INVEST EUROPE

Invest Europe's response to

ESMA Consultation on Integrated Reporting

STOCKTAKE

Q1. Do you confirm the findings presented in this stocktake section? If you have additional information, please provide all relevant details.

Yes.

We confirm that private equity managers we represent are subject to EU-level reporting, additional national reporting as well as in some cases other reporting frameworks, depending on the manager's activities and size.

We note that regulatory reporting:

- requires **significant resources due to the number of data fields** – typically carried out by service providers and representing a real administrative and financial burden on smaller managers - a cost that is ultimately passed on to investors

Many managers have long complained that reporting fields are often irrelevant in practice and do not really give investors – and regulators – the information they truly need. The exercise ESMA has launched with this consultation is also very much welcomed in that regard.

- is **not sufficiently harmonised between Member States** (as recognised by ESMA in paragraph 33, in general, and 38, for AIFMs)

The ability of Member States to request additional information makes it more difficult for managers to market funds cross-border, a reality we have detailed in our recent submission to the European Commission Consultation on the integration of EU Capital Markets. We welcome any efforts made by ESMA to tackle these inconsistencies, as they do act as a strong disincentive for managers wishing to develop a EU-wide strategy.

In practice, reporting is typically carried out with the assistance of service providers, who design standardized templates that not only frame the reporting process but also embed their own interpretations, thereby shaping market practices. However, the repeated exchanges between managers and service providers often become cumbersome and costly. Managers ultimately devote significant time and resources to reporting, despite their core mission being to support unlisted companies.

Managers of various sizes authorised under AIFMD typically estimate their reporting requirements to start at around €100K to €200K. This cost is typically harder on small managers that have just been authorised, as larger managers are better able to cope with the complexity and length of "Annex IV" AIFMD reporting.

Finally, we are not against the idea to more appropriately reflect the different fund models to avoid most funds falling under the category "others". We understand that many private equity funds are currently reporting themselves as "others" as there is no "buy-out" category.

Q2. What are the best practices for data collection for retail investment funds in EU and non-EU jurisdictions that ESMA could consider?

The below suggestions are not limited to retail investment funds but based on common reporting issues more broadly.

As a reminder, private equity funds are typically not offered to retail clients – as defined under EU law - and in nearly all situations <u>not mass-marketed</u> to private individuals.

One of the overarching comments we are making with this submission is the difference between, on one hand, funds that are mostly offered to experienced investors through a negotiated process (the typical private equity model) and, on the other, funds that are mass-marketed to retail clients, directly or through intermediaries (by and large the UCITS model). We have long argued it is somewhat perilous to fully harmonise reporting rules that apply to both models (and therefore to apply UCITS rules to all AIFs), given the differences in knowledge between one and the other.

We note that, over the past few years and steered by legislative developments such as the ELTIF Regulation, some private equity funds have increasingly been marketed to "sophisticated clients", with minimum ticket sizes starting at € 50/100K and a different liquidity profile (typically near-evergreen vehicles). While venture and private equity funds have long been marketed to a selected number of entrepreneurs and high net worth individuals, this is by and large a new development that should be encouraged in the context of the Savings & Investments Union efforts. The rise of these funds should not however lead ESMA to believe that private equity funds are soon to be mass-marketed to typical retail clients. Due to the illiquidity of assets, direct investments by small-ticket sizes private individuals in private equity funds is unlikely (the inclusion of private equity within pension and insurance portfolios is however a trend to follow).

Irrespective of these broader considerations, here are a few suggestions applying to the wider fund world:

- **Implement pre-submission validation checks:** Similar to ESMA, all NCAs should provide fund managers with a facility to validate their data against regulatory reporting rules (e.g. any errors, or anomalous data points) before formal submission. This should enable firms to identify and correct data quality issues before submission, which should reduce regulatory follow-ups post-submission, general delays, and compliance costs for both sides, as well as improve data quality. The roll out of a pre-submission validation tool should be easy to access and navigate, supported by clear guidance and training.

- **Publish feedback/ recommendations centrally:** particularly on non-numerical data collection and any points on improvement. Developing a central online "knowledge base" and question management tool to enable firms to search and submit and track regulatory reporting queries could also save both the regulators and firms time and increase consistency of reporting while minimising duplicative queries.

- **Publish structured data models and definitions:** Require all EEA regulatory returns to be accompanied by a published, machine-readable data model (e.g. Class Domain Model), including field definitions, relationships, validation rules, and data standards. This should enable firms to automate mapping from internal systems to regulatory returns, and ensure a common understanding of data definitions, reducing inconsistency.

If we acknowledge that a core reporting on their common features could apply to both UCITS and AIFs, we call for calibrated reporting fields tailored to the funds' specificities (including assets managed, e.g. non-listed equity) – see our comments on Question 5.

APPROACHES TO REPORTING

Q3. What challenges arising from overlapping EU-level and national reporting obligations (e.g. under AIFMD, UCITS, MMFR) does your institution experience? Please describe specific reporting overlaps and their operational impact quantifying and providing examples of redundant submissions.

Our understanding is that national reporting is in large part inspired by AIFMD Art 22 and 24 requirements. We have however identified at least three main types of additional, non-harmonised reporting obligations, being:

1) the obligation to report on internal control measures;

2) the obligation to report on outsourcing arrangements; and

3) the obligation to report on periodic financial statements.

Below we have provided a short description of these additional reporting obligations, followed by our assessment of how the contents of these reports overlap with some of the EU harmonised rules on (i) the annual reports (art. 22 AIFMD) and (ii) reporting to the competent authorities (art. 24 AIFMD).

a. Reporting on internal control measures

Some authorities, such as the FSMA in Belgium, expect the effective leaders (i.e. the management committee) of AIFMs to maintain an accurate description of their **internal controls**. This description must contain at least the following topics, each of which must be sufficiently elaborated:

- methodology employed by the AIFM to assess its internal control mechanisms;
- activities and organisation of the company (including support functions, staff functions, and independent control functions);
- second-line controls set-up by the compliance function for the different activities of the company;

- second-line controls set up by the risk management function for the different activities of the company; and
- controls focused on the reliability of the financial reporting process.

Each time there is a material change to the internal controls of the AIFM, these authorities wish to receive an updated version of the internal control report. By means of an annual questionnaire, the effective leaders must assess and report on the appropriateness and functioning of the internal control mechanisms to the authority.

b. Reporting on outsourcing arrangements

When AIFMs (sub)delegate critical or important functions, they must provide authorities with detailed information regarding the delegated critical or import functions and the identity of the outsourcing service provider. AIFMs must report this information to the authority by means of a questionnaire, which must be updated each time there are material changes in the outsourcing arrangements.

c. Periodic financial statements

AIFMs must periodically submit detailed financial statements to the authority (in the format prescribed by the NCA). The NCA can also, at any time, request that AIFMs provide additional (accounting) information and explanation. Such periodic statements should always be (i) complete (i.e., contain all data from the accounts and inventories on the basis of which the periodic statements are drawn up) and (ii) correct (i.e., accurately reflect all data from the accounts and inventories on the basis of which the periodic statements are drawn up).

In the feedback we have received from members, which is not meant to be exhaustive, the main content-related overlap between gold-plated national provisions and harmonised AIFMD provisions that we identify relates to the reporting on financial information.

Concretely, the detailed financial statements that AIFMs must periodically submit to the NCA will to a certain extent overlap with both the (financial) information in the annual report (see art. 22 AIFMD) and the general information to be provided to the regulator (through use of EU templates 'AIFM file 24(1)', 'AIF file 24(1)', 'AIF file 24(2)', and/or 'AIF file 24(4)' – see art. 24 AIFMD). As a result, an AIFM will sometimes need to provide financial information at 3 different intervals and in at least 3 different formats. In addition, the NCA can sometimes, always at its own discretion, ask for additional information from the AIFM.

Streamlining of reporting topics (at least at national level) could have a positive effect on the regulatory compliance burden of AIFMs. On the contrary, adding additional layers of reporting on an EU level, without removing the existing overlap on national level, will only add to the existing complexity.

Q4. Do you support the objective of developing a more integrated reporting framework covering AIFMD, UCITS, MMFR, and ECB statistical reporting? What are the key obstacles or risks linked to integrating fund reporting frameworks?

Yes, <u>but with significant caveats, in particular regarding how this objective could be achieved</u>.

Lowering the number of fields and increasing interoperability between national and EU reporting is a laudable objective. Yet, an integrated reporting model would have to be sufficiently well-designed to ensure that both the number of reporting fields and the frequency of reporting do not increase for certain types of managers.

A **UCITS/ AIFMD integrated report without appropriate caveats may result in more complexity than clarity**, even for members who manage both UCITS and AIFs. Issues could stem from an uplift of reporting requirements for private equity AIF managers if they were required to report data fields similar to those of UCITS managers; they could also stem on the NCA side at the point of review, particularly with respect to interpreting reports on similar concepts (e.g. leverage) and not respecting the fact that those have been calculated using separate methodologies under different frameworks (i.e. leverage under AIFMD versus under that under UCITS).

The main obstacle we identify, as representatives of private equity funds, is the **difficulty in setting up a common template for fund managers whose business model is effectively completely different**: UCITS and private equity funds have in practice many divergences and joint data fields could lead to much confusion for managers - simply because data fields do not really correspond to market realities. This problem already exists with existing, general AIFMD reporting fields: it could increase exponentially would the two regimes be merged.

Indeed, there are a **number of UCITS-typical fields that will not make sense in the context of a private equity fund**. This is for example the case of data around securities lending and repos. More broadly, any reporting field that is based on the idea of a predominantly liquid portfolio of transferable securities would be invalid for a long-term fund such as private equity, real estate or infrastructure. Other measures which will not sit well with a private equity fund will be measures such as VaR limits and back testing against VaR methodology – as private equity managers will, for economic reasons rather than for comfort, use measures like Invested Capital at Risk (iCAR). Mathematical stress testing of the portfolio also makes considerably less sense for private equity funds (given the long-term nature of the investments) and the liquidity risk measures are likely to look very different.

As a reminder, private equity is an illiquid asset class, whose funds are taking direct shares in businesses. The underlying assets of the fund are unquoted, operating companies with their own directors, i.e. there is no ready-made price (as with financial instruments such as publicly quoted equities) nor a standard formula for calculating prices (as with OTC derivatives). Because private equity valuations must be sound, for the entire industry to function appropriately, time is required to assess these in a proper manner. Private equity valuations are typically done quarterly 90 and 120 days after the period has ended, respectively. The quality of valuations is the quality of the external expertise to calculate these valuations, not the ability to capture public sources of information.

In that context, harmonisation of frameworks is **unlikely to be of value for the industry**. Even for managers who manage both AIFs and UCITS, the **benefits are likely to be superficial**, as they will in any case still need to respond in turn to different sets of questions in respect of each AIF and UCITS, whether it is via different sections, tabs or modules of the integrated report, an exercise that will not be that different in practice to reporting two sets of reports under the existing framework. The benefits may largely lie for the NCAs who may be able to modernise the readability of the integrated report (through AI, for example).

This may in itself be an obvious goal for ESMA (and for the NCAs) but it should hence not be presented as a regulatory simplification.

From an industry perspective, there may simply be a better case for reducing duplicative reporting by integrating AIFMD and ECB statistical reporting than merging AIFMD and UCITS data.

In light of this, ESMA should first and foremost focus on the exercise to determine which reporting elements are of high value (as expressed in section 5.1. of the consultation) not only from a broader perspective, but asset class by asset class, with a particular focus on assets classes diverging the most from the norm.

ESMA could then consider:

- which fields are effectively always relevant
- which fields are **similar but can create confusion**, both from a semantics but also practical perspective (typically leverage reporting)
- which fields are **irrelevant for certain asset classes** (typically liquidity reporting for long-term funds providing no redemption rights)

Based on the results of this exercise, ESMA could then assess the structure of reporting models, taking into consideration specificities of asset managers – and also clarifying which specificities are relevant factors. Doing it the other way around would necessarily risk creating frameworks that will not fit with the realities of some market players.

Ultimately, integrated reporting should never lead to “common standard reporting” – otherwise, the same mistakes as with the KID document could be created, where disclosure to investors is produced but largely ignored by industry participants and/or being unreadable to regulators, because seen by market players as disconnected to the investment realities (i.e.: giving indication of what a return can be after a year to a fund with no redemption rights). Furthermore, the new reporting template should be **dynamic**: fields which are irrelevant to a given fund should automatically disappear. In other words, selecting a 'not applicable' box should permanently remove all related reporting fields.

As a conclusion, we share ESMA’s goal of simplification/harmonisation but only if such harmonisation is not done at the expense of the diversity of features within the global asset management space.

Q5. Please list your preferred option of those listed in this section and highlight any other option or combination of the ones listed here that you consider effective. In your response, please outline the main expected costs and benefits associated with the options proposed, and identify any preconditions or phased implementation steps that would be necessary to ensure feasibility and proportionality.

Background

- *Option IR1: Integrated reporting - Multiple reporting obligations with reuse of data*
- *Option IR2: Full integrated reporting framework*
- *Option IR3: Full integrated reporting framework including specific national reporting requirements*

Our response:

As a general principle, we emphasize that any integrated reporting should replace - rather than add to - existing obligations.

We would only be in favour of a fully integrated reporting framework (IR2) provided that:

1) ESMA can create a regime where specificities of certain fund types are effectively included (see our response to Question 4)
2) it does not deforce existing supervisory structures
3) it does not create additional requirements

If that is not possible, then the best proposition for a specific asset class such as ours would be not to integrate the reporting at all.

We welcome the idea of ESMA to acknowledge, through the use of modules, specific fund requirements. As mentioned in the previous question, we find that there would be a significant benefit in tailoring templates to fund models, in particular taking into consideration the underlying investments and the liquidity profile of funds, as detailed in our response to the previous question. Particular care should be taken to avoid imposing liquidity disclosures to closed-ended funds with no or limited redemption rights.

Similarly, ESMA should, if integrating frameworks, acknowledge the very different pace at which managers do report. Again, ESMA should not perceive this divergence of pace, as it has often been portrayed in the past, as a favour to long-term fund managers: the frequency of reporting should simply fit with the needs of investors and the level of illiquidity of underlying investments.

We are also against the possibility for the authorities to define national-specific modules or fields that address local supervisory needs, incorporated within the same unified reporting structure.

It should be recalled that the time, effort and cost needed to introduce a new reporting system may be significant, in particular for smaller players. For instance, the migration to the ROSA system introduced in France by the AMF or the introduction of the DORA reporting were not straightforward.

In any case, **we call for a proper transition to the new reporting system to be organized**: guidelines and specific technical norms should be developed, and support should be put in place, in particular for the attention of smaller players.

Q6. To what extent should the integration or alignment of supervisory and statistical reporting extend beyond the asset management frameworks, such as EMIR, SFTR, or MiFID/MiFIR? What challenges do you foresee? Are there additional reporting regimes that should be considered for future alignment with asset management reporting?

For reasons we have laid out above, we are not convinced that the integration of reporting of every asset management framework always make sense: this view naturally extends, to an even larger extent, to a further integration to MiFID.

At present, EU AIFMs and UCITS managers are not subject to the MiFIR transaction reporting framework at all, so the integration benefit with MiFIR may be limited to situations of delegated portfolio management or orders routed via a group MiFID firm performing reception and transmission of orders

We are even sceptical, from an agnostic point of view, that it would at all be helpful for similar structures. This is because the nature and purpose of reporting for each is fundamentally different. MiFIR, EMIR and SFTR are transaction-level reporting regimes, which focus on the detail of each specific transaction. MiFIR transaction reporting, for example, has over 65 data fields per reportable transaction, and is designed predominantly to monitor potential market misconduct.

Those regimes are also more intermediated than AIFMD reporting, in that reports are normally submitted via an ARM or a trade repository, rather than directly to national or EU-level regulators. If the purpose of the fund manager reporting frameworks is (in part) to gain an oversight of risk exposures of funds, it seems likely that this can be achieved with reporting at a much less detailed level than MiFIR or EMIR.

If the goal is to limit the level of information, it may be better to reduce the duplication of reporting of common fields in MiFID, EMIR and/or SFTR instead, for example in respect to derivatives and SFTs in fund-level reports.

Q8. How should the approach to focus on reporting elements with high added-value approach be implemented to ensure proportionality, efficiency, and data quality?

As mentioned in our answer to Question 4, we suggest for ESMA to focus on the value of reporting data per type of fund, also acknowledging the fund's investor base (typically to avoid treating funds marketed to retail clients in the same way as funds exclusively offered to retail investors).

Value in reporting certain elements may be important from a UCITS perspective - both because of the liquidity of assets and the retail nature of investors – and yet remain irrelevant from a private equity perspective. Market fluctuations are a good example of this: they will be extremely relevant for daily-traded UCITS funds, and entirely irrelevant for private equity funds, which are able to sell their businesses with one or two years-delay in difficult market conditions.

DATA SEMANTICS

Q9. How can semantic data integration best be achieved across reporting frameworks? Please identify areas where alignment would be most beneficial?

See our comments on fund classification in our response to Question 1.

In the context of the development of such integrated reporting system, we support the development of a common reporting taxonomy allowing the proper integration of reporting obligations, even though this may be quite challenging.

We support ESMA's proposals to:

- create a common dictionary of data allowing a unified taxonomy for the reporting for asset management;
- identify national ad hoc reporting requirements in order to ensure better coordination;

- create a centralized database including the funds' key features.

Regarding the "AuM", it is essential that this concept, which is key to determine whether a manager is subject to AIFMD or not, continue to take into consideration the funds' specificities. It is unclear whether it would be possible to have a definition of an "AuM" that is sufficiently simple to be clear and sufficiently sophisticated to account for the way one calculates the AuM of a liquid fund compared to a closed-ended fund.

Reporting flows and data sharing

Q10. Which of the proposed options do you consider most efficient? If possible, please quantify the expected cost and benefits for each option. Would you support an alternative option involving additional actors, such as centralised reporting infrastructures?

We can see the efficiencies of a single EU point for managers reporting under Annex IV as a result of marketing registrations under national private placement regimes (for example, Article 42 AIFMD). This is likely to eliminate any variations in Member States' reporting standards in respect of the same fund marketed in each jurisdiction.

The benefits for an AIFM marketed under the AIFMD passport will be less clear. In some cases, a single point of reporting could mean increased complexity for managers, as they currently report to a NCA that is aware of their (and their national market's) specificities.

The risk of introducing a single EU reporting point for AIFMs is tied to the fact that there is quite some variation in national fund types, with which the NCA is very familiar and where any request for additional information can be targeted to the specificities of the managed fund and local market.

A single reporting point could however be relevant for those AIFMs marketed in jurisdictions where NCAs are systematically requesting additional (and arguably often irrelevant) information – and for which a centralised regime overseen by ESMA will mean a more appropriate regime. The less developed the market, the more relevant this is likely to be, as the quality of supervision is greatly dependent on the development of the local ecosystem.

The fact both of these can be equally true mean that reporting directly to ESMA (or some equivalent reporting entity) as a single EU point of data entry will only be a better solution if the benefits of the removal of gold-plating of reporting obligations are, on the whole, greater than the loss of relationship between managers and their current NCAs (and the ability of ESMA to replace that relationship).

ESMA should therefore consider how changes may, at least at first, constitute a concern for fund managers based in certain of the most developed EU jurisdictions, and therefore carefully weigh the pro's and con's of such an approach.

What is certain is that the addition of a new third-party for data collection (e.g. the AIFMD and UCITS equivalent of an EMIR or SFTR trade repository) is likely to add unnecessary costs without any clear benefits.

In conclusion, moving away from the national reporting framework is therefore not just a mere matter of cost or procedural optimisation, especially as fund structures largely differ from one country to another.

Q11. How important is it to retain the supervising NCA as an intermediary between the reporting entity and the centralised system in the reporting process?

We argue that the less intermediaries there are, the less likely the manager will be subject to additional requirements. There should either be a single EU supervisor or the NCA as a single supervisor for funds in its market – but not a mixed regime.

Q13. Would a phased implementation of the potential changes outlined in the sections on "Integrated reporting" and "Reporting flows and data sharing" help ensure proportionality and facilitate smoother transition?

Yes. This is likely to be key to any proposed change, particularly given reshaping data systems will be expensive and time consuming. Giving the industry time to get up to speed with the new standards will result in better reporting from the get-go.

Whether there should be phased implementation is likely to depend in part on what the final regime looks like. It might be beneficial to have overlapping periods where a firm can report under the old or new regime, rather than a cliff-edge date. If the new regime is more proportionate, this will allow firms who are ready earlier to benefit, while also giving sufficient time for those firms who need longer to implement the changes.

Finally, it should be made clear that firms are not required to re-submit or update any reports validly submitted under the old regime.

Reporting formats and systems

Q14. Do you consider that it would be beneficial to introduce a common standard, such as ISO 20022, across all reporting obligations within the asset management domain? What would be the costs and benefits for reporting entities of transitioning all reported data to a single standard? If ISO 20022 is not the preferred solution, what alternatives could be considered?

Yes, provided this standard has already been widely adopted by national regulators. While we see potential synergies, this would only be relevant if already used.

Q15. What would be the main advantages and disadvantages of using respective syntaxes (XML, JSON, XBRL) for all AIFMD and UCITS reporting?

Beyond the issue of the use of different syntaxes, we would like to point out that, in some countries, data collection remains non-digitised which is causing efficiency concerns. For example, in Czech Republic, reporting via the CNB portal still requires XML/XBRL manual upload.

Data granularity and use of master data

Q16. Would an increase of data granularity contribute to improved data quality, usability and reduced duplications? To what extent can the greater use of

international standards (e.g. CFI codes, LEIs) and master data reduce the compliance costs and improve interoperability in regulatory reporting?

No. This type of reporting is neither useful in a private equity context- nor even potentially feasible to put in place. Such type of granularity could only be relevant for publicly listed securities. Even if managers provided NCAs with a list of all investment holdings with no further data crunching, this would still give no meaningful information to NCAs.

As a way of background, private equity deals often comprise a relatively small number of high value transactions. As there is no "look through" in reporting (the investor makes an investment in a fund, not in underlying companies), the relevant exposure reported is likely to be of an intermediate vehicle in a PE acquisition stack (i.e. bidco), as opposed to a house entity.

This is unlikely to be very illuminating for NCAs and risks creating further misconceptions around private equity house risk and exposure (similar to reporting on leverage of portfolio companies, hence its exclusion under AIFMFD Article 6.3). Private equity managers are likely to face strong operational difficulties with reporting data instrument-level exposures, especially if the typical method of identifying instruments is via ISINs, etc., as these are not ordinarily used in a private equity context.

If ESMA considers moving forward with this, it should therefore exclude private equity firms – and other similar firms – from any increase of granularity – and consider this as an example of situation where consistency of reporting would not give meaningful results.

Q17. What are your views on implementing security-by-security as the baseline granularity? What are the main benefits and costs of the presented options? What solutions should be envisaged to ensure a proportionate approach?

We are against this idea. This would again be the use of methods irrelevant to the private equity space, for reasons explained in the previous question.

Reporting frequency

Q21. Do you consider that frequency should be aligned across reporting regimes and jurisdictions? If yes, what frequency would provide the best balance of costs and benefits? What kind of challenges would you expect in implementing it?

No.

As noted by ESMA, private equity funds have less frequent valuations due to their underlying assets.

Ultimately, not requiring a lower reporting frequency to certain types of managers is not so much a question of reporting burden than it is of inherent logic: it has limited value for the regulator to require a fund manager that has invested in a private company that will not be sold for several years to require it to do monthly reporting, unless such a fund is offering monthly liquidity to its clients. Doing this would just require a fund manager to request an employee or an external firm to report the same number for several months, with no interest for the regulator as no additional valuation will have been done in the meantime.

Would ESMA design a regime that better recognise the inherent features of long-term closed-ended funds - expressly recognising the lower valuation frequency that is needed in the case of long-term underlying assets, this could represent a significant positive step in a context where EU lawmakers seek to develop the offer of these funds, given their benefits for the EU economy.

We also note that the requirement to report to competent authorities within 30 days (as per Article 110 of the AIFMD Delegated Regulation) is impractical for private equity fund managers and is not well-tailored to the illiquid nature of private equity investments and to the practices of the private equity industry.

Q21. What solutions and criteria should be envisaged to ensure a proportionate approach with respect to the reporting frequency?

See our answer to Question 20.

Q23. Given that daily reporting requirements are already implemented in certain Member States, how such a frequency could be set up to ensure an integrated approach while avoiding a disproportionate burden for reporting entities?

As mentioned above, daily reporting requirements are always irrelevant in a private equity context and should never be imposed, including by NCAs.

Other considerations

Q25. Are there any other dimensions not considered in this discussion paper that are relevant for the establishment of a more integrated reporting system? If yes, please provide specific examples and your views on potential improvements that can be made and their priority.

No.