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EU funds under
the AIFMD for
US Managers



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Introduction

The Alternative Investment Fund Managers Directive (AIFMD) came into force on 22 July 2013, with the result that all alternative investment fund managers (AIFMs) must (subject to quite limited exemptions) be appropriately authorised to manage alternative investment funds (AIFs) which are established or marketed in the EU.

An AIFM is anyone who, at a minimum, either performs portfolio management services or risk management services for an AIF and an AIF means virtually any fund, regardless of structure, jurisdiction or investment strategy, other than a UCITS fund. Please note that this briefing will use 'AIF' and 'fund' interchangeably.

The below summarises the conditions which must be met by US managers marketing non-EU funds into the UK and EEA. Firstly, however, we will touch briefly upon the definition of marketing under the AIFMD and reverse solicitation, which continues to be permitted under the AIFMD.

What is 'marketing' and reverse solicitation?

Marketing for AIFMD purposes, means any offering or placement of shares/units in AIFs at the initiative of the AIFM or on behalf of the AIFM to or with EU investors.

The use of third party marketing agents will not circumvent the provisions of the AIFMD. By including 'on behalf of the AIFM' within the definition, the AIFMD will capture marketing by third party distribution or placement agents and a manager will therefore be subject to the AIFMD marketing rules. Furthermore, the manager will effectively be responsible for compliance with the AIFMD by such distribution or placement agents.

The above definition does indicate, however, that passive marketing, or reverse solicitation, is not considered 'marketing' under the AIFMD i.e. if an investor approaches the manager about investing in a fund without prior solicitation, then on that basis the manager would seemingly not need to comply with the AIFMD as such marketing would not be at the initiative of the manager.

There is no firm guidance as to what constitutes reverse solicitation and a manager intending to rely on reverse solicitation will need to ensure that procedures and policies are put in place to clearly demonstrate that a particular EU investor invested in the fund on this basis. It will also need to ensure that follow up communications with such an investor do not result in active marketing, for example, of another fund. It is also important to note that reverse solicitation is construed tightly by the UK's FCA. For example, according to FCA guidance, documentation available on a publicly accessible website is not considered to be sent at the initiative of an investor; thus, open websites with free access to application forms and offering documents may prejudice reliance on the passive marketing exemption.

If a manager is unwilling to rely on reverse solicitation, then the only alternative at present for US managers is to market in accordance with existing private placement regimes for the reasons set out below.

Marketing under the private placement regime

EU-authorized AIFMs marketing an EU fund may take advantage of the 'EU Passport', but the EU Passport is not yet available for EU AIFMs marketing a non-EU fund and will not be available until 2015 at the earliest. Similarly, the EU Passport is not available for US managers marketing non-EU funds into the UK and EEA. In each case, these managers will need to market such funds under the existing private placement



regime (if any) in the relevant jurisdiction i.e. in accordance with local marketing rules.

The EU Passport regime may become available to non-EU managers from 2015, but this is subject to the European Securities and Markets Authority (ESMA) recommending that the passport is made available to them and the European Commission activating the passport provisions by adopting a delegated act. If the EU Passport regime is activated, all non-EU AIFMs managing or marketing AIFs in the EU will need to apply for authorisation, choose a “regulator of reference” within an appropriate EU jurisdiction (depending on various criteria) and comply fully with the AIFMD.

Until such time as the EU Passport is available, US managers are required to market their funds in accordance with the local rules applicable in each relevant jurisdiction.

It is important to note that provisions applying in one jurisdiction may not apply in other jurisdictions and it is possible that some Member States will impose requirements which are more restrictive than other Member States or may even remove the possibility of using any national private placement regime altogether.

Marketing in the UK

AIFMD Private Placement Regime

Subject to the transitional period, if relevant (discussed below), the AIFMD imposes a number of conditions upon private placement regimes, which must be met for a non-EU AIFM to be able to market its AIFs in the EU. These are as follows:

- (i) there must be a co-operation agreement/ memorandum of understanding (MoU) in place between the relevant Member State and the regulator of the fund’s jurisdiction;
- (ii) the fund’s jurisdiction must not be designated as non-cooperative by FATF; and
- (iii) the manager must comply with certain requirements of the AIFMD, namely the disclosure obligations (to investors), transparency requirements (to regulators)

and the annual reporting obligations of the AIF (please see below for more detailed information on each of these requirements).

The non-EU AIFM will not be able to market, or continue to market, in the EU after 22 July 2013 if any of these conditions are not satisfied. Furthermore, it is important to note (as mentioned above) that private placement regimes vary and Member States have the ability to impose stricter conditions in their private placement regimes or to ban private placements altogether at any time.

The UK has determined to leave its own private placement regime unchanged, however, with one exception, namely notification to the Financial Conduct Authority (‘FCA’) (see ‘Notification to the FCA’ below).

The FCA has currently signed MoUs with a total of 43 non-EEA authorities, including, for example, with those in the US (both SEC and CFTC), FINMA (Switzerland), the Cayman Islands, Bermuda, the British Virgin Islands, Jersey, Guernsey and the Isle of Man. For the complete list, which may be updated from time to time, please see the FCA website at: www.fca.org.uk.

If the first two conditions are satisfied, the US manager must then ensure that it complies with paragraph (iii) above, as follows:

Disclosures to investors

The manager is required to make initial and on-going disclosures to investors, which includes information on all fees, charges and expenses directly or indirectly borne by investors (as well as maximum amounts) and details of any preferential treatment provided to an investor or any special arrangements, such as side pockets. This will mean that offering documents will be required to contain certain obligatory disclosures and managers will need to make a checklist of AIFMD disclosure requirements and update offering memoranda and all marketing documentation where appropriate.



Transparency requirements

The manager must make an annual report available for each fund it markets, which must include disclosures in relation to the remuneration and management fees paid by the manager to its staff (including the total amount of carried interest payments made).

Reporting obligations to the FCA

The manager is required to report regularly to the FCA in relation to the percentage of the fund's assets which are subject to special arrangements arising from their illiquid nature and also reporting in relation to the main categories of assets in which the fund invests. For US managers, the reporting requirements are similar to Form PF, but it will not be possible merely to lift all the necessary information from one report into another, as the valuation and leverage calculations differ under the AIFMD.

Disclosure obligations on acquiring control of a company

If the fund acquires control (i.e. 50% or more of the voting rights) of a listed or unlisted EU company, certain disclosure and notification requirements will be applied, including the 'asset-stripping' provisions of the AIFMD, which the manager must make to the company, its shareholders and the FCA.

Notification to the FCA

As mentioned above, the FCA has introduced one new change to its private placement regime, the introduction of three private placement registers, two of which are applicable to US managers.

The notification requires confirmation from the manager that the management of the fund complies with the relevant conditions set out in the Alternative Investment Fund Managers Regulations 2013 (as amended), the regulations implementing the AIFMD into UK law.

These conditions vary depending on whether or not the manager is a 'small' AIFM i.e. broadly an AIFM who manages leveraged assets of below €100m (such as a small hedge fund) or who manages unleveraged assets of below €500m

where there are no redemption rights within five years of initial investment in the AIFs (for instance, a typical private equity fund).

The two registers relevant to a US manager are therefore:

- (1) Article 42 Register – for non-EU AIFMs that are not small AIFMs managing AIFs; and
- (2) Small third country AIFM Register – for non-EU AIFMs that are small AIFMs managing AIFs.

These forms can be found under Forms in the AIFMD section of the FCA website at: www.fca.org.uk.

Further details regarding the FCA's private placement regime can be found in the FUND sourcebook of the FCA Handbook at FUND 10.5.

Transitional period to 22 July 2014

EU AIFMs managing an AIF in the UK immediately before 22 July 2013 benefit from transitional relief in that they do not have to comply with the AIFMD rules in respect of either managing or marketing their funds in the UK until 22 July 2014. The Alternative Investment Fund Managers Regulations 2013 have clarified that this transitional relief extends to non-EU AIFMs as well.

Thus, US managers managing an existing AIF prior to 22 July 2013 will be permitted to continue marketing in the UK under the current financial promotion rules. The transitional relief also extends to any new funds in the UK, which means that a US manager, currently marketing its existing range of funds in the UK, may launch a new fund during the transitional period under the current financial promotion rules up to 22 July 2014.

As a result, US managers benefitting from transitional relief will not need to comply with the requirements of the AIFMD private placement regime set out above until 22 July 2014.



Marketing in the EEA

At the time of writing, not all Member States have fully transposed the AIFMD into national law and until transposition actually takes place, US managers should be able to market their funds via existing private placement regimes in that jurisdiction. Please note, however, that some Member States are contemplating the elimination of such regimes upon transposition, so any manager should conduct proper due diligence in each jurisdiction in which it is considering marketing, or continuing to market, its funds.

For those jurisdictions where the private placement regime will continue, the three private placement conditions (i) – (iii) set out above under ‘AIFMD Private Placement Regime’ in the UK section will apply. In addition to these, some countries require the fund to be registered and consent obtained from the local regulator while others, like the UK, simply require notification (i.e. no approval required) to the local regulator. Those requiring registration include Germany (BaFIN), Denmark (FSA), Norway and Sweden. Furthermore, some jurisdictions may impose further requirements; Germany, for example, requires the appointment of a depositary.

Similar to the UK, however, transitional relief periods of up to one year to 22 July 2014 are available in a majority of Member States, although Netherlands and Latvia appear to have limited this relief to domestic managers only and Germany and Denmark are extending it only to a manager’s existing funds as at 22 July 2013. Malta and Ireland, on the other hand, have granted a two-year relief period to non-EU managers.

Please note that the marketing of open-ended funds in France is generally not permitted under the private placement regime and that closed-ended funds may only use the private placement regime until 2015, when all managers will be required to market under the EU Passport.

As can be seen from the above, transposition of the AIFMD varies from country to country and it will therefore be necessary for a manager to

carry out sufficient due diligence, consulting with local counsel where appropriate, prior to carrying out any marketing in the EEA.

Marketing between 2015 and 2018

Although the private placement regime is expected to remain in place until at least 2018 (see further below), not all EEA countries may retain the regime if the EU Passport is introduced in 2015. The private placement regime is expected to remain in the UK until 2018, but managers will need to determine whether this will be the case in respect of each other jurisdiction at the relevant time.

Marketing after 2018

The private placement regime is generally expected to remain in place until at least 2018, at which time ESMA is expected to report on whether this regime should stay or be abolished. If it is abolished, the only marketing route available would then be the EU Passport, subject to ESMA’s recommendation as stated above. If that is the case, all non-EU managers who wish to continue marketing their funds in the EEA will need to apply for authorisation by a “regulator of reference” and comply fully with the AIFMD.

Conclusion

Post transposition of the AIFMD, a US manager wishing to market its funds in the UK should be able to continue marketing in the UK during the transitional period under the existing private placement regime and likewise after the transitional period, but subject to the disclosure and reporting obligations and the new FCA notification requirements, as set out above.

As regards marketing in the EEA, the US manager needs to take the following into account:

- is transitional relief available in the relevant jurisdiction in which it wishes to market its funds? If so:
 - does this extend to a non-EU manager?
 - does this extend to new funds or solely to funds existing as at 22 July 2013?
- is there an existing private placement regime



in the relevant jurisdiction in which it wishes to market its funds? If so:

- are the three minimum conditions be satisfied?
- are there any additional notification/ registration requirements?
- are there any depository requirements?

A manager will also need to bear in mind the introduction of the EU Passport from 2015 onwards (subject to ESMA advice) and consider what the benefits are of authorisation and the EU Passport as against the private placement regimes.

Should you wish to discuss any of the points raised in the above or any AIFMD issues in more detail, please contact Claire at Claire.Cummings@cummingslaw.com.

**This document is for general guidance only. It does not constitute advice
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