

ZIA Zentraler Immobilien Ausschuss e.V. - Wallstraße 16 - 10179 Berlin

European Securities and Markets Authority
To whom it may concern
11-13 avenue de Friedland
75008 Paris

Präsident:
Dr. Andreas Mattner

Vorstand:
Ulrich Höller
Dr. Eckart John von Freyend
Dr. Gerhard Niesslein
Friedrich Wilhelm Patt
Bärbel Schomberg
Christian Ulbrich
Thomas Zinnöcker

Präsidium:
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Dr. Hans Volkert Volckens
Wolfgang Weinschrod
Dr. Marc Weinstock
Wolfgang Wingendorf
Claus Wisser
Thomas Ziegler

Geschäftsführer:
Axel von Goldbeck (Sprecher)
Klaus-Peter Hesse

**Zentraler Immobilien
Ausschuss e.V.**
German Property Federation
Wallstraße 16, 10179 Berlin
T: +49 (0) 30 - 20 21 585 - 0
F: +49 (0) 30 - 20 21 585 - 29
info@zia-deutschland.de
www.zia-deutschland.de

Büro Brüssel:
Rue du Commerce 31
B-1000 Bruxelles
Telefon: +32 (0) 2 - 792 10 05
Telefax: +32 (0) 2 - 25 48 90 29

VR 25863 B (Berlin-Charlottenburg)

 **BDI**
Mitgliedsverband des BDI

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Comments on the Consultation paper about ESMA's draft technical advice to the European Commission on possible implementing measures of the Alternative Investment Fund Managers Directive (ESMA/2011/209)

Dear Sirs,

First of all, we would like to thank you for the opportunity to respond to the questions of the above mentioned consultation paper.

The German Property Federation (ZIA) was founded by a number of well-known property companies in June 2006. With over 140 members ZIA provides comprehensive and uniform representation of the interests of the real estate industry and is a member of the Federation of German Industries (Bundesverband der Deutschen Industrie). ZIA is also represented in Brussels with an office of its own in order to integrate itself at European level and to advocate the interests of the German real estate industry successfully vis-à-vis the political decision makers in Brussels.

Among our members are numerous open-end and closed-end real estate funds that fall into the scope of the AIFM Directive and are therefore affected by the consultation paper and the future measures of the AIFM Directive.

Even if this has not been a focal point of ESMA's research, we would like to stress that in our view the AIFM Directive does not provide a clear definition of Alternative Investment Funds. Due to this it is unclear, whether or not real estate companies qualify as alternative investment funds. We understand that managers of open-end real estate funds as defined by the German Investment Law (InvG) as well as managers of closed-end funds are covered by the Directive. However, this does not necessarily apply to managers of (listed) property companies including Real Estate Investment Trusts (REITs). It is challenging to assess the proposals contained in the consultation paper as long as the scope of the Directive remains unclear. We would therefore welcome a new assign-

ment of ESMA to examine the scope of the Directive and to clarify the rules for the property sector.

In our comments we assume that the Directive covers open-end and closed-end real estate funds, but does not apply to listed property companies or REITs. Our comments focus on those questions in the consultation paper that are the most relevant for the real estate sector.

Part III Article 3 Exemptions and Possible Implementing Measures on Valuation

Q1: Does the requirement that net asset value prices for underlying AIFs must be produced within 12 months of the threshold calculation cause any difficulty for AIFMs, particularly those in start-up situations?

Q3: Do you consider that using the annual net asset value calculation is an appropriate measure for all types of AIF, for example private equity or real estate? If you disagree with this proposal please specify an alternative approach.

In its last discussion paper on Article 3, ESMA proposed a valuation of assets on a quarterly basis. ZIA's comments on such a frequent valuation obligation for smaller funds were very critical. We welcome that ESMA has refrained from proposing rules that would have forced the AIFs to value their assets more frequently than foreseen by article 19 of the directive. The now proposed annual valuation of assets is practicable.

We want to point out that an ongoing monitoring of the total value of assets under management must not lead to any kind of high level valuation of the assets. In our point of view monitoring should be clearly distinguished from valuation.

We are pleased, that ESMA allows different valuation methodologies for the various asset classes. In particular, established and approved methods, e.g. for illiquid assets such as real estate, should continue to be accepted in the future.

Part IV. General operating conditions

IV.I. Possible Implementing Measures on Additional Own Funds and Professional Indemnity Insurance

Potential risks arising from professional negligence to be covered by additional own funds or professional indemnity insurance (Box 6):

The suggested definition of fraud as a category of professional negligence would cause a widening of the liability risks which we do not understand. Criminal intent actions such as fraud are not negligently. Because of that reason they are not part of the relevant risks and must not be covered by additional own funds. These actions also cannot be covered by an insurance, because such damages are non-insurable.

In addition to that, the risk of fraudulent behaviour or dishonesty can only be minimised through efficient internal control systems but not prevented.

We suggest to delete all references to risks in relation to fraud and to make clear, that only losses due to dishonest, fraudulent or malicious acts by relevant persons must be covered, when the internal control system is not implemented.

Quantitative Requirements (Box 8)

Q10: Please note that the term “relevant income” used in Box 8 includes performance fees received. Do you consider this as feasible and practicable?

Q11: Please note that the term “relevant income” used in Box 8 does not include the sum of commission and fees payable in relation to collective portfolio management activities. Do you consider this as practicable or should additional own funds requirements rather be based on income including such commissions and fees (“gross income”)?

In accordance with other representatives of the real estate industry we would like to stress, that income and specifically performance fees are not reliable proxies for risk in the operation of real estate funds, because there is no correlation between performance fees earned and relevant risks taken by the AIFM. That is the reason why we support the suggestion of deleting performance fees as part of “relevant income” in the sense of Box 8.

We do not prefer one of the suggested options for calculation of additional own funds presented by ESMA. While option 1 is easier to implement option 2 might be better reflect the risk profile of the fund managers. But both options cause an over-capitalisation in relation to potential liability risks resulting from their operational activities.

Q13: Do you see a practical need to allow for the “Advanced Measurement Approach” outlined in Directive 2006/48/EC as an optional framework for the AIFM?

There is no need to implement an even more complex approach such as Advanced Measurement Approach. This approach was created for calculating operational risk in banks. AIF Managers are organized in a completely different way which makes it difficult to apply the same approach. Furthermore, only large fund managers which are mainly subsidiaries of banks would be able to calculate the ratios and to collect the detailed figures. That is why we suggest that the proposals in Box 7 should be deleted entirely.

IV.II. Possible Implementing Measures on General Principles

Q16: Paragraphs 4 and 5 of Box 11 set out additional due diligence requirements with which AIFM must comply when investing on behalf of AIFs in specific types of assets e.g. real estate or partnership interests. In this context, paragraph 4 (a) requires AIFM to set out a business plan. Do you agree with the term “business plan” or should other term be used?

The requirements suggested in para. 4 are equal to the current business standards for German fund managers engaged in the management of open-ended

real estate funds. For practicability reasons it should be made clear in para. 5 that the obligation to retain records for a period of at least five years applies only from the AIFM Directive's date of entry into force and does not affect transactions concluded before that date.

Pertaining ESMA's suggested references to a "business plan" we suggest another term, since the investment objectives, guidelines and restrictions agreed with investors are the main points.

Box 19: Fair treatment by an AIFM

Q17: Do you agree with Option 1 or Option 2 in Box 19? Please provide reasons for your view.

As pointed out by other real estate industry bodies we oppose both Options. For that reason we support BPF's comment:

"Article 12 (1) of the Directive states that "No investor in an AIF shall obtain preferential treatment, unless such preferential treatment is disclosed in the relevant AIF's rules or instruments of incorporation." This clearly contemplates that an investor can be given preferential treatment provided that this is disclosed in the AIF's rules or instruments of incorporation regardless of whether or not that preferential treatment gives rise to a material disadvantage to other investors.

ESMA's proposed advice therefore goes beyond the scope of Level 1.

It is also unclear what is meant by "an overall material disadvantage to other investors".

We suggest that ESMA's advice should make it clear that where preferential treatment may or does occur, investors are treated fairly if this is disclosed to them. The disclosure referred to in Article 12(1) can be made in general terms in the AIF's prospectus or offering document provided that the details of any such preferential treatment are disclosed to those investors affected thereby prior to investment.

In the context of real estate AIF, it is common practice for side letters to be issued and/or most favoured nation provisions to be used in relation to different groups of investors and these arrangements are disclosed to the investors affected thereby prior to investment."

Box 30: Functional and Hierarchical Separation of the Risk Management Function

Q18: ESMA has provided advice as to the safeguards that it considers AIFM may apply so as to achieve the objective of an independent risk management function. What additional safeguards should AIFM employ and will there be any specific difficulties applying the safeguards for specific types of AIFM?

Q19: ESMA would like to know which types of AIFM will have most difficulty in demonstrating that they have an independent risk management function? Specifically what additional proportionality criteria should be included when competent authorities are making their assessment of functional and hierarchical independence in accordance with the proposed advice and in consideration of the safeguards listed?

We are concerned, that especially smaller AIFM would have difficulties in the separation of risk management functions. Therefore, it appears reasonable to clarify that the obligation for implementing an independent risk management function should be proportionate to the nature, scale and complexity of the AIFM business and the AIF they manage.

To make clear how the functional and hierarchical separation of the risk management function is to fulfil we support the idea of separating the risk management from operating units, including the portfolio management function. Therefore, we also suggest that only the portfolio management function is considered as operating unit which is not responsible for all risk management tasks. Functions like reporting, accounting, valuation and monitoring investment compliance should not be permitted.

IV.VII. Possible Implementing Measures on Organisational Requirements

The implementing concept for AIFM Directive are based upon UCITS and MiFID standards which are currently in place and already practiced by German fund managers. Therefore, we strongly support ESMA's suggestion to align the Level 2 measures to the AIFM Directive with the established EU rules for the asset management industry.

Q23: Should a requirement for complaints handling be included for situations where an individual portfolio manager invests in an AIF on behalf of a retail client?

We are concerned, that such a requirement could cause a regulation by two different Directives for real estate closed-ended funds, because para. 10 MiFID contains a regulation for complaints.

Part V: Depositaries

We support ESMA's suggestions for the depositaries in general but want to highlight some concerns especially of German real estate closed-end funds. The requirements should consider the established product and the structure, because the depositary function is often performed by lawyers or auditors. That is why we support the comments of the VGF Verband Geschlossene Fonds.

Part VIII: Transparency Requirements

VIII.I. Possible Implementing Measures on Annual Reporting

Box 104 (Primary Financial Statements) and Box 105 (Content and Format of the Report on Activities for the Financial Year)

Q63: Do you agree with the approach in relation to the format and content of the financial statements and the annual report? Will this cause issues for particular GAAPs?

Regarding the content and format of the annual report to be prepared for each fund, we welcome the fact that the accounting information contained in the annual report shall be prepared in accordance with accounting standards applicable in the home Member State of the AIF.

It is very important to recognize the existing national accounting standards and the underlying national rules. E.g. in Germany, many companies, which fall into the scope of the AIFM Directive, are obliged to balance according to the rules of the German Commercial Code (HGB). It would lead to considerable costs for these companies, if they had to prepare balance sheets according to HGB rules and (only for AIFM reporting purposes) IFRS at the same time.

In addition to that we reject the suggestion in para. 7 (a) (iii) of Box 104 to present "unrealised gains on investments" as part of the income and expenditure account. This runs counter to the established reporting practice in Germany. Furthermore, this would deviate from the calculation of distributable income which is currently determined as the ordinary net income of a fund. The unrealised gains should only be provided in the overview of AIF performance and to be included in the report on activities (cf. Box 105 para. 1 (b)).

We would very much appreciate it if these comments were taken into account in the further development of the measures of the Alternative Investment Fund Managers Directive. Please do not hesitate to contact us if further advice on these matters is required.

Sincerely yours



Axel von Goldbeck