

AIFMD adopted!

On 11 November 2010, the AIFMD has been passed by the European Parliament

After nearly 19 months of heated and controversial debates, both at an industry and at a political level, the final text of the Alternative Investment Fund Managers Directive (“AIFMD”) has been adopted on its first reading in the European Parliament plenary session on 11 November 2010. The AIFMD will now enter into force around Christmas 2010, with Member States required to implement the Directive into their national laws within two years, i.e. in early 2013.

The most controversial part of the AIFMD has been the rules governing access to EU markets for non-EU alternative investment managers (“non-EU AIFM”) and alternative investment funds (“non-EU AIF”). Here a workable compromise has been reached. Non-EU AIFM and non-EU AIF will have the opportunity to benefit from the same pan-European marketing ‘passport’ as their EU competitors by 2015, should ESMA approve it.

However, once set in force, the AIFMD will not only harmonise the marketing rules of alternative products but also radically modify the whole regulatory framework which the European Non-UCITS industry has to comply with. It will introduce requirements for AIFMs as well as requirements impacting AIFs directly, especially their investment strategies.

Due to its very wide scope, this new regulation will have a massive impact on nearly all market players (currently regulated or not, in or outside the EU) and on their existing business models. They will have to review and adapt their existing set-ups and the way they operate.

Key provisions

An AIFM is defined as any legal person whose regular business is providing at least portfolio or risk management services to one or more AIF. The AIFMD however foresees some exemptions (e.g. AIFM managing AIF with AuM not exceeding €100 million or under specific conditions €500 million).

The definition of AIF covers any (open-ended or closed-ended) collective investment undertaking raising capital from a number of investors, with a view to investing it in accordance with a defined investment policy for the benefit of those investors and which does not require authorisation pursuant to the UCITS regime. However, the AIFMD states some exemptions (e.g. managed accounts, holding companies, pension funds, securitisation vehicles)

From a geographical viewpoint the AIFMD will apply to all AIFMs established in the EU managing AIFs, irrespective of the AIF’s domicile, and to non-EU AIFMs managing EU AIF or non-EU AIF marketed to EU investors.

Thus, all EU managers managing non-EU hedge funds, and the currently not-regulated private equity and real estate houses based in the EU, will be within scope.

Even EU managers of non-EU funds not marketed to EU investors will be caught. Moreover, the Directive will also apply to US, Asian and other non-EU managers of AIFs which will be marketed to EU investors.

All AIFMs in scope will have to adapt particularly to the following AIFMD requirements:

- **Authorisation:** The AIFM will have to be authorised pursuant to a harmonised procedure;
- **Capital requirements:** The AIFM will have to comply with minimum capital requirements similar to those of the UCITS Directive;
- **Remuneration:** The AIFM will have to set-up remuneration policies and practices, notably being consistent with the effective risk management and designed to avoid non appropriate risk-taking;
- **Valuation:** The AIFM will have to set-up appropriate and consistent valuation procedures ensuring at least a functional independence between the valuation function, portfolio management and the body defining the AIFM remuneration policy;
- **Depository:** The AIFM will have to ensure that for each AIF a depository is appointed. The AIFMD provides in this context a clear definition of entities which may act as depository and the permitted domiciles. It defines the duties of the depository, which are not limited to the safekeeping of the assets but also include a monitoring / supervisory function. Moreover, the AIFMD provides rules regarding the delegation of safekeeping functions. Finally it defines rules regarding the liability of the depository taking into account the different duties and different potential set-ups (e.g. the use of sub-custodians);
- **Delegation:** The AIFM will have to comply with delegation requirements similar to those of the UCITS Directive;
- **Operating conditions:** The AIFM will have to comply with specific substance, conflict of interest, risk management and liquidity management requirements;
- **Reporting and disclosure:** The AIFM will have to comply with several reporting and disclosure requirements vis-à-vis the regulators and the authorities;
- **Limitations on leverage:** The AIFMD will empower the home Member States regulators to set limits on the level of leverage employed by an AIFM. Moreover, AIF employing leverage on a substantial basis will be subject to additional disclosure requirements to regulators and investors;
- **Investments in non listed companies and issuers:** The AIFMD imposes notification duties and disclosure requirements regarding major holdings and control of non-listed companies (regulators, non-listed company, shareholders), introduces specific provisions regarding the annual report of AIFs controlling non-listed companies and sets rules regarding asset stripping;
- **Marketing provisions:** The AIFMD regulates the marketing of EU AIFs and non-EU AIFs, managed either by an EU AIFM or a non-EU AIFM, to MiFID professional investors domiciled within the EU. It is understood that passive marketing/reverse solicitation remains outside of the scope of the Directive.

With at least 48 subsidiary pieces of technical guidelines, rule making, interpretation and review to follow, many more details on how AIFMD will apply in practice will emerge over the coming months.

The “dual system”

The AIFMD introduces a passport for EU AIFMs managing EU AIF. They will be able to market to MiFID professional investors as from 2013 cross-border with a passport as long as they comply with the AIFMD.

Conversely, additional rules apply for the marketing of non-EU AIFs (managed by EU AIFMs or non-EU AIFs) and EU AIFs managed by non-EU AIFMs. In these cases the AIFMD provides for at least a specific period a dual system combining an EU passport with private placement regimes:

- **From 2013 until 2018** national private placement rules will remain possible under certain conditions;
- **From 2015**, a parallel passport regime will be introduced, which will permit non-EU AIF to be distributed on a pan-EU basis, provided certain criteria are met and the new European Securities Markets Authority (“ESMA”) approves them;
- **In 2017** ESMA will review the operation of the private placement regime and recommend whether it will be continued or terminated.

How will Luxembourg be affected?

The AIFMD will heavily affect the non-UCITS sector in Luxembourg (i.e. all funds governed by part II of the Law of 20 December 2002 relating to undertakings for collective investment, all SICARs, SIFs and a lot of currently non-regulated investment vehicles and platforms). The Luxembourg AIFM of these vehicles (e.g. their management companies) will have to analyse the AIFMD impact on their set-up and on the business model used. Moreover, all service providers of Luxembourg AIF (e.g. depositories, asset managers, investment advisors, administrators, transfer agents etc) will have to take the necessary steps to comply with the AIFMD.

However, Luxembourg seems to be very well positioned to face the challenges linked to the AIFMD, as many of the requirements in the new Directive exist today in the Luxembourg legal and regulatory framework applicable to non UCITS funds (e.g. the need for a depository). Besides, the expertise of the Luxembourg financial community in the field of regulated alternative products (e.g. hedge funds or private equity funds) is such that Luxembourg will be able to respond in a quick and efficient manner to the challenges of the AIFMD. To support our clients in this, PwC ACADEMY is offering public half-day training sessions on the topic on December 8 (English), 10 (German) and 13 (French).

In conclusion, the AIFMD could turn out to be a new and major opportunity for the Luxembourg financial sector. It will require investments and efforts but Luxembourg has all the key attributes to become the global AIF platform of tomorrow.

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