

## PRESS RELEASE

# European Leveraged Finance Association (ELFA) Explores New Regime for Loan Origination Funds in Revised AIFMD 2

**15 July 2024, London:** ELFA's Engagement Committee recently held a Member Workshop with its Expert Panel partner, Akin, to help ELFA members understand the new rules applicable to loan origination funds under the revised Alternative Investment Fund Managers Directive (AIFMD 2).

AIFMD 2 establishes a new regime for loan originating alternative investment funds (AIFs), bringing Alternative Investment Fund Managers (AIFMs) that engage in loan origination activities under a comprehensive regulatory framework. The key aspects of this new regime include:

- 20% concentration limits on certain borrowers
- Risk retention requirements for loans (5% of the notional value of loans originated for 8 years or until maturity, if shorter)
- Restrictions on lending
- Requirements for effective policies, procedures, and processes
- Prohibition on "originate to distribute" strategies
- Additional investor disclosure requirements

AIFMs that manage "loan originating AIFs" must also adhere to:

- Leverage limits (175% of net asset value (NAV) for open-ended AIFs and 300% of NAV for closed-ended AIFs)
- Mandatory closed-ended structure

### Workshop Highlights:

Ezra Zahabi, a partner at Akin, led the discussion on the implications of AIFMD 2 for loan origination funds.

**Scope of AIFMD 2:** AIFMD 2, adopted in February 2024 and effective from 15 April 2024, builds on the original AIFMD framework to better regulate alternative investment funds. Although the UK is no longer an EU member, AIFMD 2 remains relevant for non-EU AIFMs managing EU AIFs and non-EU AIFs managed by EU AIFMs. The rules may be extended to non-EU AIFs under national private placement regimes (NPPR) in the future.

**Timing and Transitional Provisions:** Member States have two years to transpose AIFMD 2 into national law, with EU-wide implementation anticipated by Q1 2026. During this period, ESMA will provide further guidance to address areas of uncertainty.

**Grandfathering Provisions:** Existing portfolios of AIFs formed before AIFMD 2 came into force are grandfathered from certain requirements such as concentration limits and leverage caps. AIFs formed after AIFMD 2's implementation must comply with all new provisions by 16 April 2026.

**Loan Origination Funds under AIFMD 2:** AIFMD 2 aims to enhance investor protection, risk management, and transparency by introducing a new regime for loan originating AIFs. The directive harmonises the regulatory framework across the EU, facilitating cross-border activities of loan originating AIFs.

### Key Requirements:

- Concentration Limits: AIFs cannot make loans exceeding 20% of their capital to other AIFs or financial undertakings.
- Risk Retention: AIFs must retain 5% of each originated loan transferred to third parties.
- Lending Restrictions: Loans to the AIFM, its staff, or related entities are prohibited, with some exceptions.
- Effective Policies and Procedures: Specific governance and risk management requirements must be met.
- Prohibition on "Originate to Distribute": Managing AIFs with the intent to transfer loans is prohibited.
- Disclosure Requirements: Enhanced transparency on loan administration costs and fees is mandated.

### Requirements for Loan Originating AIFs:

**Leverage Limits:** Set at 175% of NAV for open-ended AIFs and 300% of NAV for closed-ended AIFs.

**Closed-Ended Structure:** Loan originating AIFs must generally be closed-ended unless specific liquidity management criteria are met.

**Conclusion:** AIFMD 2 strengthens the regulatory framework for loan originating AIFs, aiming to improve investor protection, risk management, and transparency. The directive's phased implementation and ESMA's forthcoming guidance will assist firms in navigating the new requirements.

**Ends**

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### About ELFA

ELFA is a trade association comprised of European leveraged finance investors from over 60 institutional fixed income managers, including investment advisers, insurance companies, and pension funds. ELFA seeks to support the growth and resilience of the leveraged finance market while acting as the voice of its investor community by promoting transparency and facilitating engagement among European leveraged finance market participants. For more information, please visit ELFA's website: [www.elfainvestors.com](http://www.elfainvestors.com).

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