

# **UNDERSTANDING THE KEY CHANGES IN AIFMD II: ENHANCING CROSS-BORDER OPERATIONS AND GOVERNANCE**

Following extensive discussions and negotiations, on 20 July 2023 the European authorities [the Council of the EU and the European Parliament] reached a political agreement on the revision of Directive 2011/61/EU on Alternative Investment Fund Managers (AIFMD), leading to the issuance of AIFMD II on 7 February 2024. These amendments aim to harmonise existing regulatory practices, ensuring robust governance and investor protection while facilitating cross-border operations of alternative investment funds (AIFs) and their managers (AIFMs). After publication in the EU's Official Journal on 26 March 2024, AIFM 2.0 will come into force on 15 April 2024. EU member States have two years to implement the Directive.

Let's delve into the significant changes introduced by AIFMD II across various aspects of alternative investment management:

### **1. Enhanced cross-border possibilities for depositaries**

AIFMD 2 introduces the possibility of offering depositary services across borders but stops short of introducing a full-fledged cross-border depositary passport. Utilising this interim passport necessitates heightened collaboration between depositaries, their respective regulatory bodies, and those overseeing the Alternative Investment Fund (AIF) as well as, if different, the AIF Manager (AIFM). Crucially, the application of this passport under AIFMD 2 is contingent upon the "necessity principle". AIFMs must demonstrate the absence of relevant depositary services in the AIF's Member State concerning the investment strategy. Authorisation for cross-border depositary activities will be granted on a case-by-case basis, aligned with the AIF's investment strategy, until a comprehensive depositary passport is established.

AIFMD 2 broadens data reporting requirements for depositaries by incorporating the concept of a "central securities depository" (CSD) and integrating CSDs into the custody chain. The obligation for depositaries to conduct pre-emptive due diligence checks when the custodian qualifies as a CSD will be removed. Regarding the delegation of depositary custody functions, AIFMD 2 makes a distinction between: services provided by a CSD acting as an issuer where CSD will not be considered a delegation and services offered by a CSD acting as an investor CSD that will be treated as such.

Lastly, AIFMD 2 aligns with the latest updates in the EU regulatory framework, including references to MiFID II, the most recent AML Directive, and the list of non-cooperative jurisdictions for tax purposes. Importantly, it encompasses updates to this list and outlines subsequent actions required of depositaries or AIFMs based in newly added jurisdictions.



## **2. Ancillary Services Expansion**

A notable addition to AIFMD II is the extension of ancillary services that AIFMs may provide. These now include benchmark administration and credit servicing, aligning with evolving market demands and practices.

## **3. Enhanced AIFM Authorisation Requirements**

AIFMD II sets forth detailed criteria for AIFM authorisation, emphasising the need for appropriate human and technical resources. Notably, AIFMs are required to have at least two full-time equivalents domiciled within the European Union, enhancing oversight and governance.

## **4. Regulation of AIFs with Lending Activities**

AIFMD II introduces comprehensive regulations for AIFs engaged in lending operations. These regulations encompass effective lending policies, borrower concentration limits, prohibitions on extending credit to specific entities, retention of loan notional value, and structural requirements for AIFs with significant lending exposure.

## **5. Liquidity Management Tools**

Recognising the importance of effective liquidity risk management, AIFMD II empowers AIFMs managing open-end AIFs with access to a range of liquidity management tools. AIFMs are required to select at least one additional tool from a predefined list, ensuring adequate safeguards for investor interests during exceptional market conditions.

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To conclude, the new AIFMD II is satisfactory as-is, however, ESMA is due to provide essential operative details to clarify specific uncertainties. EU member states have a period of 24 months to transpose the AIFMD II into their national legislation.