INVESTMENT COMPANY INSTITUTE

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July 27, 2009

Via Email
Mr. Emil Paulis
Director, DG MARKT/G
Financial Services Policy & Financial Markets
European Commission
200 Rule de la Loi
B-1049 Brussels, Belgium
emil.paulis@ec.europa.eu

Dear Mr. Paulis:

The Investment Company Institute[1] welcomes efforts by the European Commission to create a harmonized EU regime to protect against the potential risks associated with certain types of alternative investment funds. The proposed Directive on Alternative Investment Fund Managers (the "Directive")[2] would establish an EU framework for monitoring and supervising the risks that alternative investment fund managers pose and permit such managers to provide services and market their funds to professional investors across the EU market. If structured and implemented appropriately, a "passport" regime for the distribution of alternative investment funds to professional investors in the EU may benefit EU investors by providing them with more investment choices, and the EU investment management industry by creating additional growth opportunities.

We are concerned, however, that the Directive fails to adequately take into consideration the global nature of the investment management industry and the broad range of investment products that are offered to investors in the EU and throughout the world. An overly broad regulatory regime, such as

[1] The Investment Company Institute is the national association of U.S. investment companies, including mutual funds, closed-end funds, exchange-traded funds (ETFs), and unit investment trusts (UITs). ICI seeks to encourage adherence to high ethical standards, promote public understanding, and otherwise advance the interests of funds, their shareholders, directors, and advisers. Members of ICI manage total assets of $10.6 trillion and serve over 93 million shareholders.

[2] The text of the proposed Directive on Alternative Investment Fund Managers (the "Directive") is available at, http://ec.europa.eu/internal_market/investment/docs/alternative_investments/fund_managers_proposal_en.pdf.

the current draft of the Directive would appear to create, may have unforeseen and unintended consequences that can significantly and detrimentally impact EU investors, investors in other countries, the EU investment management industry and the global investment management industry. We, therefore, strongly urge those involved in drafting or reviewing the Directive to consider fully the far-reaching consequences of the Directive and to tailor it to more precisely meet the desired objective.

This letter conveys our primary concerns with the Directive based on information available to us at this time. As further information about the Directive becomes available, and as we have the opportunity to further consider the impact of the Directive, we may identify and communicate additional concerns.

Effect on U.S. Registered Investment Companies

We have significant concern about the Directive because it appears that if an alternative investment funds manager, as defined under the Directive (an "AIFM"), provides investment management services to a company registered under the U.S. Investment Company Act of 1940 (a "U.S. RIC"), the provisions of the Directive would apply to the AIFM's activities with respect to the U.S. RIC. Because certain provisions of the Directive are incompatible with the Investment Company Act of 1940 (the "ICA"), a U.S. RIC would be unable to retain an AIFM as its investment adviser or sub-adviser.

We read the Directive as applying to an AIFM's activities with respect to U.S. RICs because, with a few narrow exceptions,[3] the proposal provides that the Directive will apply to all AIFMs established in the European Community that provide management services to one or more alternative investment funds (each, an "AIF"), regardless whether the AIF is domiciled inside or outside of the European Community. An AIF means any collective investment fund other than a UCITS fund. Under the proposal, if an EU investment manager is required to comply with the Directive, the provisions of the Directive appear to apply to the AIFM's activities with respect to *all* of the AIF managed by the AIFM, whether or not the specific AIF is domiciled in the EU or offered to EU investors.[4] Under this reading

[3] The Directive excludes (1) AIFMs established in the EU that do not provide management services to an AIF domiciled in the EU and do not market AIF in the EU and (2) AIFMs that meet the requirements of the de minimis exemption for small managers.

[4] For example, Article 17 of the proposed Directive requires, "[f]or *each* AIF it manages, the AIFM shall ensure that a depositary is appointed. . ." (emphasis added). Similarly, Article 12 of the Directive requires the AIFM to employ a liquidity management system for "*each* AIF it manages" and Article 16 of the Directive requires the AIFM to ensure that a valuator is appointed which is independent of the AIFM to establish the value of assets and the value of AIF shares "for *each* AIF that it manages" (emphasis added).

of the Directive, if an EU investment manager provides management services to a U.S. RIC and the manager also manages EU-domiciled AIF and markets such funds in the EU, then all of the manager's activities, including the manager's activities with respect to the U.S. RIC, would be subject to the Directive.

As mentioned above, if the Directive applies to an AIFM's activities with respect to a U.S. RIC, AIFMs would be unable to provide investment management services to U.S. RICs because of the conflict between certain provisions of the ICA and the Directive.[5] In addition, a number of provisions in the Directive result in new requirements that differ so significantly from current regulatory requirements applicable to U.S. RICs and common practice, as to be unworkable.[6] If U.S. RICs are unable to retain AIFMs as investment advisers or sub-advisers, EU investment management firms could be seriously harmed; these firms would need either to forego potentially successful business opportunities, or organize their operations so that U.S. RIC investment management services are not provided by an AIFM that is required to be authorized under the Directive. In fact, EU investment advisers manage a significant amount of the assets of U.S. RICs. As of May 31, 2009, $1.178 trillion out of $9.983 trillion of the assets of open-ended U.S. RICs (11.8%) and $292.3 billion out of $424.4 billion of the assets of U.S. RICs that are exchange-traded funds (68.9%) were advised by investment advisers that have a European parent entity.[7] Global investment managers often have affiliated entities in various countries in order to provide clients with the highest level of expertise in a particular region. At a time when the global economy is suffering and the financial services industry is under considerable strain, we caution against taking action that could slow recovery without a compelling justification.[8] Further, and of more direct concern to the ICI, the Directive may harm U.S. RIC investors, both institutional and retail, because they may be unable to avail themselves of the expertise offered by entities that are AIFMs.

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[5] As just one example, Article 17 of the Directive, which sets forth requirements regarding the appointment of a depositary, conflicts with the provisions of the ICA regarding custody.

[6] For example, the provisions of the Directive found in Article 20 (disclosure to investors), Article 21 (reporting obligations to competent authorities) and Article 13 (investment in securitisation positions) will result in requirements that may prove unworkable for U.S. RICs.

[7] This figure does not include U.S. RIC assets that are sub-advised by investment managers with a European parent company because we do not track this information.

[8] Regulations in other jurisdictions may similarly prohibit investment funds that fall under the definition of AIF from retaining AIFMs to provide investment management services due to the incompatibility of the other country's regulations with the Directive, which would magnify the adverse impact of the Directive.

We are also concerned that the Directive will prohibit U.S. investment advisers from marketing[9] shares of U.S. RICs, including exchange-traded funds and closed-end funds, to EU investors unless the U.S. RIC meets the conditions specified in Article 35 for marketing an AIF domiciled in a third country and its investment adviser is authorized as an AIFM in accordance with Article 39 of the Directive. Because these conditions appear unlikely to be met, at least in the near-term, EU investors will be denied the opportunity to invest in pooled investment vehicles that are subject to an extensive regulatory regime with investor protection and disclosure as its focus, which would negatively impact both EU investors and U.S. RICs.

Recommended Exclusion

We recommend that, in order to address these serious consequences of the Directive as it appears to apply to U.S. RICs, the Directive be revised to exclude U.S. RICs from its provisions. Excluding U.S. RICs from the provisions of the Directive would not be inconsistent with the objective of the Directive – extending appropriate regulation and oversight to certain actors and activities that embed significant risks.[10] U.S. RICs are very similar to UCITS, which are excluded from the definition of AIF. Like UCITS, U.S. RICs are highly regulated investment vehicles that disclose substantial information regarding their activities to both regulators and the market and do not raise the same concerns regarding lack of oversight as are raised with alternative investment funds that are less regulated, or not regulated at all. In addition, the ICA and other U.S. federal securities laws impose upon U.S. RICs stringent requirements designed to protect investors and mitigate risks, including detailed requirements regarding custody of assets, leverage, transactions with affiliates, valuation of assets, maintenance and review of compliance policies and procedures, and the content of materials provided to prospective and current investors.

To enforce compliance by U.S. RICs with U.S. federal securities laws, the U.S. Securities and Exchange Commission (the "SEC") has been given broad authority to review the activities of U.S. RICs and to investigate suspected inappropriate behavior. Further, in order to enhance the ability of the SEC and

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[9] The Directive defines marketing as "any general offering or placement of units or shares in an AIF to or with investors domiciled in the Community, regardless of at whose initiative the offer or placement takes place." *See* Article 3(e) of the Directive.

[10] *See* Proposal for a Directive of the European Parliament and of the Council on Alternative Investment Fund Managers (April 30, 2009), Explanatory Memorandum, page 2.

regulators in foreign jurisdictions to pursue violators of securities laws across borders, the SEC has entered into memoranda of understanding concerning the exchange of information related to the enforcement of securities laws with numerous foreign jurisdictions, including with many EU member states.

Given the strict regulatory regime under which U.S. RICs operate, we believe that excluding U.S. RICs from the provisions of the Directive would not be inconsistent with the objective of the Directive. Subjecting U.S. RICs to the provisions of the Directive would, in our view, unnecessarily hurt both investors and investment managers, without a corresponding benefit.

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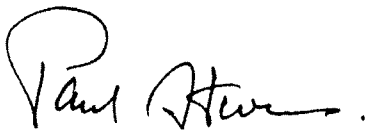
We appreciate the opportunity to express our views on the Directive and hope that our comments will be helpful as you further consider this important issue. Should you wish to discuss our comments further, or if you have any questions regarding our letter, please do not hesitate to contact me.

Sincerely,



Paul Schott Stevens
President and CEO

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