BlackRock

BlackRock response to ESMA consultation on the draft regulatory technical standards under the revised ELTIF Regulation

Executive summary

BlackRock welcomes the revision of the ELTIF framework and the opportunity to reflect on the future standards applying under the ELTIF regulation, following its review by EU co-legislators.

At the heart of the Capital Markets Union initiative is the realisation that the European Union has a once-in-a-generation opportunity to address its financing needs while empowering EU citizens to achieve their long-term financial goals. Channelling more funding towards private markets is a core objective in building Europe's economic resilience. Offering European citizens a greater choice of long-term growth investment opportunities will be key to ensuring their welfare and enhancing the value of their savings in the long term.

Reinforcing the attractiveness of the ELTIF as an efficient and trusted fund structure is crucial to achieving these goals. We see increasing demand from retail investors and their advisors to invest in 'long-term' assets such as private equity, private infrastructure and private credit investments. Feedback from distributors is clear that these are the types of strategies they wish to include as a standard component of portfolios for clients with a long-term investment horizon.

ELTIF is the vehicle of choice to catalyse that movement in Europe. Now that we are confident that level 1 rules are fit for purpose, we are grateful for the opportunity to comment on the future level 2 framework.

Our comments to the various questions below are grounded in the following key principles, which we hope will also be reflected in the final RTS:

- **Need to remain faithful to the overarching objective of ELTIF reform –** we strongly believe the RTS should stay true to the objectives and the spirit of the level 1 text that was agreed by co-legislators, in particular as it pertains to the objective of allowing long-term or evergreen ELTIFs that can effectively offer the possibility for clients to redeem during the life of the fund. This will help to differentiate ELTIF from the traditional institutional private markets fund structures, and we strongly believe it will unlock greater retail participation and ELTIF uptake.
- **Liquidity management tools (LMTs) and redemption rules should be looked at holistically –** it is the conjunction of all of an ELTIF's product features and the liquidity characteristics of the underlying investment that will determine whether LMTs and redemption rules are fit for purpose and aligned with the objective to increase uptake and retail participation in ELTIF markets. For example, private credit and infrastructure debt and equity all have different liquidity characteristics which the manager will need to reflect when building an appropriate liquidity profile into the fund structure. Crucially, minimum

holding periods, minimum notice periods and redemption limits interact with each other and cannot be seen in isolation when assessing the liquidity profile of an ELTIF. If rules are too restrictive on one or more of these aspects, it will adversely impact the attractiveness of ELTIF.

- **Setting the right liquidity profile is always about balance** – while we understand the basis of questions around setting minimum standards, we believe that responsibility for finding the right equilibrium between LMTs that can manage the risks of an ELTIF's assets and target clients is best calibrated by the fund manager. The fund manager remains responsible for the liquidity it can offer investors, based on a detailed and case-by-case assessment of portfolio construction, target return, operational aspects and target investors' liquidity needs. We therefore believe the level 2 measures should focus on principles, factors to take into consideration, and - only when necessary - *minimum* standards that are subject to derogation and can be adapted to the wide range of ELTIFs that may be launched.

QUESTIONS

Q1: Do you agree with the proposed approach in relation to the RTS under the abovementioned Articles 9(3), 21, and 26(2) of the ELTIF Regulation?

Q2: Do you agree that the abovementioned pieces of legislation and regulatory material are relevant for the purpose of the RTS on Article 25(3) of the ELTIF Regulation? Which other pieces of legislation and regulatory material do you consider relevant for that purpose)?

Q3: Do you agree with the abovementioned assumptions? In relation to the ELTIF cost ratio figures to be expressed as yearly percentages (of the capital of the ELTIF), would you see merit in expressing it instead in terms of maximum percentages (and, in the prospectus, only refer to the corresponding yearly figures included in the KID, or in the annual report of the ELTIF)?

Q4: Do you agree that the types of cost mentioned in the present paragraph are annual costs that could be expressed as a percentage of the capital? What are your views on the list of "other costs" referred to above in paragraph 31(b) which are suggested to be added, as compared to the list of "other costs" referred to in Article 25(1)(e) of the ELTIF Regulation?

Q5: Do you agree that the types of cost mentioned in paragraph 32 are fixed costs and that an assumption on the duration of the investment is necessary to calculate these costs in the numerator of the overall cost ratio mentioned in Article 25(2), provided that this overall ratio is a yearly ratio? Would you see merit in specifying what is to be meant by the "setting-up" of the ELTIF, as referred to in Article 25(1)(a) of the ELTIF Regulation? If yes, could you indicate which elements of the "setting-up" of the ELTIF should be clarified?

Q6: Do you agree that the types of costs mentioned in paragraph 35 may be considered as fixed costs in the case of an ELTIF?

Q7. Would you see merit in including a specific grand-fathering clause (in relation to the RTS under Article 25(3) of the ELTIF Regulation) for ELTIFs benefitting from the grandfathering clause provided for in Article 2 of Regulation 2023/606?

Q8: Do you agree with the proposed amendment to the existing RTS under the first paragraph of Article 18(6) of the ELTIF Regulation?

We agree with the proposed changes to the existing RTS to align them with the new wording of article 18.

Q9: Do you agree with the proposed criteria to determine the minimum holding period (referred to in point (a) of paragraph 2 – Article 18(6)(a)) of the ELTIF Regulation? What are your views on the setting of a minimum of X years for all ELTIFs, irrespective of their individual specificities (with X equal to 3, for example), with respect to the abovementioned minimum holding period?

Our experience, notably as a manager of several ELTIF 1 funds, has shown us that a long minimum lock-in period (5 years or half the life of the fund in the case of ELTIF 1) can be detrimental to the functioning of ELTIFs, as it prevents the fund manager from setting a tailored minimum period that aligns with clients' expectations, the fund characteristics (assets classes, asset maturity), as well as the other liquidity tools at its disposal.

We strongly suggest leaving the length of any lock-up period to be determined by the manager. The RTS could, as envisaged in the draft, consider specifying certain factors which should be taken into account in making such a determination, for instance taking into account that private markets funds have very different ramp-up periods (credit funds can ramp up in 12-18 months while certain infrastructure funds can take up to 4 years).

ELTIFs are products covered by the PRIIPs regulation, which means retail investors are given a prominent "recommend holding period" when investing in these funds and we would welcome consistency in approach when disclosing recommended holding periods.

Q10: Do you agree with the proposed approach in relation to the minimum information to be provided to the competent authority of the ELTIF (referred to in point (b) of paragraph 2 – Article 18(6)(b) of the ELTIF Regulation)?

We are comfortable with the information to be provided at the time of authorisation of the ELTIF but are of the view that the only information that should be provided on an ad-hoc basis during the life of the ELTIF should be strictly limited to material changes to information already provided. In particular, the RTS should have specific guidelines and prescribed reporting standards for disclosure of the information detailed in paragraphs 78 and 79. Our view is that if the published and pre-approved redemption policy is being followed, including the use of LMTs, it would not add to the quality of supervisory oversight to advise the regulator in advance of the use of such tools and could prevent them being operated in a timely manner.

Q11:

a) **Do you agree with the proposed approach in relation to the requirements to be fulfilled by the ELTIF in relation to its redemption policy and liquidity management tools, referred to in points (b) and (c) of Article 18(2) – Article 18(6)(c) of the ELTIF Regulation)?**
b) **What are your views on the setting of a maximum redemption frequency on a quarterly basis, for all ELTIFs, irrespective of their individual specificities, as suggested in paragraph 83?**

c) **What are your views on the setting of a notice period of Y months for all ELTIFs (with Y equal to 12, for example)? What are your views on the options 1 and 2, set out in paragraphs 87 to 90, in relation to the specific requirements/circumstances where the notice period could be less than one year, and the numerical values of the parameters Z(1) to Z(4), under option 1, and Y, under option 2?**

d) **In your view, how do these requirements on the redemption policy and liquidity management tools of the ELTIF would compare to those applying to existing long-term investment AIFs which would be similar to ELTIFs (e.g. in terms of eligible assets)? Where possible, please support your answers by providing examples of current liquidity set-up for similar long-term funds marketed to retail investors, analyses of the data available to assess the value of ELTIF long term assets and the length of the valuation process.**

A.

We underline the importance of considering liquidity management tools and redemption rules on a holistic basis. Indeed, the right balance between investor protection, operational efficiency and commercial attractiveness can only be found by combining several features and mechanisms which shall be aligned with the investment strategy and the liquidity profile of underlying assets of the fund. Crucially, minimum holding periods, frequency of redemption windows, minimum notice periods and redemption limits interact with each other and cannot be considered separately when assessing the liquidity profile of an ELTIF. If rules are too restrictive on one or more of these aspects, it will likely adversely impact the attractiveness of ELTIF and the take-up among retail investors.

On the investment side, the proposed option 1 (minimum portion of liquid assets) does not reflect the reality of portfolio construction for these types of products. ELTIFs are designed to invest in long-term assets, as part of a diversification strategy at the level of a client's portfolio. That diversification should not be done at the level of the product, as this would defeat the purpose of creating differentiated returns for the client. We should remember that ELTIF investments are expected to represent only a small subset of the retail client's financial assets (themselves a smaller subset of a client's total wealth) – based on appropriateness rules regarding portfolio composition, suitability tests and warnings already set out in MiFID Level 1 and Level 2 texts by the co-legislators. Effective portfolio composition should mean that in case of need, clients will therefore be able to draw on more liquid assets in their portfolio, before turning to their reserves allocated to less liquid ELTIF investments which have a longer recommended holding period.

On the use of liquidity management tools, we strongly caution against limiting redemption gates to "exceptional circumstances" especially if the definition of a gate covers liquidity caps set out in the fund documents and clearly disclosed in advance to investors as proposed in Option 2 on an ex ante basis. Gates are an important and common tool for fund managers investing in assets with limited liquidity, in normal and stressed market conditions alike. The widespread availability of gates has – rightfully – been encouraged by regulators and legislators on a global scale . Our view is that subject to appropriate disclosures in the offering documents pertaining to the relevant fund, gates structured as caps on available liqudity are not necessarily more difficult to understand for retail investors than other aspects of financial investing. We would also recommend that access to such liquidity is determined on a pro rata basis on the relevant dealing day rather than on a first come first served basis to maintain fairness between investors.:

As noted above ELTIFs we expect ELTIFs are to be sold with the relevant appropriateness and/or suitability test. We would not expect first time investors that are not familiar with investment funds to be buyers of ELTIFs, but rather we expect ELTIFs to be sold to more experienced retail investors.
To help end-investors understand the importance of gates as a liquidity risk management tool, it may be necessary to provide enhanced information and education to distributors and investment advisors on the function and purpose of gates, as part of client suitability and appropriateness assessments. This can be achieved through best practice guides in cooperation with the relevant trade associations and national competent authorities.

B & C.
On redemption frequencies and notice periods (points b and c), setting strict and perhaps arbitrary minimums/maximums would not be appropriate, as it would not reflect the wide variety of cases in which the ELTIF strategy and assets could allow for more/less frequent redemptions or shorter/longer notices. The fund manager is best placed to set its funds' liquidity terms; therefore we do not think there is merit in setting a minimum notice period of "Y" months, as there are a number of factors which may dictate how much notice managers need. In particular, in our view a blanket 12-month notice applying to all ELTIF irrespectively of their investment strategy and other LMTs would likely not appropriately reflect the nature of each fund and strategy, with a risk that a substantial portion of ELTIF strategies and product will be considered un-sellable through many investor channels.

While we welcome ESMA providing optionality in determining redemption frequencies and notice periods, we do not believe that either Option 1 or Option 2 by themselves would give the sufficient flexibility to all existing and future possible ELTIF investment strategies and client bases.
Asset managers' risk teams have their own complex and detailed models for liquidity management, details of which are shared with their NCAs as part of reporting on liquidity risk management programmes. We agree with the proposal to require managers to submit these analytical frameworks, assumptions, and liquidity stress testing as part of the application process but would support leaving the determination of the appropriate redemption frequency to managers and justify their choices of tools to supervisory discussion on fund authorisation and on an ongoing basis as part of ongoing liquidity stress testing requirements.

Q12: Do you agree with the proposed criteria to assess the percentage referred to in point (d) of Article 18(2) – Article 18(6)(d))?

The proposed approach is more flexible and aligned with market practice, insofar that it gives the asset manager sufficient margin to determine the percentages of assets that can be redeemed. We support this approach.

Q13: Do you agree with the principle-based approach suggested above, in relation to the ESMA RTS under Article 19(2a)?
Yes, we would support this principle-based approach. The development of efficient redemption/subscription matching mechanism will require innovation and extensive collaboration between ELTIFs manufactures, distributors and other third parties (including custodians, fund platforms etc.). It is therefore important to preserve some flexibility for market participants in order to build commercially viable and operationally feasible mechanisms.

As the ELTIF market can still be considered to be in its early stages, it is important to note that we expect redemptions under article 18 of ELTIF to remain the primary source of liquidity for retail investors wishing to exit from their long-term ELTIF investments. As the number of ELTIF funds and investor will increase over the years, the secondary market is expected to become deeper. ESMA will then be able to review whether the matching mechanisms are fit for purpose.

Q14: Do you agree with the proposals suggested above and corresponding draft RTS, in relation to the transfer process for both exiting and potential investors, and the role of the manager of the ELTIF or the fund administrator in conducting transfers, and the matching of respective requests?

Q15: Do you agree with the proposed approach and corresponding draft RTS, in relation to the periods of time during which exiting and potential investors may request transfer of shares or units of the ELTIF? If both systems under Article 18(2) and 19(2a) coexist, how could the risk of arbitrage between different prices in the primary and the secondary markets be, in your view, mitigated? How could (retail) investors be ensured that the purchase or sale of shares on the secondary market will be executed at prices that reflect the value of the ELTIF?

Q16:m Do you agree with the proposals above and the corresponding draft RTS, in relation to the determination of the execution price and the proration conditions and the level of the fees, costs and charge, if any, related to the transfer process?

Q17: Do you agree with the proposals above, and the corresponding draft RTS, in relation to the timing and the nature of the disclosure of information with respect to the transfer process conditions?

Q18: Are you of the view that any of the requirements of the draft RTS under the amending ELTIF Regulation should be adjusted to take into account the specificities of listed ELTIF? If yes, could you specify which requirement should, in your view, be amended?

Q19: 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 redemption policy of ELTIF under Article 18(2) of the ELTIF Regulation? Which other types of costs or benefits would you consider in this context?

Q20: 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 matching mechanism of ELTIF under Article 19(2a) of the ELTIF Regulation? Which other types of costs or benefits would you consider in this context?

Q21: Do you agree with the above-mentioned reasoning in relation to the possible costs and benefits of the option taken by ESMA as regards common definitions, calculation methodologies and presentation formats of costs of ELTIFs? Which other types of costs or benefits would you consider in this context?