LMA Loan Market Association

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LMA response to the ESMA Consultation Paper on the draft regulatory technical standards on open-ended loan-originating AIFs under the AIFMD

Dear Sir or Madam,

The Loan Market Association (**LMA**) would like to thank ESMA for the opportunity to provide feedback on the draft regulatory technical standards (**RTS**) on open-ended loan originating alternative investment funds (**OE LO AIFs**) under the revised Alternative Investment Fund Managers Directive (**AIFMD**).

The LMA is the voice of the loan markets across Europe, the Middle East and Africa. With over 880 members across over 69 jurisdictions, we represent an ever-growing diversity of participants in international capital markets, including institutional investors, private and public sector issuers, banks, non-banks, technology solution platforms and market infrastructure providers, spanning EMEA and other global jurisdictions.

The consultation is particularly relevant to the LMA's mission to **reduce barriers to accessing capital** and to **increase cross-border liquidity of loan assets**.

The LMA very much supports the ESMA approach of making it possible for loan originating alternative investment funds to be open-ended. We believe that OE LO AIFs will **attract a broader investor base**, that might be hesitant to commit to closed-ended structures with long lock-in periods, allowing investors to redeem their units at periodic intervals, enhancing the liquidity of their investments.

In line with the EU's broader competitiveness agenda, we would like to share the following **key considerations** within the context of this consultation:

1. The LMA welcomes ESMA's approach in providing a **harmonised implementing framework** tailored to the specificities of OE LO AIFs, allowing managers to demonstrate to their respective national competent authorities (**NCAs**) that they can maintain an open-ended structure for loan originating funds.
2. The LMA believes that the RTS should be aligned with market trends aimed at meeting investors' increasing demands for **alternative investment strategies** with a liquid profile, thereby contributing – in parallel – to the European Commission's competitiveness objectives.

3. The LMA believes that a **measured approach** should not be overly prescriptive, specifically in relation to the authorisation process and (minimum) liquidity thresholds.
    a. An **authorisation requirement** for OE LO AIFs would not be in the spirit of the AIFMD and would make the European fund industry less competitive as compared to non-EU markets.
    b. A **regulatory minimum of liquidity** would not be desirable, as funds' liquidity profiles can vary significantly over time and the risk of liquidity shortfall is already addressed via existing liquidity management tools (including stress testing).

Response to consultation (Questions 1-22)

Question 1 –Are there any elements other than the redemption policy, the availability of liquid assets, the performance of liquidity stress tests and ongoing monitoring that AIFMs shall take account to demonstrate that the liquidity management system of the OE LO AIFs they manage is sound? If yes, please specify.

The LMA generally agrees that the elements set out in Article 1 of the draft RTS, as referenced in Section 2.2 of the consultation paper, are relevant for consideration in the context of demonstrating to an NCA that the proposed liquidity management system for an OE LO AIF is sound.

The LMA believes that, currently, there are **no other elements** that should be taken into account to demonstrate that the liquidity management system of OE LO AIFs is sound.

On the basis of **current AIFMD provisions**, AIFMs already need to have processes and procedures in place considering the characteristics of all the funds they manage. As outlined by ESMA in para 6 of the consultation paper, ESMA has performed an assessment of the existing AIFMD level 2 provisions on liquidity management to establish whether there were any gaps that would need to be addressed to account for the specificities of OE LO AIFs. In para 11 of the consultation paper, ESMA has already concluded that there are no such gaps to be filled

The LMA believes that the redemption policy, availability of liquid assets, the performance of liquidity stress tests and ongoing monitoring elements should be tailored to reflect existing OE LO AIFs' standards as applied in other jurisdictions, and that the EU should **avoid introducing new requirements** which may introduce further complexity or additional administrative costs, thereby contradicting the Commission's competitiveness objectives.

Additionally, the LMA does not believe that it is appropriate to require all OE LO AIFs to hold a **proportion of liquid assets**, as suggested in Article 1(2)(b) of the draft RTS. The appropriateness of targeting a minimum proportion of liquid assets within an OE LO AIF will depend on a variety of factors relating to its structure, including but not limited to the investment strategy and investor base. Having regard to these factors, it should even be permissible to have no proportion of liquid assets in certain circumstances [please see our answer to Question 4 for a more detailed analysis].

Question 2 – Do you agree with the list of factors set out in Article 2 of the draft RTS to be considered by AIFMs to establish an appropriate redemption policy for an OE LO AIF? If not, please justify your position.

The LMA acknowledges that the list of factors set out in Article 2 of the draft RTS are relevant for consideration when developing an appropriate redemption policy for an OE LO AIF. In our view, the list of factors **does not need to be considered** in order to establish an appropriate redemption policy for OE LO AIFs – given the diversity of funds. The relevant factors to be considered, should be based on the investment policy and characteristics of the managed funds; this list of factors should not be limitative. Additionally, we caution in the setting of any arbitrary limits under the RTS, which could limit the growth and success of OE LO AIFs.

In addition to our previous remarks on the **proportion of liquid assets** [under Question 1], it should be noted that seeking to consider certain of these factors **ex-ante** may prove challenging. For example, Article 2(1)(g) of the draft RTS referencing "*The anticipated level of subscriptions and redemptions of investors*" may prove challenging where such information is not available, cannot be reliably estimated by historical data (or proxies), or can only be estimated based on prospective investor input.

Finally, it should be considered whether a suitable redemption policy could be implemented at AIFM level (taking a principles-based approach which would then be applied depending on the mechanics of the relevant fund), rather than on a fund-by-fund basis.

Question 3 – Are there any other factors that AIFMs shall consider to demonstrate that the redemption policy of the OE LO AIFs they manage is appropriate? If yes, please provide a list of such factors and explain why they shall be included.

With reference to the answer provided under Question 1, the LMA believes that **there are currently no other factors** to be considered to demonstrate that the redemption policy of the OE LO AIFs they manage is appropriate. As outlined by ESMA in paragraph 6 of the consultation paper, ESMA performed an assessment of the existing AIFMD level 2 provisions on liquidity management to establish whether there were any gaps that would need to be addressed to account for the specificities of OE LO AIFs. Per the above, in paragraph 11 of the consultation paper, ESMA has already concluded that there are no such gaps to be filled.

Question 4 – Do you agree that AIFMs that intend to manage OE LO AIFs shall determine an appropriate proportion of liquid assets to be able to meet redemption requests? If not, please justify your positions?

The LMA welcomes ESMA's proposal to the extent that it recognises that the AIFM is best placed to develop the liquidity management framework for an OE LO AIF. However, we believe that AIFMs **should not be required** to determine a level of liquid assets on a pre-launch basis, as multiple criteria need to be considered in order to assess the liquidity of a fund within that context and, under AIFMD, a list of useful liquidity management tools has already been included.

It is important to note that requested amounts for redemption as well as cash-flow schedules (including credit risk) **may change substantially over time**, and therefore would not continue to reflect the defined proportion of liquid assets set out by the AIFM. Therefore, defining a set proportion of liquid assets would not necessarily allow AIFMs to adequately meet redemption requests in all cases.

The LMA further proposes that the AIFM should have the ability to determine which portion of the AIF's portfolio may be deemed 'liquid' for the purpose of meeting redemption requests, taking due consideration of other liquidity management tools. We believe that **portfolio composition is not the only way** to ensure liquidity in a fund and referring to a defined level of liquid assets does not always make sense. As the EU considers the long-term benefits of a Savings & Investment Union, trying to unlock the potential of longer-term funds, ESMA might want to consider provisions that would stimulate and support long-term financing, such as via ELTIFs and OE LO AIFs. This could be achieved by introducing flexibility as regards a zero proportion of liquid assets, depending on the specific circumstances. Introducing a minimum liquidity threshold may therefore limit the ability of the European fund industry to remain competitive as against other funds.

Question 5 – Do you agree with the list of factors that AIFMs shall consider to establish the appropriate amount of liquid assets? If not, please justify your position. Shall AIFMs consider other factors, and if yes what are these factors?

The LMA supports ESMA's proposed list of factors, as it defines in a flexible manner the elements AIFMs would have to take into account to establish the appropriate amount of liquid assets. We believe that **no other factors need to be added,** and we support, in particular, paragraph 3 of Article 3, which underlines that other investments made by the OE LO AIF may also be considered as liquid, provided that certain conditions are met. It may however be helpful to include reference to the fund's redemption terms, as set out in the fund documentation, as an additional factor.

The LMA believes that the factors listed by ESMA may be used to determine the liquidity profile of the fund in a dynamic and flexible manner. On the other hand, a rule-defined liquid assets requirement on a pre-launch basis would not be desirable in our view. The reasons for this are many and includes the fact that seeking to consider certain factors **ex-ante** may prove challenging in practice. For example, Article 3(1)(n) of the draft RTS referencing "*The investor base including the investor type, potential investor concentration and their anticipated subscription and redemption behaviours*" may prove challenging to apply where such information is not available, cannot be reliably estimated by historical data (or proxies), or can only be estimated based on prospective investor input.

Question 6 – Do you agree that cash flow generated by the loans granted by OE LO AIFs shall be considered as liquid assets? If not, please justify your position.

The LMA generally believes that it **should remain the responsibility of the manager** to determine which assets are considered to be 'liquid' for this purpose. We believe that it is not the intention of the AIFMD Level 1 text to have a pre-defined list of liquid and non-liquid assets in the RTS.

In addition, we note Article 3(1)(l) of the draft RTS states that "*The expected incoming cash flow of the portfolio*" should be considered by AIFMs when determining an appropriate proportion of liquid assets. However, it is **not necessarily the case** that cash flows generated by assets held within an OE LO AIF can be used to meet redemption requests. Rather, such cash flows can be used to pay regular distributions / income to investors (e.g., on a quarterly basis) or to cover management charges etc. As such, ESMA may, therefore, wish to reflect this in its draft RTS.

Question 7 – Do you agree that AIFMs may consider other assets as liquid if they can demonstrate that these assets can be liquidated within the notice period, to meet redemption requests, without significantly diluting their value? If not, please justify your positions.

The LMA agrees that managers **may consider other assets** as liquid if they can demonstrate that these assets can be liquidated within the notice period, to meet redemption requests, without significantly diluting their value, as long as the used methodologies are documented as part of the manager's liquidity risk management framework.

We also agree with ESMA that it is not appropriate to specify within the draft RTS all assets that can be considered ex-ante as liquid given the diverse nature of in-scope funds' investment strategies, investor bases, and operating models.

However, it should be avoided that redemptions can only be a **percentage** of a part of the portfolio deemed to be liquid, rather than a portion of the entire portfolio.

Question 8 – Are there any other types of assets that could be considered as liquid for the purpose of the availability of liquid assets? If yes, please give examples and explain why they could be considered as liquid for the purpose of the availability of liquid assets. Conversely, are there any other types of assets that shall not be considered as liquid? If yes, please specify.

Provided that the draft RTS define liquid assets in a principle-based manner, the LMA does not see the need to extend the definition further or to establish a list of liquid and non-liquid assets. Managers determine liquidity **in line with their policies** and should continue to have the right to decide how they assess the liquidity of the overall portfolio.

Question 9 – In your practical experience, how do AIFMs that manage OE LO AIFs determine the level of liquid assets to be held by the fund to meet redemption requests? In particular, how do they calibrate the amount of liquid assets with respect to the maturity of the loans granted and the number of loans in the portfolio?

The LMA would like to stress that AIFMs have **detailed liquidity management plans** in place, as well as well-structured redemption policies. The AIFMs are responsible to determine which assets are considered liquid, under the general supervision of their regulator. It should be noted that the sale of assets is only one way of meeting redemption requests, and that managers may decide to use other means (e.g. borrowing, use of subscription proceeds), irrespective of the liquidity of their portfolio.

Question 10 – Do you believe there should be a regulatory minimum amount of liquid assets to be held by an OE LO AIFs and, if yes, please specify it? Should this minimum apply across all types of OE LO AIFs, or should it differ among OE LO AIFs and, if yes, how?

The LMA does not believe there should be a regulatory minimum amount of liquid assets to be held by OE LO AIFs, as each fund's liquidity profiles will **vary over time** and the risk of liquidity shortfall is addressed via existing liquidity management tools.

Instead, AIFMs should ensure that the risk of liquidity shortfall is minimised through accurate comparisons of liabilities and asset liquidities, using sufficiently conservative assumptions, e.g., via liquidity stress testing, as well as taking into consideration various available liquidity management tools.

Question 11 – Do you agree with the draft provisions on liquidity stress testing set out in Article 4 of the draft RTS? If not, please justify your positions.

We agree with the draft provisions on liquidity stress testing as set out in the draft RTS, and would like to highlight that ESMA did not identify any gaps in current rules.

Question 12 – What other parameters, if any, AIFMs managing OE LO AIFs shall take into account when performing liquidity stress tests?

In our view, the conduct of liquidity stress tests should remain at the discretion of the AIFMs, and therefore, the approach should not be further prescribed by additional parameters.

Question 13 – What could be the criteria that would justify a frequency of liquidity stress tests higher or lower than on a quarterly basis?

The LMA generally agrees with ESMA's assessment that the frequency of stress testing may be impacted by the liquidity of the asset base, the concentration of the investor base, and use of financial leverage. However, the impact of deteriorating market conditions should already be caught within an AIFM's liquidity stress testing framework and so may **not necessarily require** the frequency of stress testing to change.

The frequency of the liquidity stress-tests should at least be aligned with the redemption policy set for the OE LO AIF. **Factors** that may lead to a higher frequency stress-testing exercise could be:

- Higher dealing frequency,
- More concentrated investor base,
- Fund characteristics: funds with more complex or volatile investment strategies may require more frequent liquidity stress tests to ensure they can handle sudden market changes,
- Market conditions: during periods of market instability or high volatility, increasing the frequency of liquidity can help in better managing liquidity risks.

Per the above, there may be circumstances where no liquidity stress testing may be appropriate as a frequency (for example, where there is limited pricing visibility available to run any meaningful liquidity stress tests due to the nature of the fund holdings).

Question 14 – Do you agree with ESMA's proposal on ongoing monitoring set out in Article 5 of the draft RTS? If not, please justify your position.

The LMA agrees with the elements listed in Article 5, which we understand to be non-exhaustive.

Question 15 – What are the parameters that AIFMs managing OE LO AIFs shall monitor to ensure that the AIF has a sufficient level of liquid assets to meet redemption requests?

The total liquidity generating capacity for the fund at a given time horizon will be defined as the sum of the liquid assets that can be sold over that horizon and the total cash generated from loan payments, under conservative assumptions on the (credit) risk factors that affect these repayments.

Loans held in the portfolio and the various ways in which they can be designed and managed, are important sources of liquidity in OE LO AIFs. Managers would monitor the cash flows scheduled from those loans and their amortisation.

For assets that are not loans originated by the AIF, the AIFM should monitor the cost of disposing of these assets for multiple redemption thresholds, in line with the notice period of the AIF.

In addition, the AIFM could leverage on the results of stress-tests on the loan portfolio to determine a conservative term structure of liquidity generation from repayments.

Other methods, such as borrowing, could also be used to meet redemption requests (irrespective of the liquidity of the AIF portfolio). Finally, it should be noted that that funds with less prescriptive redemption mechanics may not need to conduct this type of ongoing monitoring as liquid assets would not be required in order to satisfy the fund's redemption requirements.

Question 16 – How do AIFMs that manage OE LO AIFs monitor the liquidity of the loans originated by the AIFs?

AIFMs define policies and procedures when funds are created, including liquidity management tools and monitoring activities.

Question 17 – If you are managing an open-ended loan-originating AIFs, please indicate:

a) **the size of these funds, specifying the smallest size as well as the average size;**

b) **the number of loans originated by these funds, specifying the smallest number as well as the average number of loans;**

c) **the loan-origination strategy you implement (direct lending, mezzanine, distressed debt, venture debt, diversification strategy etc);**

d) **the policy of the fund regarding the management of non-performing loans;**

e) **the shortest, highest and average redemption frequency and, if any the notice period;**

f) **among the loans you granted, please indicate (as a % of the number of loans granted, and as a % of the total amounts of the loans):**

   i. **the share of shareholders' loans**[1]**;**

   ii. **the share of non-performing loans;**

   iii. **the share of loans whose maturity has been extended;**

Not applicable.

Question 18 – If you are managing an open-ended loan-originating AIFs, have you already sold loans to meet redemptions requests? What were the main characteristics of the secondary market you used to sell them (i.e.: types of counterparties, time required to achieve the sales process, liquidity, overall cost of transaction etc)?

Not applicable.

Question 19 – If you are managing OE LO AIFs, what are the types of loans originated, how frequently do you value them and what is their level of liquidity?

Not applicable.

[1] Shareholders' loans are defined Article 4(1) of AIFMD *as means a loan which is granted by an AIF to an undertaking in which it holds directly or indirectly at least 5 % of the capital or voting rights, and which cannot be sold to third parties independently of the capital instruments held by the AIF in the same undertaking*.

Question 20 – If you are managing OE LO AIFs, what are the liquidity management tools you are using to comply with the obligations set out in Article 16 (1) and (2) of the AIFMD? Are you also using liquidity management tools other than those listed in Annex V of AIFMD, and if yes, what are these tools?

Not applicable.

Question 21 – 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 RTS on open-ended loan originating AIFs? Which other types of costs or benefits would you consider in that context?

The LMA would like to stress that an **authorisation or approval requirement** for OE LO AIFs would not be in the spirit of the AIFMD and would go against the EU's competitiveness objectives.

While the recent AIFMD rules introduced a set of fund-specific requirements regarding AIFs that engage in loan origination activities, the provisions made it clear that the burden of compliance remains on the AIFM. This was also clearly explained in Art. 16(2a) AIFMD, which allows loan-originating AIFs to be open-ended "*provided that the AIFM that manages it is able to demonstrate to the competent authorities of the home Member State of the AIFM*" that certain requirements are fulfilled. The Directive **does not specify** when this exercise has to take place, in particular, that it has to be made before setting up the fund. We believe it is for the NCA to enquire on these requirements when it sees fit and in line with its national rules and practices.

As **no separate authorisation** by competent authorities was added to the AIFMD rules, the LMA believes, it cannot be established by means of an RTS. It would contradict level 1 provisions and clearly go beyond the mandate given to ESMA under Art. 16(2f) AIFMD. This would also impair the ability of such funds to compete for investors on a global market, as their time-to-market perspective would be significantly affected.

Additionally, we would like to highlight that ESMA states that its proposals are unlikely to lead to significant **additional costs** to the extent that they provide clarifications on Level 1 provisions and do not impose additional obligations beyond those already set by the EU AIFMD in relation to loan-originating AIFs.

Question 22 – Is there any ESG and innovation-related aspects that ESMA should consider when drafting the RTS under the AIFMD?

The LMA believes that the RTS under the AIFMD would not be the **proper piece of EU legislation** to include ESG and innovation-related requirements.

Additionally, we would like to highlight that ESMA's fund name requirements push managers toward long-term, impact-driven investments, whereas the RTS for AIFMD liquidity rules require **flexibility** for investor redemptions. This creates structural constraints for open-ended sustainable AIFs, particularly in private markets.

In this response, the LMA has shared its **key considerations** aimed at ensuring that the regulatory framework for OE LO AIFs supports the broader EU agenda, while maintaining adequate risk management safeguards. We look forward to further engaging with ESMA and EU policymakers to shape a regulatory environment that unlocks the full potential of alternative financing in the EU's evolving financial landscape.

The LMA would be happy to further discuss the details of the consultation and remains at ESMA's disposal for any questions that may arise. Please do not hesitate to contact Scott.McMunn@lma.eu.com, Hannah.Vanstone@lma.eu.com or Evelien.Alblas@lma.eu.com should you wish to discuss this response in more detail.

Yours faithfully,

Scott McMunn

CEO, Loan Market Association

Appendix

The LMA is the voice of the loan markets across Europe, the Middle East and Africa. With over 880 members across over 69 jurisdictions, we represent an ever-growing diversity of participants in international capital markets, including institutional investors, private and public sector issuers, banks, non-banks, technology solution platforms and market infrastructure providers, spanning EMEA and other global jurisdictions. Its membership also consists of regulatory and governmental bodies, including the European Commission.

At a time when access to diversified and efficient financing is critical for the European economy, the LMA believes that a **measured approach** to loan originating funds can support the EU's broader ambitions of fostering competitiveness and innovation.

The EU is facing an increasingly complex global economic landscape, characterised by intensifying competition from other major economies, rapid technological developments, and the need for strategic investments in areas such as sustainability, digital transformation, and industrial resilience (incl. defence). Competitive capital markets and **diversified financing channels** are essential to ensuring that European businesses – particularly SMEs, scale-ups, and infrastructure projects – can access the capital they need to grow and compete internationally. Loan-originating funds can play an important role in **filling financing 'gaps'** left by traditional banking channels, contributing to a more resilient and dynamic financial ecosystem.

As the European Commission advances its work on the **Savings and Investments Union (SIU)**, the treatment of private credit and alternative financing vehicles such as OE LO AIFs must be aligned with the overarching goal of enhancing the **EU's financial sovereignty and global competitiveness**. A balanced and measured regulatory framework that ensures investor protection and financial stability, while avoiding unnecessary constraints on market development, will be essential to mobilising private capital for strategic sectors and fostering long-term economic growth.