21 September 2011

Response to ESMA Consultation Paper (ESMA/2011/270, dated 23 August 2011)

The African Venture Capital Association (AVCA) is an industry association representing African private equity and venture capital companies, and their general and limited partners representing approximately $24 billion in Funds under Management. Our members which number 90 are amongst the largest African private equity and venture capital firms in the world, the largest international development institutions and global professional service firms which support our industry's growth and development.

AVCA was founded in 2000, formally registered in Cameroon in 2002, and actively works through industry conferences, training sessions, research, and information dissemination. We aim to be the principal knowledge centre for the pan-African private equity and venture capital industry; the key service provider to our constituency by being member-centric in our approach and; a catalyst for the continent to derive its economic growth from the private sector.

The AVCA is concerned that the implementation of the AIFMD in Europe should not unintentionally disrupt or impede the provision of private equity and venture capital to African economies. We note in particular that the marketing of funds from third countries in Europe from July 2013 will be subject to there being adequate co-operation agreements in place between supervisory authorities. The AVCA would not wish to see the process for putting those administrative arrangements in place delay the ability of funds to continue to attract investments from European investors.

The AVCA is grateful for the opportunity to comment and would be willing to discuss any aspect with ESMA.

Questions 1 and 2

Delegation of risk management and portfolio management to entities in a third country

1. Art 20.1 (c) of the AIFMD (2011/61/EU) ("the directive") provides that AIFMs may delegate the task of portfolio management or risk management to a third country firm if either (i) the entity is

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registered or authorised in the third country and subject to supervision or (ii) if not so registered or authorised, then with the prior approval of the home state regulator.

2. Art. 20.1(d) provides that there must be a co-operation agreement with the relevant third country regulator in any event. This implies that the option of delegating to an unregulated entity with prior approval in art. 20.1(c) is not workable because sub-paragraph (d) of art. 20.1 assumes there will always be a relevant regulatory authority in the third country with whom a co-operation agreement has to be maintained. It therefore could be taken as ruling out the possibility of delegating tasks to a wholly unregulated entity in a third country even though that is a possibility contemplated by art. 20.1(c) of the directive. The draft technical guidance on which ESMA is consulting could go some to way to addressing this problem. The last sentence of explanatory paragraph 12, page 9 touches on the situation where prior approval is sought but is unclear and potentially ambiguous on the point. Paragraph 12 of the explanatory text should be clarified so as to make clear that it is possible for tasks to be delegated to a wholly unregulated entity in a third country subject to this being approved by the competent authority in the home state of the AIFM.

3. In Box 1, page 7, it is unclear what is meant by the enforcement of 'regulations' in para 4(e). It is unclear whether this is a reference to regulations in the third country or in the home state of the AIFM that is delegating tasks to an entity in the third country. This should be clarified to expressly refer (where applicable - see above) to the third country regulations and to the authorities in the third country responsible for the enforcement of the regulations.

4. The equivalence test contained in paragraph 5 of Box 1 when read together with paragraph 10 of the explanatory text (and the cross reference to Box 67 of the main draft guidance) may unduly constrain the types of entity in a third country to which portfolio management and risk management may be delegated. Box 67 of the main technical guidance issued by ESMA in July 2011 refers to the impossibility of delegating to an entity that is only authorised to engage in "collective portfolio management". This rules out the possibility of delegation to a UCITS investment companies or to an internally managed AIF but arguably there should not be an

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automatic, unqualified, application of these typologies to third country entities because the system of regulation may incorporate differently classified financial entities. It is obviously sensible that delegation of these tasks should only be made to entities in third countries that are organised to undertake asset management but care should be taken not to transpose the third countries the necessity for rigid categories or definitions of such entities drawn from EU legislation.

5. Paragraph 8 of the Box 1 explanatory text, page 8, suggests MMoUs centrally negotiated with ESMA might be desirable. In principle the AVCA supports the proposal for single MMoUas it consider this would be more likely to be conducive to ensuring that the necessary inter-authority arrangements are in place in time for the commencement of the AIFMD in July 2013. This comment applies generally in respect of the co-operation arrangements contemplated in this technical guidance.

Questions 3 and 4

Appointment of third country Depositary art 21(6)

6. It is questionable whether the test "have the same effect" in art. 21.6 (b) of the directive actually means "equivalence" in the way suggested by ESMA. It is suggested that the "same effect" test should properly be given a looser meaning such that it would be sufficient if a depositary in a third country is subject to regulation that produces the same effect in terms of the overall level of protection provided. This would be a more judgement based test than one that simply looks for equivalence in the form, content and wording of regulatory provisions.

7. It is questionable whether the capital requirements that must be applied a third country as set out in Box 2, para 1(c) are appropriate. The requirements must be equivalent to those imposed under EU law on a credit institution or on an investment firm under the MiFID. A MiFID investment firm that is permitted to carry out custody functions (and is not a credit institution) may have a basic capital requirement which is far lower than a credit institution. The base requirement for a credit institution is 5m euro – yet a custodian that is a MiFID firm might have a base capital requirement applied to it from a range of

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125k to 750k euro plus an expenditure based requirement. Rigidly transposing these two capital regimes may not always be appropriate where for example an institution licensed under a banking regime in a third country is not required to comply with capital requirements equivalent to the EU credit institutions requirements because for example it has a limited business model that is restricted to custodial and depositary functions. In this event although licensed as a bank it may have to comply with capital requirements that are lower than those imposed under the EU capital requirements directive. Simply labelling an entity as a bank may be inappropriate for this purpose.

8. The same point applies in relation to 'operating conditions' in Box 2 para 1(d) – the typologies of credit institution and MiFID investment firm may need to be applied flexibly to take account of third country approaches to the regulation and licensing of financial entities.

9. Box 2 para 1(f) could be clarified to make clear that it is referring to local third party sanctions in respect of contraventions of third country regulations and conditions.

10. It might be also helpful for this section of ESMA's explanatory text to its guidance on the appointment of third party depositaries to make clear that the guidance is without prejudice to art. 21.3 (c) of the directive in the case of private equity type funds which in particular do not 'generally invest in assets that must be held in custody'. In this event the depositary may be an entity that carries out depositary functions as part of its professional duties etc. This opens up the possibility that in the case of private equity funds it may, for example, be possible for an administration company, accountant or registrar to undertake the depositary function. Article 21(6), to which this aspect of ESMA's technical advice is directed, is expressly stated to be without prejudice to 21(3). It may be helpful if ESMA were to acknowledge this at least in the explanatory text and more generally reach out to third countries with a view to establishing the kind of situations and entities that would result in 21(3) being satisfied.

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Questions 5 and 6

Supervision

11. It is not clear what is meant by Box 3 paragraph 2 – the third country authority should assist the EU competent authority "… to enforce EU legislation and national implementing legislation breached by the entity". The expression "EU legislation" is not defined. It is not clear what powers the third country should have in relation to contraventions that have not taken place in its jurisdiction? It may not be possible for such a jurisdiction to be established or to be legally effective in a third country?

12. Generally the AVCA supports the idea of using the IOSCO Multi-lateral MoU of May 2002 and the IOSCO Technical Committee Principles for Supervisory Co-Operation for the purposes of the proposed MMOU to implement the inter-authority arrangements required by the AIFMD.

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