

September 2025

Follow us on [LinkedIn](#) 

Regulatory Update

AIFMD II Liquidity Management Tools: A Deep Dive Into the Draft Regulatory Technical Standards

By [Zachary Milloy](#)

In the evolving landscape of EU financial regulation, the revised Alternative Investment Fund Managers Directive (AIFMD II) represents a significant step forward in enhancing liquidity risk management for alternative investment funds (AIFs). Adopted in 2024 and set for transposition by Member States by April 2026, AIFMD II introduces a harmonized framework for liquidity management tools (LMTs) to better align fund liquidity profiles with redemption demands, particularly in stressed market conditions.

The European Commission announced the delayed adoption of the draft Regulatory Technical Standards (RTS), originally due by 15 August. This update focuses on the draft RTS, as detailed in the April 2025 final report submitted to the European Commission. These RTS specify the characteristics, activation, deactivation and calibration of LMTs, aiming to promote consistency across open-ended AIFs while allowing flexibility for diverse investment strategies.

The Core Mandate: Selecting and Implementing LMTs

Under AIFMD II, alternative investment fund managers (AIFMs) of open-ended AIFs must select at least two LMTs from a prescribed list in Annex V of the Alternative Investment Fund Managers Directive (AIFMD), ensuring they are appropriate to the fund's investment strategy, liquidity profile and underlying assets. This requirement addresses vulnerabilities exposed by events like the COVID-19 market turmoil, where mismatched liquidity led to forced asset sales and investor disadvantages. The European Securities and Markets Authority's (ESMA) draft RTS emphasize that AIFMs retain primary responsibility for LMT selection, calibration and use without prescriptive mandates that could limit adaptability. Notably, tools like "soft closures" (temporary halts on new subscriptions) can supplement the selected LMTs but do not count toward the minimum two.

The RTS encourage a balanced approach: AIFMs should consider at least one anti-dilution tool (e.g., to mitigate first-mover advantages) and one quantitative tool (e.g., for volume-based restrictions) to cover both normal and stressed scenarios. Factors influencing selection include the fund's legal structure, dealing frequency, investor base and stress-testing outcomes. For funds with illiquid assets, such as real estate or private debt, the RTS underscore the need for tools that prevent material dilution without overly constraining redemptions.

Key Specifications in the Draft RTS: Tool-by-Tool Breakdown

The draft RTS provide granular details on nine LMTs, focusing on their operational mechanics. Below is a summary of the most salient requirements, highlighting activation thresholds, calibration methods and any tool-specific nuances.

- **Suspension of Subscriptions, Repurchases and Redemptions:** This tool must apply uniformly across all share classes and investors for the same duration, with no partial implementations allowed. Activation is reserved for exceptional circumstances, such as severe market stress, and requires clear policies on handling unexecuted orders. The RTS clarify that suspensions can coincide with NAV halts, but deactivation must follow a reassessment of conditions to ensure investor protection.
- **Redemption Gates:** A standout feature of the RTS is the flexibility in thresholds, which can be expressed as a percentage of NAV, a monetary value, a proportion of liquid assets or a combination — tailored to AIFs, unlike the more rigid NAV-based approach for UCITS. Activation occurs when thresholds are breached, with options for proportionate execution or full processing of small orders to safeguard retail investors. Calibration should reflect net or gross redemptions, and gates cannot activate automatically without AIFM discretion. This tool's design addresses feedback from consultations, enhancing practicality for funds with varying liquidity profiles.
- **Extension of Notice Periods:** The RTS define this as an addition to the minimum notice period (e.g., in days or weeks), excluding settlement delays beyond the AIFM's control. It maintains redemption frequency but provides breathing room for orderly asset liquidation. Activation can be time-bound and renewable, with calibration based on asset liquidity and stress indicators. Unlike some tools, it applies fund-wide without share-class variations.
- **Redemption Fees:** These fees must capture both explicit costs (e.g., brokerage fees or taxes) and implicit ones (e.g., market impact or bid-ask spreads) expressed as a percentage or fixed amount, potentially tiered by order size. The RTS require fees to benefit the fund, deducted from gross redemptions, with regular reviews to adapt to market changes. Activation is discretionary but calibration avoids predetermined ranges to allow dynamic responses.
- **Swing Pricing and Dual Pricing:** Swing pricing adjusts NAV via a “swing factor” to pass costs to transacting investors, with full (always applied) or partial (threshold-based) options. The factor accounts for transaction costs and market impacts, capped but justifiable if exceeded. Dual pricing creates separate bid/ask prices or adjusts a single NAV, similarly reflecting costs. Both tools emphasize governance and transparency, with calibration tied to net capital flows — ideal for funds with frequent dealings but less so for illiquid assets.
- **Anti-Dilution Levies:** Similar to redemption fees, these levies are triggered by significant net activity, levied as a percentage or monetary value on subscriptions/redemptions. The RTS stress estimation of costs like spreads and impacts, with reviews in stressed conditions to prevent dilution. Activation thresholds ensure targeted use, promoting fairness among investors.
- **Redemptions in Kind:** Assets are distributed pro-rata to redeemers, excluding ETF primary market participants to avoid operational hurdles. The RTS mandate policies for asset selection and valuation, with activation suited to high-concentration or illiquid portfolios.
- **Side Pockets:** These segregate illiquid assets (physically or via new share classes) to maximize value, not just for liquidation. Activation criteria must be predefined with ongoing monitoring and no new subscriptions allowed. This tool is particularly relevant for closed-ended elements within open-ended structures.

Notably, the RTS do not differentiate extensively between open- and closed-ended funds, as LMT mandates primarily target open-ended AIFs. However, loan-originating AIFs face additional liquidity stress testing under AIFMD II, indirectly influencing LMT calibration.

Disclosure, Supervisory Reporting and Governance

AIFMs must disclose LMT policies in fund documents, including activation scenarios and potential impacts, to foster investor awareness without mandating exhaustive details that could trigger runs.

Supervisory reporting to national competent authorities (NCAs) includes demonstrations of LMT appropriateness upon request, with ESMA guidelines reinforcing best practices for calibration without imposing rigid governance structures. Changes from ESMA's July 2024 consultation — such as removing uniform share-class rules and softening disclosure mandates — reflect market input following the consultation.

Practical Implications and Next Steps

For AIFMs, the draft RTS offer welcome flexibility, enabling tailored liquidity strategies that could reduce systemic risks and enhance investor confidence. However, implementation demands robust internal policies, potentially increasing operational costs for smaller managers. Existing funds have a 12-month grace period post-RTS entry into force (expected after Commission adoption before the end of 2025) to comply with guidelines.

AIFMs should proactively assess their liquidity frameworks. This harmonized approach not only strengthens EU fund resilience but also aligns with global trends in liquidity regulation, positioning the EU as a leader in effective asset management.

The Commission is in the process of adopting the final draft RTS which ESMA submitted, making some changes that are not considered substantive. The updates are expected to include inserting an express provision providing for investor-level gates to fall under redemption gates, as per the AIFMD II Level 1 intention.



If you have any questions concerning these developing issues, please do not hesitate to contact any of the following Paul Hastings London lawyers:

Zachary Milloy
+44-20-3023-5190

zacharymilloy@paulhastings.com

Diala Minott
+44-20-3023-5181

dialaminott@paulhastings.com

Catherine Gokah
+44-20-3986-1270

catherinegokah@paulhastings.com

Paul Hastings LLP

Stay Current is published solely for the interests of friends and clients of Paul Hastings LLP and should in no way be relied upon or construed as legal advice. The views expressed in this publication reflect those of the authors and not necessarily the views of Paul Hastings. For specific information on recent developments or particular factual situations, the opinion of legal counsel should be sought. These materials may be considered ATTORNEY ADVERTISING in some jurisdictions. Paul Hastings is a limited liability partnership. Copyright © 2025 Paul Hastings LLP.