'.
- Fund manager/ fund Board may decide to apply the extension of notice period for a determined period of time (i.e. for several consecutive dealing dates).
- The same extension of notice period shall apply to all redeeming investors and in the case of funds with multiple share classes, the same extension of notice period shall apply.

47. ESMA believe that the RTS for the extension of notice periods shall be the same under the AIFMD and UCITS Directive.

Q16. Do you agree with the description of extensions of notice period and their characteristics? If not, please justify your position.

Q17. Do you agree that the same extension of notice period shall apply to all investors or different extensions of notice periods per share class/unit shall be allowed? Please justify your position.

Q18. Do you agree that extensions of notice period may be applied for a pre-defined period of time (for a pre-defined number of dealing dates)? If not, please justify your position.

Q19. Do you think there is merit for the characteristics of extensions of notice period to differ between different investment strategies and between AIFs and UCITS? If yes, how?

Q20. How would you execute redemption orders that have been placed but not executed before the notice period is extended? Would you execute them under the original notice period, or would you execute them at the following dealing day?

Q21. How would you ensure fair treatment of investors when deactivating the extension of notice period?

2.2.5 Redemption fees

48. According to the revised AIFMD and UCITS Directive, a redemption fee means a fee, within a predetermined range that takes account of the cost of liquidity that is paid to the fund by unit-holders or shareholders when redeeming units or shares, and that ensures that unit-holders or shareholders who remain in the fund are not unfairly disadvantaged.

- Characteristics of redemption fees

49. Redemption fees are predetermined fixed fees that are charged to redeeming investors and paid to the fund whatever the change in the net capital of the fund is (i.e. transaction-based fees). This means that when applying a redemption fee, the impact of other subscriptions and redemptions on the NAV of the funds are not taken into account (as opposed to anti-dilution levies and swing pricing).

50. Redemption fees shall impose on redeeming shareholders or unit-holders the explicit and implicit estimated costs of portfolio transactions caused by redemptions, including any significant market impact of assets sales to meet those redemptions.

51. Redemption fees shall be expressed as percentage of the redemption orders. They may be expressed as a range with a minimum, which cannot be 0, and maximum amount, to take into account that transactions costs might increase in stressed market conditions.

52. Redemption fees may be applied irrespective of the amount of the redemption orders or only when the redemption orders exceed a certain threshold that could be expressed as a percentage of the NAV of the fund or as a number of shares/units redeemed, or a combination of both.

53. Regarding the calibration of redemption fees, ESMA provides guidance in the CP on the Guidelines on LMT of UCITS and open-ended AIFs (see section 5.5.4.1 of the draft Guidelines).

54. Funds may have a single level of redemption fees or different levels of redemption fees (e.g. the larger the redemption order the higher the redemption fee, so called ‘tiered approach’).

55. Therefore, the characteristics of redemption fees would include:

- Redemption fees correspond to transaction-based costs which are fixed or have low variation. Redemption fees are deducted from the money received by redeeming investors.
- Redemption fees are paid to the fund to the benefit of remaining investors.
- Redemption fees shall impose on redeeming shareholders or unit-holders the explicit and implicit estimated costs of portfolio transactions caused by redemptions, including any estimated significant market impact of assets sales to meet those redemptions.
- Redemption fees may apply to all redemption orders or only to redemption orders that exceed a certain threshold which can be expressed as a percentage of the NAV of the fund or as a number of shares/units redeemed by investors or both.
- Investors placing redemptions orders that correspond to a certain redemption fee level shall all be charged the same redemption fee.

56. ESMA believes that the RTS on redemption fees shall be the same for AIFMD and the UCITS Directive.

Q22.Do you agree with the description of redemption fees and the corresponding characteristics? If not, please justify your position.

Q23.Can you think of any other redemption fee mechanism than the ones described above? If yes, please provide examples.

Q24. Do you think there is merit for the characteristics of redemption fees to differ between different investment strategies and between AIFs and UCITS? If yes, how?

2.2.6 Swing pricing

57. According to the revised AIFMD and UCITS Directive, swing pricing means a pre-determined mechanism by which the net asset value of the units or shares of an investment fund is adjusted by the application of a factor (‘swing factor’) that reflects the cost of liquidity.

- Characteristics of swing pricing

58. The swing factor shall impose on redeeming and subscribing shareholders or unit-holders the explicit and implicit costs of portfolio transactions caused by subscriptions or redemptions, including any estimated significant market impact of assets purchases or sales to meet those subscriptions or redemptions.
59. When swing pricing is activated, the NAV of the fund is adjusted to incorporate the swing factor. The NAV published by the fund manager shall be the swung NAV (i.e. the NAV with

the application of the swing factor) and all transacting investors (i.e. both subscribing and redeeming investors) shall transact on the basis of the swung NAV.

60. Fund managers selecting swing pricing may decide to adjust the NAV of the fund on every dealing date for which there is a net activity of any size between redemptions or subscriptions (commonly referred to as “full swing”) or only when the net redemptions or subscriptions are greater than a predetermined swing threshold (commonly referred to as “partial swing”).

61. Under both types of swing pricing, the direction of the swing (i.e., whether the swing factor is added to or deducted from the NAV) is determined by the net capital activity of the day. Therefore, for a given dealing date, if the net difference between redemptions and subscriptions results in net subscriptions, the swing factor will be added to the NAV that will be adjusted upward. On the contrary, for a given dealing date, if the net difference between redemptions and subscriptions results in net redemptions, a swing factor will be deducted to the NAV that will be adjusted downward.

62. Under both types of swing pricing, a fund manager may decide to have either a single swing factor or apply progressively increasing swing factors depending on the net capital activity (commonly referred to as “tiered approach“). A tiered approach intends to account for increased activities in redemptions and subscriptions that generate higher transaction costs and market impact in relative terms (i.e. transactions costs that increase more rapidly than the net capital activity of the fund).

63. Guidance on the calibration of swing pricing is further detailed in the CP on the Guidelines on LMT for UCITS and open-ended AIFs (see section 6.5.4.2 of the draft Guidelines).

64. Thereby, fund managers may also choose to apply different swing factors for net subscriptions and net redemptions.

- Therefore, the characteristics of swing pricing would include:
- The swing threshold (“full swing“ or “partial swing“).
- The swing factor which shall reflect the estimated cost of liquidity and used to adjust the NAV (“swung NAV“).
- The swing factor shall impose on redeeming and subscribing shareholders or unit-holders the explicit and implicit estimated costs of portfolio transactions costs caused by subscriptions or redemptions, including any significant market impact of assets purchases or sales to meet those subscriptions or redemptions.
- For a given dealing date, if the net difference between redemptions and subscriptions results in net subscriptions, the swing factor is added to the NAV that is adjusted upward. On the contrary, for a given dealing date, if the net difference

between redemptions and subscriptions results in net redemptions, a swing factor is deducted from the NAV that is adjusted downward.

- When activated, all transacting investors are transacting on the basis of the adjusted NAV (subscribing and redeeming investors). In the case of funds with multiple share classes, the same swing factor shall be applied.

65. ESMA believes that the RTS on swing pricing shall be the same for AIFMD and the UCITS Directive.

Q25. Do you agree with the description of swing pricing and the corresponding characteristics? If not, please justify your position.

Q26. Can you think of any characteristics of swing pricing that the ones described above?

Q27. Do you think there is merit for the characteristics of swing pricing to differ between different investment strategies and between AIFs and UCITS? If yes, how?

Q28. Do you agree that in the case of funds with multiple share classes, the same swing factor shall be applied to all share classes? If not, please justify your position.

2.2.7 Dual pricing

66. According to the revised AIFMD and UCITS Directive, dual pricing means a pre-determined mechanism by which the subscription, repurchase and redemption prices of the units or shares of an investment fund are set by adjusting the NAV per unit or share by a factor that reflects the cost of liquidity.

- Characteristics on dual pricing

67. In the IOSCO guidance on Anti-dilution tools, dual pricing refers to the calculation of two NAVs per valuation point and there can be two ways to implement it:

    a) calculating one NAV which incorporates assets' ask prices and the other NAV which incorporates assets' bid prices. Subscribing investors pay the NAV calculated using ask asset prices and redeeming investors receive the NAV calculated using bid asset prices;

    b) setting an 'adjustable spread' around the fund's NAV under which assets are priced on a mid-market basis, with a bid price at which the fund redeems shares and an offer price at which the fund issues new shares. The difference between these two prices is known as the spread as estimated by the fund manager, which could be dynamic to reflect the liquidity costs in prevailing market conditions.

68. ESMA agrees that these methods should be the two methods used by fund managers to calculate dual pricing.

69. Therefore, the characteristics of dual pricing would include:

- The method that would consist of one of the two following calculation methods:
  - The fund has two NAVs with one NAV calculated using the ask prices of the assets and one NAV calculated using the bid prices of the assets. Subscribing investors shall subscribe on the basis of the NAV calculated according to the ask prices and redeeming investors shall redeem on the basis of the NAV calculated according to the bid prices.
  - The NAV of the fund, under which assets are priced, is adjusted by a factor that reflects the cost of liquidity. Subscribing investors shall subscribe on the basis of the NAV to which is added the adjusted factor and redeeming investors shall redeem on the basis of the NAV from which the adjusted factor is deducted.
- In the case of funds with multiple share classes, the same methods shall apply to all share classes.

70. Therefore, although dual pricing and swing pricing share the same objective of imposing transaction costs to investors, their mechanism is different. In particular, with swing there is only one NAV for all transacting investors (i.e. the "swung NAV") whereas with dual pricing there are two NAVs (one for subscribing investors and one for redeeming investors).

71. ESMA believes that the RTS on dual pricing shall be the same for AIFMD and the UCITS Directive.

Q29. Do you agree with the description of the dual pricing and the corresponding characteristics? If not, please justify your position.

Q30. Are there any other calculation methods for dual pricing that should be considered? If yes, please give example.

Q31. Do you think there is merit for the characteristics of dual pricing to differ between different investment strategies and between AIFs and UCITS? If yes, how?

2.2.8 Anti-dilution levy

72. According to the revised AIFMD and UCITS Directive anti-dilution levy means a fee that is paid to the fund by a unitholder or shareholder at the time of a subscription, repurchase or redemption of units or shares, that compensates the fund for the cost of liquidity incurred because of the size of that transaction, and that ensures that other unit-holders or shareholders are not unfairly disadvantaged.

    - Characteristics on anti-dilution levy

73. Anti-dilution levies are charged to redeeming or subscribing investors in the case of a change in the net capital activity of the fund (i.e. if the number of redemptions exceed the number of subscriptions or vice-versa).

74. In particular, anti-dilution levies shall impose on redeeming and subscribing shareholders or unit-holders the explicit and implicit estimated costs of portfolio transactions caused by subscriptions or redemptions, including any estimated significant market impact of assets purchases or sales to meet those subscriptions or redemptions.

75. The same anti-dilution levy may be applied to all subscribing / redeeming investors or, where possible, based on an individual investor's in / outflows and charged to each investor accordingly.

76. An anti-dilution levy may be charged on every dealing date for which there is a net activity of any size between redemptions or subscriptions or if it exceeds a certain pre-determined threshold.

77. Anti-dilution levies are different from redemption fees in the sense that they are variable and calibrated according to the fund's net flows. Redemption fees on the contrary are pre-determined fixed fee (regardless of the net flow of the fund), which can be increased under, for example, stressed market conditions (i.e. expressed as range).

78. Therefore, the characteristics of an anti-dilution levy would include:

    - The level of the levy is expressed as a percentage of the redemption/subscription order.
    - There can be a pre-determined activation threshold.
    - For a given dealing date, if the net difference between redemptions and subscriptions results in net subscriptions, an anti-dilution levy will be charged to subscribing investors. Conversely, for a given dealing date, if the net difference between redemptions and subscriptions results in net redemptions, an anti-dilution levy will be charged to redeeming investors.
    - When activated, all redeeming (or subscribing) investors shall be charged an anti-dilution levy. The amount of the levy charged to investors may be the same for all subscribing/redeeming investors or tailored to the exact transaction costs of the redeeming/subscribing investors if the fund manager is in capacity to quantify them exactly per investor.

79. Regarding the calibration of the anti-dilution levy, ESMA provides draft guidance in the CP on the Guidelines on LMT for UCITS and open-ended AIFs (see section 6.5.4.4 of the draft Guidelines).

80. ESMA believes that the RTS on anti-dilution levy shall be the same for AIFMD and the UCITS Directive.

Q32. Do you agree with the description of the anti-dilution levy and the corresponding characteristics? If not, please justify your position.

Q33. Are there any other calculation methods for anti-dilution levy that ESMA shall consider? If yes, please give example.

Q34. In the case of funds with multiple share classes, would you see the possibility for different anti-dilution levies depending on share classes? Please justify your position.

Q35. Do you think there is merit for the characteristics of anti-dilution levy to differ between different investment strategies and between AIFs and UCITS? If yes, how?

2.2.9 Redemptions in kind

81. According to the AIFMD and UCITS Directive, redemption in kind means transferring assets held by the fund, instead of cash, to meet redemption requests of unit-holders or shareholders.

82. The AIFMD and the UCITS Directive sets out some conditions for the use of redemptions in kind.

83. For UCITS, redemption in kind shall only be activated to meet redemptions requested by professional investors and if the redemption in kind corresponds to a pro rata share of the assets held by the UCITS. However, the redemption in kind needs not to correspond to a pro rata share of the assets held by the UCITS if that UCITS is solely marketed to professional investors, or if the aim of that UCITS' investment policy is to replicate the composition of a certain stock or debt securities index and that UCITS is an ETF. For AIFs, the conditions are the same as for UCITS.

84. This means that when redemptions in kind are used, the liquidity structure of the fund shall be maintained, and professional investors shall receive securities/assets that correspond to a pro rata share of their holdings in the fund. However, if the fund is solely marketed to professional investors or if the fund is an ETF and its investment strategy is to replicate a certain stock or debt securities, professional investors may receive securities/assets that do not correspond to a pro rata share of their holdings.

85. Therefore, the characteristics of redemptions in kind would include:

    - Redemptions in kind allows funds to avoid the sale of sizable blocks of securities in response to redemption requests and avoid significant transaction costs and market price impact, and protect remaining investors.
    - Redemptions in kind shall only be used to meet redemption requests from professional investors.

- If the fund is solely marketed to professional investors or if the investment policy of the fund is to replicate the composition of a certain stock or debt securities index and that fund is an ETF fund, fund managers are not required to transfer assets to professional investors on a pro rata basis of the assets held by the fund. The same type of transfer of assets (i.e pro rata share or not) shall apply to all redeeming investors.

86. ESMA is of the view that the RTS on redemption in kind shall be the same for AIFMD and the UCITS Directive.

Q36. Do you agree with the description of redemptions in kind and the corresponding characteristics? If not, please justify your position.

Q37. Can you think of any characteristics of redemptions in kind?

Q38. Do you think there is merit for the characteristics of redemption in kinds to differ between different investment strategies between AIFs and UCITS? If yes, how?

2.2.10 Side pockets

87. According to the revised AIFMD and UCITS Directive, side pockets mean separating certain assets, whose economic or legal features have changed significantly or become uncertain due to exceptional circumstances, from the other assets of the fund.

88. The revised AIFMD and UCITS Directive provide that side pockets are possible for both UCITS and AIFs. Side pockets are not part of the two LMTs that AIFMs and UCITS shall at least select but are always available to investment funds and their fund managers.

89. As far as UCITS are concerned, the revised UCITS Directive also clarifies that, where a UCITS activates side pockets as referred to in Article 84(2), point (a), by means of asset separation, the separated assets may be excluded from the calculation of limits laid down in Chapter VII on "Obligations concerning the investment policies of UCITS".

- Characteristics of side pockets

90. Two forms of side pockets would then be possible:

- Physical separation, under which
  - Either the assets for which there are valuation issues or legal uncertainty are transferred into a new fund, while the remaining assets, for which there are no issues, remain in the existing fund; or
  - the assets for which there are valuation issues or legal uncertainty remain in the existing fund, while the assets for which there are no issues are transferred into a new fund.

- Accounting segregation with assets for which there are valuation issues or legal uncertainty allocated to a dedicated share class of the fund.

91. However, regarding the creation of a side pocket via physical separation, ESMA is of the view that the process shall differ between UCITS and AIFs. Indeed, according to Article 1(5) of the UCITS Directive, Member States shall prohibit UCITS which are subject to this Directive from transforming themselves into collective investment undertakings which are not covered by this Directive. This means, that it should not be possible for a UCITS to create a side pocket via physical separation by placing the assets for which there are problems into a new fund created for the purpose of the side pocket.

92. Therefore, in the case of UCITS, side pockets with physical separation of the assets shall only be done as follows:

    - The assets for which there are no issues are transferred to a new UCITS created for the purpose of the operation (or merged into an existing UCITS); and
    - The assets for which there are problems remain in the original UCITS that is closed for redemptions and subscriptions and put into liquidation.

93. However, in the case of AIFs, AIFMs shall have the discretion to either transfer the assets for which there is an issue in a new fund (i.e. the side pocket) and keep the original AIF with the rest of the portfolio of assets for which there is no issue or do the opposite (i.e. assets with no issues going into a new AIF created for the purpose of the operation and the assets for which there are problems remain in the original AIF that is closed for redemptions and subscriptions and put into liquidation).

94. The other characteristics of side pockets would be (for both physical separation and accounting segregation):

    - The side pocket shall be closed-ended.
    - Investors shall receive shares/units of the side pockets on a pro rata-basis of their holdings in the original fund.
    - The fund manager shall manage the side pockets with the sole objective of being liquidated.
    - Cash resulting from the sale of assets located in the side pocket shall not be reinvested and paid to investors.
    - The fund manager shall allocate a proportion of liquid assets to the side pocket in order to fulfil any possible liabilities arising from the management of the side pocket.
    - The fund manager shall manage the rest of the fund according to the disclosed investment strategy.

- New subscriptions and redemptions in the fund shall be executed on the basis of the assets of the funds from which assets of the side pocket are excluded.

95. Except for the creation of side pockets with physical separation where there is a difference between UCITS and AIFs, ESMA is of the view that all the other characteristics of side pockets shall be the same between UCITS and AIFs.

Q39. Do you agree with the description of side pockets and the corresponding characteristics? If not, please justify your position.
Q40. Do you agree that in the case of UCITS, side pockets created by physical separation should only be done with the creation of a new UCITS where the assets for which there are no problems are placed? If not, please explain your position.

Q41. Can you think of any other characteristics of side pockets that ESMA should consider? In particular, do you think that the characteristics of side pockets shall differ between UCITS and AIFs (in addition to the creation of side pockets via physical separation of the assets)? If, yes please elaborate.

Q42. Do you see merit in specifying further the characteristics that side pocket created by means of accounting segregation should have? If yes, can you please explain how you have created side pocket via accounting segregation? Have you encountered any legal constraints or are you aware of any legal constraints in your jurisdiction that may limit the use of side pockets via asset segregation?

Q43: Do you agree that the assets in the side pocket should always be managed with the view to liquidate them? Or could there be circumstances, where a reintegration with the normal assets could be contemplated? Please explain.

3 Annexes

3.1 Annex I

Summary of questions

Q1. Do you agree with the proposed characteristics of suspension of subscriptions, repurchases and redemptions? If not, please justify your position.

Q2. Do you agree that orders that have been placed but not executed before the fund manager suspends shall not be executed until the suspension is lifted? If not, please explain why these orders shall be executed.

Q3. Once the fund is reopened for subscriptions, repurchases and redemptions, what would be your approach to redemption orders that have not been executed before the fund was suspended?

Q4. Do you think there are circumstances where subscriptions, repurchases and redemptions may not be reopened simultaneously? If yes, what are these circumstances?

Q5. Can you think of any further characteristics of suspension of subscriptions, repurchases and redemptions?

Q6. Do you think there is merit for the characteristics of suspension of subscriptions, repurchases and redemptions gates to differ between different investment strategies and between AIFs and UCITS? If yes, how?

Q7. Do you agree with the description of redemption gates and their characteristics? If not, please justify your position.

Q8. The draft RTS provides that the redemption gate threshold shall be expressed as a percentage of the NAV of the fund considering the net redemption orders for a given dealing day. Are you aware of any other method that ESMA should consider in the RTS? If yes, please explain.

Q9. Do you agree that redemption gates may be either activated automatically when the activation threshold is exceeded or that the fund manager/ fund Boards may decide whether or not to activate the redemption gate? Do you believe that automatic activation of redemption gates could create a first mover advantage?

Q10. Do you think that the automatic activation of redemption gates shall not be permitted for some types of funds. If yes, please explain your position.

Q11. Do you agree that the activation threshold shall not be expressed at the level of the single redemption order? If not, please justify your position.

Q12. In the case of activation of redemption gates, do you agree that investors should have the right to cancel the non-executed part of their redemption orders? In particular, should there be a different approach between UCITS and AIFs?

Q13. Do you think there is merit in having different characteristics of redemption gates for different investment strategies and between AIFs and UCITS? If yes, how?

Q14. In the case of funds with multiple share classes, do you agree that the same redemption gate shall apply to all share classes? If not, please justify your position.

Q15. Can you think of any further characteristics of redemption gates?

Q16. Do you agree with the description of extensions of notice period and their characteristics? If not, please justify your position.

Q17. Do you agree that the same extension of notice period shall apply to all investors or different extensions of notice periods per share class/unit shall be allowed? Please justify your position.

Q18. Do you agree that extensions of notice period may be applied for a pre-defined period of time (for a pre-defined number of dealing dates)? If not, please justify your position.

Q19. Do you think there is merit for the characteristics of extensions of notice period to differ between different investment strategies and between AIFs and UCITS? If yes, how?

Q20. How would you execute redemption orders that have been placed but not executed before the notice period is extended? Would you execute them under the original notice period, or would you execute them at the following dealing day?

Q21. How would you ensure fair treatment of investors when deactivating the extension of notice period?

Q22.Do you agree with the description of redemption fees and the corresponding characteristics? If not, please justify your position.

Q23.Can you think of any other redemption fee mechanism than the ones described above? If yes, please provide examples.

Q24. Do you think there is merit for the characteristics of redemption fees to differ between different investment strategies and between AIFs and UCITS? If yes, how?

Q25. Do you agree with the description of swing pricing and the corresponding characteristics? If not, please justify your position.

Q26. Can you think of any characteristics of swing pricing that the ones described above?

Q27. Do you think there is merit for the characteristics of swing pricing to differ between different investment strategies and between AIFs and UCITS? If yes, how?

Q28. Do you agree that in the case of funds with multiple share classes, the same swing factor shall be applied to all share classes? If not, please justify your position.

Q29. Do you agree with the description of the dual pricing and the corresponding characteristics? If not, please justify your position.

Q30. Are there any other calculation methods for dual pricing that should be considered? If yes, please give example.

Q31. Do you think there is merit for the characteristics of dual pricing to differ between different investment strategies and between AIFs and UCITS? If yes, how?

Q32. Do you agree with the description of the anti-dilution levy and the corresponding characteristics? If not, please justify your position.

Q33. Are there any other calculation methods for anti-dilution levy that ESMA shall consider? If yes, please give example.

Q34. In the case of funds with multiple share classes, would you see the possibility for different anti-dilution levies depending on share classes? Please justify your position.

Q35. Do you think there is merit for the characteristics of anti-dilution levy to differ between different investment strategies and between AIFs and UCITS? If yes, how?

Q36. Do you agree with the description of redemptions in kind and the corresponding characteristics? If not, please justify your position.

Q37. Can you think of any characteristics of redemptions in kind?

Q38. Do you think there is merit for the characteristics of redemption in kinds to differ between different investment strategies between AIFs and UCITS? If yes, how?

Q39. Do you agree with the description of side pockets and the corresponding characteristics? If not, please justify your position.

Q40. Do you agree that in the case of UCITS, side pockets created by physical separation should only be done with the creation of a new UCITS where the assets for which there are no problems are placed? If not, please explain your position.

Q41. Can you think of any other characteristics of side pockets that ESMA should consider? In particular, do you think that the characteristics of side pockets shall differ between UCITS and AIFs (in addition to the creation of side pockets via physical separation of the assets)? If, yes please elaborate.

Q42. Do you see merit in specifying further the characteristics that side pocket created by means of accounting segregation should have? If yes, can you please explain how you have created side pocket via accounting segregation? Have you encountered any legal constraints or are you aware of any legal constraints in your jurisdiction that may limit the use of side pockets via asset segregation?

Q43: Do you agree that the assets in the side pocket should always be managed with the view to liquidate them? Or could there be circumstances, where a reintegration with the normal assets could be contemplated? Please explain.

Q44. Do you agree with the above-mentioned reasoning in relation to the possible costs and benefits of the option taken by ESMA as regards the characteristics of LMTs set out in Annex IIA of the UCITS Directive? Which other types of costs or benefits would you consider in that context?

Q45. Is there any ESG and innovation-related aspects that ESMA should consider when drafting the RTS under the UCITS Directive?

Q46. Do you agree with the above-mentioned reasoning in relation to the possible costs and benefits of the option taken by ESMA as regards the characteristics of LMTs set out in Annex V of the AIFMD? Which other types of costs or benefits would you consider in that context?

Q47. Is there any ESG and innovation-related aspects that ESMA should consider when drafting the RTS under the AIFMD?

3.2 Annex II

Legislative mandate to develop technical standards

- Article 16(2)(g) of AIFMD

"ESMA shall develop draft regulatory technical standards to specify the characteristics of the liquidity management tools set out in Annex V.

When developing those draft regulatory technical standards, ESMA shall take account of the diversity of investment strategies and underlying assets of AIFs. Those standards shall not restrict the ability of AIFMs to use any appropriate liquidity management tool for all asset classes, jurisdictions and market conditions".

- Article 18a (3) of the UCITS Directive

"ESMA shall develop draft regulatory technical standards to specify the characteristics of the liquidity management tools set out in Annex IIA.

When developing those draft regulatory technical standards, ESMA shall take account of the diversity of investment strategies and underlying assets of UCITS. Those standards shall not restrict the ability of UCITS to use any appropriate liquidity management tool for all asset classes, jurisdictions and market conditions."

3.3 Annex III

Cost-benefit analysis

1. Introduction

The revised UCITS Directive and the AIFMD establish a list of Liquidity Management Tools that shall be available to UCITS and AIFs. The list of LMTs and their definitions are the same in both Directives.

This consultation paper sets out proposals for the RTS specifying the characteristics of these LMTs.

This draft cost-benefit analysis (CBA) is qualitative by nature. Should relevant data be received through the consultation process, ESMA will take it into account when finalising the RTS and will include it in the CBA accompanying the final report.

2. Technical options on the characteristics of LMTs

The following options were identified and analysed by ESMA to address the policy objectives of the RTS under the UCITS Directive and the AIFMD.

In identifying the options set out below and choosing the preferred ones, ESMA was guided by the relevant rules of the UCITS Directive and the AIFMD.

- Draft RTS under Article 18a (3) of the UCITS Directive

Policy objective	
Baseline scenario	The baseline scenario should be understood for this CBA as the application of the requirements set out in the UCITS Directive (i.e. the provision on LMTs) without any further specification. This would leave NCAs and also management companies complete discretion to determine the precise characteristics of LMTs. This could clearly lead to a lack of harmonisation in the application of a key provision in the UCITS Directive. The main benefit of the RTS is to establish harmonised characteristics of the LMTs listed in Annex IIA of the UCITS Directive. Such harmonisation will contribute to the uniformed application of the legislation by management companies and to supervisory convergence

	between NCAs. This will ultimately also participate to increasing investor protection and financial stability in the EU.
Options	The RTS aim to promote the objectives of the Level 1 Directive by setting out the exact characteristics of LMTs. This should contribute to the creation of a level playing field across member States, which will help ensure that LMTs are used in a consistent manner by management companies. This should reduce the scope for regulatory arbitrage, which could otherwise hamper the key objectives of the Level 1 Directive.
Option 1	Do not develop RTS and rely only on the requirements set out in the UCITS Directive.
Option 2	The RTS would provide high level characteristics for each LMT and would leave to national legislations and/or market practices to determine the exact characteristics.
Option 3	The RTS would provide detailed characteristics, distinguishing, if applicable, between investment strategies and UCITS and AIFs.
Preferred option	ESMA decided to consult on Option 3 and discarded Option 1 and 2. Option 3 is the option in which the level of prescriptiveness of the characteristics of LMTs is high, ensuring a high level of convergence and harmonisation, in the context of the requirements set in the UCITS Directive and the corresponding RTS empowerments for ESMA. ESMA also included specific dedicated questions to stakeholders on certain alternative characteristics, such as the method for determining the redemption gate threshold or the merit in distinguishing the characteristics according to investment strategies.

- Draft RTS under Article 16(2)(g) of AIFMD

Policy objective	
Baseline scenario	The baseline scenario should be understood for this CBA as the application of the requirements set out in the AIFMD (i.e. the provision on LMTs) without any further specification. This would leave NCAs and

	also AIFMs complete discretion to determine the precise characteristics of LMTs. This could clearly lead to a lack of harmonisation in the application of a key provision in the AIFMD. The main benefit of the RTS is to establish harmonised characteristics of the LMTs listed in Annex V of AIFMD. Such harmonisation will contribute to the uniformed application of the legislation by management companies and to supervisory convergence between NCAs. This will ultimately also participate to increasing investor protection and financial stability in the EU.
Option 1	Do not develop RTS and rely only on the requirements set out in the AIFMD.
Option 2	The RTS would provide high level characteristics for each LMT and would leave to national legislations and/or market practices to determine the exact characteristics.
Option 3	The RTS would provide detailed characteristics, distinguishing, if applicable, between investment strategies and between UCITS and AIFs.
Preferred option	ESMA decided to consult on Option 3 and discarded Option 1 and 2. Option 3 is the option in which the level of prescriptiveness of the characteristics of LMTs is high, ensuring a high level of convergence and harmonisation, in the context of the requirements set in the UCITS Directive and the corresponding RTS empowerments for ESMA. ESMA also included specific dedicated questions to stakeholders on certain alternative characteristics, such as the method for determining the redemption gate threshold or the merit in distinguishing the characteristics according to investment strategies.

3. Assessment of the impact of the various options on the characteristics of LMTs

- Draft RTS under Article 18a(3) of the UCITS Directive

Options	Qualitative description
Benefits	The main benefit of the proposed option is to provide a great level of harmonization and prescriptiveness for the characteristics of LMTs, contributing to the creation of a level playing field across Member States.
Costs	ESMA took the view that the proposed approach was unlikely to lead to significant additional costs to the extent that it provided clarifications on the Level 1 provisions and does not impose additional obligations beyond those already set by the UCITS Directive in relation to the use of LMTs.
Costs to regulator	The proposed approach will lead to additional costs for regulators, in particular with respect to the ongoing supervision of the liquidity management of UCITS but the benefits of such tasks, in terms of mitigation of any investor protection and financial stability related issues related to UCITS, clearly outweigh these costs.
Compliance costs	Compared with the current framework, the proposed approach will add certain compliance costs for management companies, in particular in relation to the supervision of their liquidity management, but the benefits of such duties, in terms of mitigation of any investor protection and financial stability related issues related to UCITS, clearly outweigh these costs.
ESG-related aspects	ESG-related aspects are not of direct relevance to the specific nature of the proposed RTS on the characteristics of LMTs, as well as, to the draft Guidelines on LMTs for UCITS and open-ended AIFs.
Innovation-related aspects	Innovation-related aspects are not of direct relevance to the specific nature of the proposed RTS on the characteristics of LMTs.
Proportionality-related aspects	The identified benefits outweigh the comparably limited costs, hence no proportionality-related aspects are expected to be impacted by this option.

Q44. Do you agree with the above-mentioned reasoning in relation to the possible costs and benefits of the option taken by ESMA as regards the characteristics of LMTs set out in Annex IIA of the UCITS Directive? Which other types of costs or benefits would you consider in that context?

Q45. Is there any ESG and innovation-related aspects that ESMA should consider when drafting the RTS under the UCITS Directive?

- Draft RTS under Article 16(2)(g) of AIFMD

Options	Qualitative description
Benefits	The main benefit of the proposed option is to provide a great level of harmonization and prescriptiveness for the characteristics of LMTs, contributing to the creation of a level playing field across Member States.
Costs	ESMA took the view that the proposed approach was unlikely to lead to significant additional costs to the extent that it provided clarifications on the Level 1 provisions and does not impose additional obligations beyond those already set by the AIFMD in relation to the use of LMTs.
Costs to regulator	The proposed approach will lead to additional costs for regulators, in particular with respect to the ongoing supervision of the liquidity management of AIFs but the benefits of such tasks, in terms of mitigation of any investor protection and financial stability related issues related to AIFs, clearly outweigh these costs.
Compliance costs	Compared with the current framework, the proposed approach will add certain compliance costs for management companies, in particular in relation to the supervision of their liquidity management, but the benefits of such duties, in terms of mitigation of any investor protection and financial stability related issues related to AIFs, clearly outweigh these costs.
ESG-related aspects	ESG-related aspects are not of direct relevance to the specific nature of the proposed RTS on the characteristics of LMTs.

Innovation-related aspects	Innovation-related aspects are not of direct relevance to the specific nature of the proposed RTS on the characteristics of LMTs.
Proportionality-related aspects	The identified benefits outweigh the comparably limited costs, hence no proportionality-related aspects are expected to be impacted by this option.

Q46. Do you agree with the above-mentioned reasoning in relation to the possible costs and benefits of the option taken by ESMA as regards the characteristics of LMTs set out in Annex V of the AIFMD? Which other types of costs or benefits would you consider in that context?

Q47. Is there any ESG and innovation-related aspects that ESMA should consider when drafting the RTS under the AIFMD?

3.4 Annex IV

Draft technical standards under the AIFMD

COMMISSION DELEGATED REGULATION (EU) …/..

of […]

supplementing Directive 2011/61/EU of the European Parliament and of the Council with regard to regulatory technical standards specifying the characteristics of liquidity management tools

(Text with EEA relevance)

THE EUROPEAN COMMISSION,

Having regard to the Treaty of the Functioning of the European Union,

Having regard to Directive 2011/61/EU of the European Parliament and of the Council on Alternative Investment Fund Managers, and in particular Article 16(2)(g),

Whereas,

(1) Suspensions of subscriptions, repurchases and redemptions are not part of the two liquidity management tools that AIFMs shall at least select according to Article 16(2)(b) of Directive 2011/61/EU. AIFMs should be able to use suspensions of subscriptions, repurchases and redemptions, in exceptional circumstances, and where justified having regard to the interests of the AIF's shareholders or unit-holders.

(2) Suspensions of subscriptions should apply simultaneously to suspensions of repurchases and redemptions and for the same period of time.

(3) The use of suspensions of subscriptions, repurchases and redemptions, should be temporary and accompanied with a plan for the future of the AIF. In particular, after suspensions of subscriptions, repurchases and redemptions are lifted there could be a number

of possible outcomes, including, reopening the AIF for subscriptions, repurchases and redemptions, the AIFM deciding to create a side pocket or put the AIF into liquidation.

(4) With regard to redemption gates, in order to ensure a consistent use of redemption gates by AIFMs, the characteristics should address the method for determining the activation threshold and the treatment of the non-executed part of redemption orders resulting from the use of redemption gates. The method for determining the activation threshold should consist in considering all redemption orders for a given dealing date and the non-executed part of redemption orders should be automatically transferred to the next dealing date.

(5) When AIFMs activate redemption gates, shareholders or unit-holders should have the right to withdraw that part of their redemption order(s) that has not been executed.

(6) Regarding the activation of redemption gates, given the variety of investment strategies and the fact that some AIFs may have very frequent dealing dates, including daily dealing dates, AIFMs should have the flexibility to determine whether or not to automatically activate redemption gates when the activation threshold is exceeded.

(7) With regard to extensions of the notice period, they should not have any impact on the dealing frequency of the fund. This means that if the notice period of a fund is extended, the dealing frequency of AIFs should not be modified, and AIFs should continue to offer the same dealing frequency to their shareholders or unitholders.

(8) The extension of notice period should be the period of time that is added to the minimum notice period that investors or unit-holders should respect when placing their redemption orders.

(9) Regarding redemptions fees they should impose on redeeming shareholders or unit-holders the estimated explicit and implicit costs of portfolio transactions caused by redemptions, including any estimated significant market impact of assets sales to meet those redemptions.

(10) Redemption fees should be based on individual redemption orders and should be deducted from the amount of the money paid to redeeming investors for the benefit of the fund.

(11) Swing pricing should be composed of a swing factor whose purpose should be to impose on redeeming and subscribing shareholders or unit-holders the estimated explicit and implicit costs of portfolio transactions caused by subscriptions or redemptions, including any significant market impact of assets purchases or sales to meet those subscriptions or redemptions.

(12) When swing pricing is activated, the NAV of the AIF should be adjusted to incorporate the swing factor and the NAV published by the AIFM should be the NAV with the application of the swing factor.

(13) AIFMs selecting swing pricing may decide to adjust the NAV of the fund on every dealing date for which there is a net activity of any size between redemptions or subscriptions (commonly referred to as “full swing”) or only when the net redemptions or subscriptions are greater than a predetermined swing threshold (commonly referred to as “partial swing”). Under both types of swing pricing, the direction of the swing (i.e., whether the swing factor is added to or deducted from the NAV) should be determined by the net capital activity of the dealing date. Therefore, for a given dealing date, if the net difference between redemptions and subscriptions results in net subscriptions, the swing factor would be added to the NAV that will be adjusted upward. On the contrary, for a given dealing date, if the net difference between redemptions and subscriptions results in net redemptions, a swing factor would be deducted from the NAV that will hence be adjusted downward. Under both types of swing pricing, a fund manager may decide to have either a single swing factor or apply progressively increasing swing factors depending on the net capital activity (commonly referred to as “tiered approach“). A tiered approach intends to account for increased activities in redemptions and subscriptions that generate higher transaction costs in relative terms when transactions costs increase more rapidly than the net capital activity of the AIF.

(14) Regarding dual pricing AIFMs should have the possibility to choose between two methods. One method should consist in calculating one NAV which incorporates assets’ ask prices and the other NAV which incorporates assets’ bid prices for subscribing investors to pay the NAV calculated using ask asset prices and redeeming investors receive the NAV calculated using bid asset prices. The other method should consist in setting an ‘adjustable spread’ around the fund’s NAV under which assets are priced on a mid-market basis, with a bid price at which the fund redeems shares and an offer price at which the fund issues new shares. The difference between these two prices is known as the spread as estimated by the fund manager, which could be dynamic to reflect the liquidity costs in prevailing market conditions.

(15) Anti-dilution levies should impose on redeeming and subscribing shareholders or unit-holders the estimated explicit and implicit costs of portfolio transactions caused by subscriptions or redemptions, including any estimated significant market impact of assets purchases or sales to meet those subscriptions or redemption. Anti-dilution levies should be charged to redeeming or subscribing investors in the case the number of redemptions exceed the number of subscriptions, or vice-versa, resulting in a change in the net assets or liabilities of the funds.

(16) Regarding redemptions in kind, they should only be available for redemption orders placed by professional investors and executed on a pro rata basis of their assets held by the AIFs.

AIFMs may derogate from the obligation to execute redemption in kind on a pro rata basis only if the AIF is solely marketed to professional investors or if the aim of the AIF's investment policy is to replicate the composition of a certain stock or debt securities index and that the AIF is an exchange-traded fund as defined in Article 4(1), point (46), of Directive 2014/65/EU.

(17) When AIFMs decide to execute redemption orders from professional investors in kind, they should apply the same method to all redeeming investors.

(18) Regarding side pockets, AIFMs should have the possibility to choose between physical separation of the assets, for which there are valuation issues or legal uncertainty, or accounting segregation.

(19) For side pockets created with physical separation, assets for which there are valuation issues or legal uncertainty should either be transferred into a new fund or remain in the original AIF. For side pockets created with accounting segregation assets for which there are valuation issues or legal uncertainty are allocated to a dedicated share class of the AIF.

(20) The same characteristics should apply to both types of side pockets. Once created, side pockets should be closed for subscriptions and redemptions and should be managed with the sole purpose of being liquidated. Cash resulting from the sales of these assets should not be reinvested by AIFMs.

21) AIFMs may use other tools than the ones referred to in Annex V of Directive 2011/61/EU to manage the liquidity of the AIFs they manage but these other tools should not be considered as liquidity management tools for the purpose of complying with the obligation to select at least two liquidity management tools under Article 16(2)(b) of Directive 2011/61/EU.

Article 1

Suspension of subscriptions, repurchases and redemptions

1. Suspensions of subscriptions shall apply simultaneously, and for the same period of time, to suspensions of repurchases and redemptions.
2. Suspensions of subscriptions, repurchases and redemption shall apply to all shareholders or unitholders.
3. In the case of AIFs with multiple share classes, the suspension of subscriptions, repurchases and redemptions shall apply to all the share classes of the AIFs.
4. Subscriptions, repurchases and redemptions orders that have been placed, but not executed before the subscriptions, repurchases and redemptions of the AIF are

suspended, shall not be executed before AIF is reopened for subscriptions, repurchases and redemptions.

Article 2

Redemption gates

1. A redemption gate shall include an activation threshold predefined as the net redemption orders an AIF receives for a given dealing date in proportion to the NAV of the AIF.
2. When the net redemption orders for a given dealing date exceeds the activation threshold, the redemption gate may be automatically activated or at the discretion of the AIFM or fund Board if applicable.
3. When the activation threshold is exceeded, the AIFM or fund Board may decide to execute all redemptions orders in full, at the condition that the full execution of the redemption orders is compatible with the liquidity structure of the AIF, that it applies equally to all redeeming shareholders or unitholders, and that the interest of non-redeeming investors is preserved.
4. When a redemption gate is activated, the same level of redemption gate shall apply to all redeeming shareholders or unit-holders in proportion to their redemption orders.
5. When a redemption gate is activated, the non-executed part of the redemption orders shall be carried forward to the following dealing date unless the shareholders or unitholders have requested the cancellation of the non-executed part of their redemption orders.
6. Non-executed parts of redemption orders that are carried forward to the next dealing date may have priority over redemptions orders submitted for the following dealing date.
7. The characteristic set out in paragraph 1 of this Article shall not apply to European Long-Term Investment Funds set out under Regulation 2015/760 for which the characteristics of the activation threshold of redemption gates are defined in Article 18 (2) (d) of Regulation 2015/760 and in article XYZ of Delegated Regulation (insert the final reference).

Article 3

Extension of notice periods

1. The extension of notice periods shall be the period of time added to the normal notice period that shareholders or unit-holders shall respect when placing their redemption order.
2. The same extension of the notice period shall apply to all shareholders or unit-holders of the AIF.

3. In the case of AIFs with multiple share classes, the same extension of the notice period shall apply to all share classes.
4. If the AIFM or the fund Board extends the notice period, it shall not accept redemption orders that have been placed after the extension of the notice period that do not comply with the extension of the notice period.
5. Extensions of notice periods may apply to a pre-defined number of dealing dates.

Article 4

Redemption fees

1. Redemption fees are predetermined fees charged to redeeming shareholders or unit-holders and which are deducted from the amount paid to shareholders or unit-holders as the result of the execution of their redemption orders.
2. Redemption fees shall impose on redeeming shareholders or unit-holders the explicit and implicit estimated costs of portfolio transactions caused by redemptions, including any estimated significant market impact of assets sales to meet those redemptions.
3. Redemption fees shall be levied in favour of the AIF.
4. Redemption fees shall be expressed as a percentage of the redemption orders of the shareholders or unit-holders and may be expressed as a range with a minimum and a maximum percentage.
5. Redemption fees may be applied irrespective of the amount of individual redemption orders or contingent on the size of the redemption order.
6. AIFs may have different levels of redemption fees based on the size of redemptions orders.
7. Shareholders or unit-holders that have placed redemption orders that fall within the same level of redemption fees shall bear the same redemption fee.

Article 5

Swing pricing

1. Swing pricing shall include a swing factor expressed as a percentage of the NAV of the AIF.
2. The swing factor shall impose on redeeming and subscribing shareholders or unit-holders the explicit and implicit estimated costs of portfolio transactions costs caused by

subscriptions or redemptions, including any estimated significant market impact of assets purchases or sales to meet those subscriptions or redemptions.

3. If the difference between the redemption orders and the subscription orders, for a given dealing date results in net redemptions, the NAV of the AIF at which all shareholders or unit-holders transact, shall be adjusted by deducting the swing factor from the NAV of the AIF.
4. If the net difference between the redemption orders and the subscriptions orders, for a given dealing date results in net subscriptions, the NAV of the AIF at which all shareholders or unit-holders transact, shall be adjusted by adding the swing factor to the NAV of the AIF.
5. AIFMs may apply swing pricing each time there is a net change in the number of shares of the AIF (*full swing*) or if the net change exceeds a certain predefined threshold referred to as a trigger threshold (*partial swing*).
6. AIFMs using swing pricing may have different swing factors corresponding to different trigger thresholds.
7. In the case of AIFs with multiple share classes, the swing factor(s) and the trigger threshold(s) shall be the same for all shareholders and unit-holders.

Article 6

Dual pricing

1. At the discretion of the AIFM or fund Board as applicable, dual pricing shall consist of one of the two following calculation methods:
    a. The AIF has two NAVs with one NAV calculated using the ask prices of the assets in which the AIF is invested and one NAV calculated using the bid prices of the assets in which the AIF is invested. Subscribing shareholders or unit-holders shall subscribe on the basis of the NAV calculated according to the ask prices and redeeming shareholders or unit-holders shall redeem on the basis of the NAV calculated according to the bid prices.
    b. The AIF has one NAV that is adjusted by a factor that reflects the cost of liquidity. Subscribing shareholders or unit-holders shall subscribe on the basis of the NAV to which is added the adjusted factor and redeeming shareholders or unit-holders shall redeem on the basis of the NAV to which the adjusted factor is deducted.
2. The same calculation method, as described in paragraph 1) shall apply to all shareholders or unit-holders.

3. In the case of AIFs with multiple share classes, the AIFM shall apply the same calculation method to all share classes.

Article 7

Anti-dilution levy

1. Anti-dilution levies shall impose on redeeming and subscribing shareholders or unit-holders the explicit and implicit estimated costs of portfolio transactions caused by subscriptions or redemptions, including any significant market impact of assets purchases or sales to meet those subscriptions or redemptions.
2. If the net difference between the redemption orders and the subscription orders, for a given dealing day results in net redemptions, an anti-dilution levy is deducted from the amount paid to redeeming shareholders or unit-holders as per the execution of redemption orders.
3. If the net difference between the redemption orders and the subscription orders, for a given dealing day results in net subscriptions, an anti-dilution levy is charged to subscribing shareholders or unit-holders. I
4. Anti-dilution levies may include a trigger threshold determined in advance by the AIFM or the fund Board as applicable. In the case of an anti-dilution levy with a trigger threshold, the anti-dilution levy shall be applied only if the net difference between the redemption orders and the subscription orders, for a given dealing date, exceeds the trigger threshold.
5. AIFMs or fund Boards as applicable may decide to apply the same anti-dilution levy to transacting shareholders or unit-holders or to charge the transacting shareholders or unit-holders with the exact transaction costs resulting from their redemption orders.

Article 8

Redemptions in kind

1. Redemptions in kind allow funds to avoid the sale of sizable blocks of securities in response to redemption requests and avoid significant transaction costs and market price impact, and protect remaining investors.
2. Redemptions in kind shall only be used to meet redemption requests from professional investors.
3. If the AIF is solely marketed to professional investors or if the investment policy of the AIF is to replicate the composition of a certain stock or debt securities index and that AIF is an

ETF fund, AIFMs or the fund Board as applicable may decide whether they transfer assets to professional investors on a pro rata basis of the assets held by the AIF. AIFMs shall apply the same type of transfer of assets (i.e., pro rata share of each asset or not) to all redeeming professional investors for a given AIF.

Article 9

Side pockets

1. Side pockets shall take the form of:
    a. A specific share class(es) of the AIF (*accounting segregation*); or
    b. A fund where the assets for which there are valuation issues or legal uncertainty are located (*physical segregation*).
2. For side pockets referred to in paragraph 1 b) of this Article, AIFMs may decide to keep the assets for which there are no valuation issues or legal uncertainty in the original AIF and transfer the assets for which there are valuation issue or legal uncertainty into a new fund created specifically for the purpose of this operation (or via a merger into an existing AIF). AIFMs may also decide to transfer the assets for which there are no valuation issues or legal uncertainty into a new AIF.
3. Shareholders or unit-holders shall receive shares or units of the side pocket pro rata of their holdings in the AIF.
4. Side pockets shall be closed-ended and AIFMs shall manage the side pockets with the sole objective of being liquidated.
5. AIFMs shall place within side pockets the amount of cash necessary for fulfilling future potential liabilities arising from the management of the side pocket.
6. Cash resulting from the potential sale of assets of the side pocket shall not be reinvested and shall be paid to shareholders or unitholders.
7. After the side pocket is created, AIFMs shall manage the AIF according to the AIF rules.
8. When a side pocket is created via accounting segregation, new subscriptions, redemptions and repurchases shall be executed on the basis of the NAV of the AIF from which assets for which there are valuation issues or legal uncertainty shall be excluded.

Article 10

Entry into force

This Regulation shall enter into force on the day following that of its publication in the *Official Journal of the European Union.*

It shall apply from […]

This Regulation shall be binding in its entirety and directly applicable in all Member States.

Done at Brussels,

3.5 Annex V

Draft regulatory technical standards under the UCITS Directive

COMMISSION DELEGATED REGULATION (EU) …/..

of […]

supplementing Directive 2009/65/EC of the European Parliament and of the Council with regard to regulatory technical standards specifying the characteristics of liquidity management tools

(Text with EEA relevance)

THE EUROPEAN COMMISSION,

Having regard to the Treaty of the Functioning of the European Union,

Having regard to Directive 2009/65/EC of the European Parliament and of the Council on Undertaking for Collective Investment in Transferable Securities, and in particular Article 18a(3),

Whereas,

(1) Suspensions of subscriptions, repurchases and redemptions are not part of the two liquidity management tools that AIFMs shall at least select according to Article 18a(2) of Directive 2009/65/EC. Management companies should be able to use suspensions of subscriptions, repurchases and redemptions, in exceptional circumstances, and where justified having regard to the interests of the AIF's shareholders or unit-holders.

(2) Suspensions of subscriptions should apply simultaneously to suspensions of repurchases and redemptions and for the same period of time.

(3) The use of suspensions of subscriptions, repurchases and redemptions, should be temporary and accompanied with a plan for the future of the UCITS. In particular, after suspensions of subscriptions, repurchases and redemptions are lifted there could be a number of possible outcomes, including, reopening the UCITS for subscriptions, repurchases and

redemptions, the management company deciding to create a side pocket or put the UCITS into liquidation.

(4) With regard to redemption gates, in order to ensure a consistent use of redemption gates by management companies, the characteristics should address the method for determining the activation threshold and the treatment of the non-executed part of redemption orders resulting from the use of redemption gates. The method for determining the activation threshold should consist in considering all redemption orders for a given dealing date and the non-executed part of redemption orders should be automatically transferred to the next dealing date.

(5) When management companies activate redemption gates, shareholders or unit-holders should have the right to withdraw that part of their redemption order(s) that has not been executed.

(6) Regarding the activation of redemption gates, given the variety of investment strategies and the fact that some UCITS may have very frequent dealing dates, including daily dealing dates, management companies should have the flexibility to determine whether or not to automatically activate redemption gates when the redemption gate threshold is exceeded.

(7) With regard to extensions of the notice period, they should not have any impact on the dealing frequency of the fund. This means that if the notice period of a fund is extended, the dealing frequency of the UCITS should not be modified, and the UCITS should continue to offer the same dealing frequency to their shareholders or unitholders.

(8) The extension of notice period should be the period of time that is added to the minimum notice period that investors or unit-holders should respect when placing their redemption orders.

(9) Regarding redemptions fees they should impose on redeeming shareholders or unit-holders the estimated explicit and implicit costs of portfolio transactions caused by redemptions, including any estimated significant market impact of assets sales to meet those redemptions.

(10) Redemption fees should be based on individual redemption orders and should be deducted from the amount of the money paid to redeeming investors for the benefit of the UCITS.

(11) Swing pricing should be composed of a swing factor whose purpose should be to impose on redeeming and subscribing shareholders or unit-holders the estimated explicit and implicit costs of portfolio transactions caused by subscriptions or redemptions, including any estimated

significant market impact of assets purchases or sales to meet those subscriptions or redemptions.

(12) When swing pricing is activated, the NAV of the UCITS should be adjusted to incorporate the swing factor and the NAV published by the management company should be the NAV with the application of the swing factor).

(13) Management companies selecting swing pricing may decide to adjust the NAV of the UCITS on every dealing date for which there is a net activity of any size between redemptions or subscriptions (commonly referred to as “full swing”) or only when the net redemptions or subscriptions are greater than a predetermined swing threshold (commonly referred to as “partial swing”). Under both types of swing pricing, the direction of the swing (i.e., whether the swing factor is added to or deducted from the NAV) should be determined by the net capital activity of the dealing date. Therefore, for a given dealing date, if the net difference between redemptions and subscriptions results in net subscriptions, the swing factor would be added to the NAV that will be adjusted upward. On the contrary, for a given dealing date, if the net difference between redemptions and subscriptions results in net redemptions, a swing factor would be deducted from the NAV that will hence be adjusted downward. Under both types of swing pricing, the management company may decide to have either a single swing factor or apply progressively increasing swing factors depending on the net capital activity (commonly referred to as “tiered approach“). A tiered approach intends to account for increased activities in redemptions and subscriptions that generate higher transaction costs in relative terms when transactions costs increase more rapidly than the net capital activity of the UCITS.

(14) Regarding dual pricing, management companies should have the possibility to choose between two methods. One method should consist in calculating one NAV which incorporates assets’ ask prices and the other NAV which incorporates assets’ bid prices for subscribing investors to pay the NAV calculated using ask asset prices and redeeming investors receive the NAV calculated using bid asset prices. The other method should consist in setting an ‘adjustable spread’ around the fund’s NAV under which assets are priced on a mid-market basis, with a bid price at which the UCITS redeems shares and an offer price at which the UCITS issues new shares. The difference between these two prices is known as the spread as estimated by the management company, which could be dynamic to reflect the liquidity costs in prevailing market conditions.

(15) Anti-dilution levies should impose on redeeming and subscribing shareholders or unit-holders the estimated explicit and implicit costs of portfolio transactions caused by subscriptions or redemptions, including any estimated significant market impact of assets purchases or sales to meet those subscriptions or redemption. Anti-dilution levies should be charged to redeeming or subscribing investors in the case the number of redemptions exceed

the number of subscriptions, or vice-versa, resulting in a change in the net assets or liabilities of the UCITS.

(16) Regarding redemptions in kind, they should only be available for redemption orders placed by professional investors and executed on a pro rata basis of their assets held by the UCITS. Management companies may derogate from the obligations to execute redemption in kind on a pro rata basis only if the UCITS is solely marketed to professional investors or if the aim of the UCITS' investment policy is to replicate the composition of a certain stock or debt securities index and that the UCITS is an exchange-traded fund as defined in Article 4(1), point (46), of Directive 2014/65/EU.

(17) When management companies decide to execute redemption orders from professional investors in kind, they should apply the same method to all redeeming investors.

(18) Regarding side pockets, management should have the possibility to choose between physical separation of the assets for which there are valuation issue or legal uncertainty or accounting segregation.

(19) According to Article 1(5) of the UCITS Directive, Member States shall prohibit UCITS which are subject to this Directive from transforming themselves into collective investment undertakings which are not covered by this Directive. Therefore, this means that for side pockets created with physical separation, it should not be possible for a UCITS to create a side pocket via physical separation by placing the assets for which there are problems into a new fund creating for the purpose of the side pocket.

(20) For side pockets created with accounting segregation assets for which there are valuation issues or legal uncertainty are allocated to a dedicated share class of the UCITS.

(21) The same characteristics should apply to both types of side pockets. Once created, side pockets should be closed for subscriptions and redemptions and should be managed with the sole purpose of being liquidated. Cash resulting from the sales of these assets should not be reinvested by the management company.

(22) Management companies may use other tools than the ones referred to in Annex IIA of Directive 2009/65/EC to manage the liquidity of the UCITS they manage but these other tools should not be considered as liquidity management tools for the purpose of complying with the obligation to select at least two liquidity management tools under Article 18a(2) of Directive 2009/65/EC.

Article 1

Suspension of subscriptions, repurchases and redemptions

1. Suspensions of subscriptions shall apply simultaneously, and for the same period of time, to suspensions of repurchases and redemptions.
2. Suspensions of subscriptions, repurchases and redemption shall apply to all shareholders or unitholders.
3. In the case of UCITS with multiple share classes, the suspension of subscriptions, repurchases and redemptions shall apply to all the share classes of the UCITS.
4. Subscriptions, repurchases and redemptions orders that have been placed, but not executed before the subscriptions, repurchases and redemptions of the UCITS are suspended, shall not be executed before the suspension of subscriptions, repurchases and redemptions is lifted.

Article 2

Redemption gates

1. A redemption gate shall include an activation threshold, predefined as the net redemption orders an UCITS receives for a given dealing day in proportion to the net asset value of the UCITS.
2. When the net redemption orders for a given dealing day exceeds the activation threshold, the redemption gate may be automatically activated or at the discretion of the management company.
3. When the activation threshold is exceeded, the management company may decide to execute all redemptions orders in full, at the condition that the full execution of the redemption orders is compatible with the liquidity structure of the UCITS, that and it applies equally to all redeeming shareholders or unitholders, and that the interest of non-redeeming investors is preserved.
4. When a redemption gate is activated, the same level of redemption gate shall apply to all redeeming shareholders or unit-holders in proportion of their redemption orders.
5. When a redemption gate is activated, the non-executed part of the redemption orders shall be carried forward to the following dealing day unless the shareholders or unit-holders have requested the cancellation of the non-executed part of their redemption orders.
6. Non-executed parts of redemption orders that are carried forward to the next dealing day may have priority over redemptions orders submitted for the following dealing day.

Article 3

Extension of notice periods

1. The extension of notice periods shall be the period of time added to the normal notice period that shareholders or unit-holders shall respect when placing their redemption order.
2. The same extension of the notice period shall apply to all shareholders or unit-holders of the UCITS.
3. In the case of UCITS with multiple share classes, the same extension of the notice period shall apply to all share classes.
4. If the management company extends the notice period, it shall not accept redemption orders that have been placed after the extension of the notice period that do not comply with the extension of the notice period.
5. Extensions of notice periods may apply to a pre-defined number of dealing days.

Article 4

Redemption fees

1. Redemption fees are fees charged to redeeming shareholders or unit-holders and which are deducted from the amount paid to shareholders or unit-holders as the result of the execution of their redemption orders.
2. Redemption fees shall impose on redeeming shareholders or unit-holders the explicit and implicit estimated costs of portfolio transactions caused by redemptions, including any estimated significant market impact of assets sales to meet those redemptions.
3. Redemption fees shall be levied in favour of the UCITS.
4. Redemption fees shall be expressed as a percentage of the redemption orders of the shareholders or unit-holders and may be expressed as range with a minimum and a maximum.
5. Redemption fees may be applied irrespective of the amount of individual redemption orders or contingent on the size of the redemption order.
6. UCITS may have different levels of redemption fees based on the size of redemptions orders.
7. Shareholders or unit-holders that have placed redemption orders that fall within the same level of redemption fees shall bear the same redemption fee.

Article 5

Swing pricing

1. Swing pricing shall include a swing factor expressed as a percentage of the NAV of the UCITS.
2. The swing factor shall impose on redeeming and subscribing shareholders or unit-holders the explicit and implicit estimated costs of portfolio transactions costs caused by subscriptions or redemptions, including any estimated significant market impact of assets purchases or sales to meet those subscriptions or redemptions.
3. If the difference between the redemption orders and the subscription orders, for a giving dealing day results in net redemptions, the NAV of the UCITS at which at all shareholders or unit-holders transact, shall be adjusted by deducting the swing factor from the NAV of the UCITS.
4. If the net difference between the redemption orders and the subscriptions orders, for a given dealing day results in net subscriptions, the NAV of the UCITS at which all shareholders or unit-holders transact, shall be adjusted by adding the swing factor added to the NAV of the UCITS.
5. Management companies may apply swing pricing each time there is a net change in the number of shares of the UCITS (full swing) or if the net change exceeds a certain predefined threshold referred to as a trigger threshold (partial swing).
6. Management companies using swing pricing may have different swing factors corresponding to different trigger thresholds.
7. In the case of UCITS with multiple share classes, the swing factor(s) and the trigger threshold(s) shall be the same for all shareholders and unit-holders.

Article 6

Dual pricing

1. At the discretion of the management company, dual pricing shall consist of one of the two following calculation methods:
    a. The UCITS has two NAVs with one NAV calculated using the ask prices of the assets in which the UCITS is invested and one NAV calculated using the bid prices of the assets in which the UCITS is invested. Subscribing shareholders or unit-holders shall subscribe on the basis of the NAV calculated according to the ask

prices and redeeming shareholders or unit-holders shall redeem on the basis of the NAV calculated according to the bid prices.

b. The UCITS has one NAV that is adjusted by a factor that reflects the cost of liquidity. Subscribing shareholders or unit-holders shall subscribe on the basis of the NAV to which is added the adjusted factor and redeeming shareholders or unit-holders shall redeem on the basis of the NAV to which the adjusted factor is deducted.

2. The same calculation method, as described in paragraph 1) shall apply to all shareholders or unit-holders.

3. In the case of UCITS with multiple share classes, the management company shall apply the same calculation method to all share classes.

Article 7

Anti-dilution levy

1. Anti-dilution levies shall impose on redeeming and subscribing shareholders or unit-holders the explicit and implicit estimated costs of portfolio transactions costs caused by subscriptions or redemptions, including any estimated significant market impact of assets purchases or sales to meet those subscriptions or redemptions.

2. If the net difference between the redemption orders and the subscription orders, for a given dealing day results in net redemptions, an anti-dilution levy is deducted from the amount paid to redeeming shareholders or unit-holders as per the execution of redemption orders.

3. If the net difference between the redemption orders and the subscription orders, for a given dealing day results in net subscriptions, an anti-dilution levy is charged to subscribing shareholders or unit-holders.

4. Anti-dilution levies may include a trigger threshold. In the case of an anti-dilution levy with a trigger threshold, the anti-dilution levy is applied only if the net difference between the redemption orders and the subscription orders, for a given dealing day, exceed a certain threshold set in advance by the management company.

5. Management companies may decide to apply the same anti-dilution levy to transacting shareholders or unit-holders or to charge the transacting shareholders or unit-holders with the exact transaction costs resulting from their redemption orders.

Article 8

Redemptions in kind

1. Redemption in kind allow funds to avoid the sale of sizable blocks of securities in response to redemption requests and avoid significant transaction costs and market price impact, and protect remaining investors.
2. Redemptions in kind shall only be used to meet redemption requests from professional investors.
3. If the UCITS is solely marketed to professional investors or if the investment policy of the UCITS is to replicate the composition of a certain stock or debt securities index and that UCITS is an ETF fund, management companies may decide whether they transfer assets to professional investors on a pro rata basis of the assets held by the UCITS. Management companies shall apply the same type of transfer of assets (i.e., pro rata share of each asset or not) to all redeeming professional investors for a given UCITS.

Article 9

Side pockets

1. Side pockets shall take the form of:
    a. A specific share class of the UCITS (*accounting segregation*); or
    b. A fund where the assets for which there are valuation issues or legal uncertainty are located (*physical segregation*).
2. For side pockets referred to in paragraph 1 b) of this Article, management companies shall suspend the subscriptions and redemptions of the UCITS and transfer the assets for which there are no valuation issues or legal uncertainty in a new UCITS created specifically for the purpose of this operation (or via a merger into an existing UCITS in so far as the merger complies with the requirements set out in Chapter VI of Directive 2009/65/EC).
3. In the case of the side pocket not created with a merger, the newly-created UCITS shall be authorised and managed according to investment strategy of the original UCITS.
4. Shareholders or unit-holders shall receive shares or units of the side pocket pro rata of their holdings in the UCITS.
5. Management companies shall place within the side pockets the amount of cash necessary for fulfilling future potential liabilities arising from the management of the side pocket. Cash resulting from the potential sale of assets of the side pocket shall not be reinvested and shall be paid to shareholder or unitholders.

6. Side pockets shall be closed-ended and management companies shall manage side pockets with the sole objective of being liquidated.
7. After the side pocket is created, management companies shall manage the UCITS according to the UCITS rules.
8. When a side pocket is created via accounting segregation, new subscriptions, redemptions and repurchases shall be executed on the basis of the NAV of the UCITS from which assets for which there are valuation issues or legal uncertainty shall be excluded.

Article 10

Entry into force

This Regulation shall enter into force on the day following that of its publication in the *Official Journal of the European Union.*

It shall apply from […]

This Regulation shall be binding in its entirety and directly applicable in all Member States.

Done at Brussels,