

ESMA issues advice on extension of the AIFMD Third Country Passport to 12 non-EU countries, including the United States

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Key takeaways

- ESMA has published advice on the extension of the AIFMD passport in respect of 12 non-EU countries, including the United States.
- In the case of the United States, the ESMA advice is broadly positive, although some reservations were expressed. Specifically, ESMA stated that while it saw no significant obstacles to the extension of AIFMD passport to funds marketed by US managers to professional investors which do not involve a public offering, it is concerned that extending the AIFMD passport to funds involved in public offerings could result in an unlevel playing field between EU and non-EU AIFMs.
- ESMA identified that there are no significant obstacles to the application of the AIFMD passport to Canada, Guernsey, Japan, Jersey, and Switzerland, and when assessed only in relation to AIFs (and not AIFMs), to Hong Kong and Singapore.
- Although the advice generally is positive in relation to Australia, some reservations were expressed that may result in changes to the Australian regulatory framework regarding the extension to all EU member states of the 'class order relief'.
- In relation to Bermuda, the Cayman Islands and the Isle of Man, ESMA was unable to issue definitive advice on some key criteria.
- The European Commission may set a date for the extension of the passport within three months of positive ESMA advice, however ESMA has indicated that EU institutions might wait until ESMA has issued positive advice on more non-EU countries before triggering the extension. The timetable for the extension of the passport to non-EU countries therefore continues to be uncertain.

Firms should continue to monitor whether or not the European Commission sets a date for the extension of the AIFMD passport to relevant non-EU countries and if it does set a date, to analyse whether they would wish to take up the passport.

- In the meantime, non-EU AIFMs and EU-AIFMs of non-EU AIFs should continue to market under each EU country's national private placement regime (if available).
- ESMA will continue its work on assessing whether the passport should be made available to relevant non-EU countries.

ESMA issues advice on extension of the AIFMD Third Country Passport to 12 non-EU countries, including the United States

The European Securities and Markets Authority (ESMA) today published its final advice (Advice) on extending the application of the marketing passport under the Alternative Investment Fund Managers Directive (AIFMD) to non-European managers.

The AIFMD applies to alternative investment fund managers (AIFMs) seeking to manage or market alternative investment funds (AIFs) in the European Union (EU). Currently, AIFMD's application to AIFMs not established in the European Union (non-EU AIFMs) is relatively limited and, as a consequence, these non-EU AIFMs do not have the same freedom as their European counterparties when seeking to market their funds across the EU.

The current position with respect to marketing under the AIFMD (and use of the passport provisions), for both the EU and non-EU AIFMs, is summarised below.

Current AIFMD position

EU AIFMs marketing AIFs

An EU AIFM that wishes to market an EU AIF must do so using the AIFMD marketing passport. This requires a notification by the AIFM to its home country regulator setting out specific information on the AIF to be marketed and list of the other EU countries into which marketing will take place. Within twenty (20) working days after the submission of this notification the AIFM is permitted to market the AIF to professional investors in the specified EU countries. It should be noted that some EU countries have "gold-plated" AIFMD, so that even with a passport, an AIFM nevertheless may be met with local representative and fee requirements, for example.

Non-EU AIFMs marketing AIFs in the EU and EU AIFMs marketing non-EU AIFs in the EU

The AIFMD marketing passport is not currently available for non-EU AIFMs wishing to market AIFs in the EU, for EU AIFMs marketing non-EU AIFs in the EU or in respect of EU AIFs that are feeder funds to non-EU master AIFs. Instead these managers must comply with the national private placement regime (NPPR) requirements for each of the EU countries into which they wish to market. These requirements differ between EU countries. In some cases (such as in the UK and Luxembourg) the NPPR requirements are relatively light, in others (such as in France and Germany) the requirements are more extensive, and in some EU countries marketing under the NPPR is not available at all (such as in Italy). The overall impact of AIFMD has been to limit the access that non-EU AIFMs have in raising capital from European investors; in circumstances where NPPR notifications have been made, non-EU AIFMs are subject to on-going requirements (such as periodic reporting) which have further increased the cost and regulatory burden of marketing in the EU. It should be noted that managers relying on the reverse solicitation "exemption" under AIFMD also face the issue of a difference in interpretation of the marketing behaviour that may constitute a valid reverse solicitation.

ESMA's advice

Background

Under the provisions of the AIFMD, ESMA had been tasked with assessing and advising on the possible extension of the marketing passport to non-EU AIFMs and also to AIFs which are currently subject to the NPPRs. In July 2015, ESMA assessed six jurisdictions and advised that there are no obstacles to the extension of the marketing passport to Guernsey, Jersey and Switzerland (subject to Switzerland enacting certain then-pending legislation). ESMA could not reach a definitive view on Hong Kong, Singapore and the United States (US), citing concerns on competition, regulatory issues, and a lack of sufficient evidence to properly assess the relevant criteria. ESMA then stated that it will continue to work on the assessment of the above countries. Australia, Bermuda, the Cayman Islands, Japan, Isle of Man and Singapore were added to the list of countries to be assessed at the request of the European Commission.

As well as the threshold criteria regarding co-operation arrangements, for each country, ESMA assessed whether there were significant obstacles regarding investor protection, competition, market disruption and the monitoring of systemic risk which would impede the application of the AIFMD passport. Each country was assessed separately.

A summary of the Advice is set out below.

US

There are no significant obstacles regarding investor protection and the monitoring of systemic risk which would impede the application of the AIFMD passport to the US. With respect to the competition and market disruption criteria, ESMA determined there is no significant obstacle for funds marketed by managers to professional investors that do not involve any public offering. However, ESMA determined that in the case of funds marketed by managers to professional investors that do involve a public offering, a potential extension of the AIFMD passport to the US risks an unlevel playing field between EU and non-EU AIFMs. The market access conditions which would apply to these US funds in the EU under an AIFMD passport would be different from, and potentially less onerous than, the market access conditions applicable to EU funds in the US that are marketed by managers involving a public offering. ESMA suggested, therefore, that EU legislators may wish to consider possible options including:

- granting the AIFMD passport only to those US funds dedicated to professional investors to be marketed in the EU by managers that do not involve any public offering;
- granting the AIFMD passport only to those US funds that are not mutual funds (under the US Investment Company Act of 1940); and
- granting the AIFMD passport only to those US funds that restrict investment to professional investors as defined in AIFMD.

It should be noted that these issues appear to be less relevant to the offering of private investment funds which tend to be offered by way of private placement.

Canada, Guernsey, Japan, Jersey and Switzerland

There are no significant obstacles regarding investor protection, competition, market disruption and the monitoring of systemic risk impeding the application of the AIFMD passport to these countries.

Hong Kong and Singapore

ESMA only considered the position in relation to AIFs, and not AIFMs, in these countries and concluded that there are no significant obstacles regarding investor protection, competition, market disruption and the monitoring of systemic risk impeding the application of the AIFMD passport.

However, ESMA did note that both Hong Kong and Singapore operate regimes that facilitate the access of undertakings for collective investment in transferable securities (UCITS) only from certain EU countries to retail investors in their territories. Nevertheless, because the UCITS regime is essentially a regime that facilitates marketing to retail investors and the AIFMD is essentially a regime that enables marketing to professional investors, this did not create an obstacle to competition.

Australia

There are no significant obstacles regarding investor protection, monitoring systemic risk, market disruption and obstacles to competition impeding the application of the AIFMD passport to Australia, provided (in relation to market disruption and obstacles to competition) the Australian Securities and Investment Commission extends to all EU Member States the 'class order relief', currently available only to some EU Member States.

Bermuda and Cayman Islands

There are no significant obstacles regarding competition, market disruption and the monitoring of systemic risk impeding the application of the AIFMD passports to these countries.

However, in respect of the investor protection criterion, ESMA's view is that no definitive advice may be given until AIFMD-like regimes that are referenced in the Advice are adopted. Specifically, in respect of the effectiveness of enforcement assessment in relation to the investor protection criterion, the Advice references a review of regulations (in the case of Bermuda) and a legislative amendment (in the case of the Cayman Islands) that may address this criterion. ESMA states that it is unable to issue definitive advice until such review is completed and legislative amendment is adopted.

Isle of Man

There are no significant obstacles regarding competition, market disruption and the monitoring of systemic risk impeding the application of the AIFMD passports to the Isle of Man. However, ESMA's view is that the absence of plans to put in place an AIFMD-like regime makes it difficult to assess the investor protection criterion. With respect to the assessment of the effectiveness of enforcement, ESMA could not provide a more thorough assessment at the time of the publishing of the Advice.

Other issues

In addition to the non-EU jurisdictions identified above:

- ESMA has surveyed EU countries and drawn up a list of other non-EU countries that might be included in an assessment of whether the AIFMD passport should be extended to them. These countries are: Bahamas, Brazil, British Virgin Islands, Curacao, Mexico, Mauritius, South Africa, South Korea, Thailand and the US Virgin Islands. ESMA states that the assessment of the 12 countries covered by the Advice could then be followed by assessments of "other non-EU countries beyond June 2016"; and
 - ESMA has gathered intelligence on investor protection, competition, potential market disruption and monitoring of systemic risk with respect to the following non-EU countries: Malaysia, Egypt, Chile, Peru, India, China and Taiwan. ESMA noted that these countries have not been assessed in any detail at this stage due to no memorandum of understanding being in place between national regulators in EU countries and the national regulators of the above non-EU countries or there being a lack of management and/or marketing activity linking these countries to the EU.

Next steps in the legislative process

The Advice is addressed to the European Council, the European Parliament and the European Commission. Of particular interest is the fact that, as noted by ESMA in the Advice, the Advice in some cases cannot be considered positive. Under AIFMD, the European Commission must adopt a delegated act within three months of having received a positive opinion from ESMA, specifying the date on which the third country passporting rules will apply. However, ESMA also indicated in the Advice that the European Council, the European Parliament and the European Commission should consider waiting until ESMA has delivered positive advice on a sufficient number of non-EU countries before triggering the extension of the passport to non-EU countries. The earliest date for the extension of the AIFMD passport to non-EU countries was October 2015. Given the delays to the extension of the AIFMD passport, the European Commission may feel that it is unable to agree to further delays. Of course, this would need to be balanced against the adverse impact of extending the passport only in respect of a limited number of non-EU countries.

The timetable for implementation of the extension of the AIFMD passport to non-EU countries otherwise remains unclear at this stage.

Next steps for managers

Managers should continue to monitor whether the European Commission will set a date for extending the passport to non-EU countries. For the time being, in practice non-EU AIFMs and EU AIFMs of non-EU AIFs will likely need to market AIFs under each EU country's NPPR or, where available, pursuant to reverse solicitation. However, if a date is set for extending the passport to non-EU countries, managers will need to analyse their position in terms of (a) accessing the AIFMD passport, and therefore likely needing to comply with nearly all of the AIFMD (including the requirements on remuneration, for example), or (b) continuing to utilise NPPRs, to the extent that these regimes are available. It is not known what approach may be taken by EU countries to the availability of NPPRs in the event that the AIFMD passport is extended to non-EU countries. Also, it should be noted that if the European Commission decides to extend the AIFMD passport to non-EU countries that a three year period is triggered after which AIFMD NPPRs may be switched off.

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