

# PASSPORTING AND DISTRIBUTION UNDER THE AIFMD

PAOLO BRIGNARDELLO OF FUNDSQUARE DISCUSSES KEY CONSIDERATIONS AROUND DISTRIBUTION UNDER THE DIRECTIVE'S NEW REGIME



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joined Fundsquare in 2013 as head of product management and marketing. He is responsible for strategic product positioning and evolution. In his role, Paolo carries out product portfolio management and product development initiatives by assessing markets' evolution against product capabilities.

**A**t the starting point of AIF distribution following the implementation of the AIFMD on 22 July 2013, there are now concrete plans underway for the distribution of products under this new regime. Changes in passporting and distribution, as well as marketing to professional and retail investors, are still something the industry is coming to terms with.

The AIFMD is also set to change onshore and offshore strategies. With many groups today, offshore funds will most likely remain offshore for a period of time, allowing managers to fully understand the impact of this regulation. However, the medium- to long-term outlook will most likely see a shift of distribution to what will be the most profitable jurisdictions. The AIFMD covers a wider variety of vehicles than those covered under Ucits IV including retail-oriented, such as fund of funds and master-feeder structures, and institutional or professional oriented funds, such as closed-ended funds and real estate funds.

## PASSPORTING UNDER THE AIFMD

The possibility of passporting under the AIFMD has given managers a new opportunity to operate both Ucits and an AIF under a single company authorised to manage both types of funds, known as a Super Management Company (Super ManCo). The primary benefit of a Super ManCo is the lower cost as there is no need for the duplication of the technical infrastructure that is common of both Ucits and AIFs. The Super ManCo approach may also have limited capital implications as Ucits management companies' capital requirements are equivalent to those for AIFMs.

There is likely to be an increase of Super ManCos as a result of the AIFMD. However there are complexities around operating these in multiple jurisdictions. Managers who have products in different locations will face the challenge of complying with different local authorities with different interpretations of the Directive's requirements.

The AIF passporting will benefit from what has already been put into place under Ucits IV and for those who already run Ucits products, the process is not anything new. The passporting request procedure is complex, and although there are a number of service providers who understand and are able to offer assistance for this process, the real difficulties come for managers who have products

in multiple jurisdictions in complying with the differing local administrative procedures and specific rules of the requirements.

However the AIFMD has given some guidelines as to the necessary passporting process. In order to be certified that the AIFM conforms to EU law, the following evidence needs to be provided:

- Information on the legal representative, the depositary and the payment agent including confirmations by such parties that they assume their respective roles.
- Investment terms, articles of association or partnership agreement, the prospectus and the key investor information document.
- Last annual report and financial statements. Information on the intended sales process.
- Undertaking by the AIFM that it will fulfill certain obligations with BaFin.
- Documents and information that the AIF and the AIFM are effectively supervised in their country of domicile.
- Requisite agreements for master/feeder structures, if applicable.

Co-operation agreements for passporting must also be in place between regulators in the member states where the AIFs are established, where they are marketed, and the home country of the AIF, all which must not be considered non-co-operative countries by FATF.

## MARKETING TO PROFESSIONAL INVESTORS

Under the AIFMD, marketing is defined as 'any direct or indirect offering or placement at the initiative of the AIFM or on behalf of the AIFM of units or shares in an AIF it manages to or with investors domiciled in the Union.' When taking this wording into consideration, it becomes clear that reverse enquiries by the investors, thus 'passive' marketing, by the AIFMs would not be caught under the definition of marketing by the Directive.

NPPRs will be the only regime available to non-EU AIFMs for marketing within Europe until 2015. There are different interpretations nationally of what constitutes as professional investor or private placement. As of today, only 17 countries (Luxembourg included) have decided to allow private placements as of September 2013.



### MARKETING TO RETAIL INVESTORS

The Directive states that EU member states may allow EU and non-EU AIFMs to market to retail investors regardless of where the AIF was established or whether it is being marketed on a domestic or cross-border basis but the member state can impose stricter requirements on this marketing than that of professional investors. The member states are also required to notify the European Commission and Esma of any additional requirements.

### DISCLOSURE AND ONGOING TRANSPARENCY

One of the challenges surrounding the AIFMD will be the detailed amount of information that is required to be disclosed to investors, as provided in Article 23 of the Directive. The AIFMD also requires periodical disclosure of the AIF's assets. The disclosure and reporting requirements under the AIFMD are split into three groups: initial disclosures to investors, ongoing disclosures to investors and information required to be reported to regulators.

The disclosure required includes the type of investment vehicle, investment strategy, leverage, collateral, how changes in strategy may be implemented, service providers (such as AIFM, depositary, valuer, auditor, prime broker etc), valuation procedures, fees and expenses, provisions to ensure fair treatment of investors, subscription and redemption procedures and liquidity management procedures. Material changes to this information must also be disclosed to investors, and any change to depositary liability must be notified without delay.

The AIFMD also requires additional information, which may not currently be included in an AIF's prospectus, to be disclosed to investors prior to their initial investment, including a description of how the AIFM is complying with the requirement that it have additional funds to

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cover the potential liability risks arising from professional negligence or to hold professional indemnity insurance against liability arising from professional negligence, the latest net asset value of the AIF or the latest market price of the unit or share of the AIF, and the historical performance of the AIF.

A warning that I would give to managers at this stage of implementation is that while there has been a lot of focus on looking at the regulatory reporting to comply with the label, now it is time to really look at becoming compliant with the requirements of distribution. Most managers have been scrambling to get licensed for their product but now it is time to look at how to be compliant with the distribution obligations, not only the passporting, but also the disclosure to investors, ensuring that the investors receive the right documentation prior and during the relationship of them investing in the product.

Fundsquare provides a full range of products within the regulatory services space. We focused on providing the fund industry with tools aimed at further harmonising interactions with regulators and handling a network of regulators both European and outside. We have built the capability throughout the years and, of course, with the compulsion of the Ucits directives. When the Ucits directives entered into the game and there was the need to passport the product across Europe and beyond, Fundsquare built work flow tools to allow management companies to report directly to those authorities to follow up on what the authorities were agreeing or not on passporting of a specific product and then supporting the dissemination to other authorities of all the documentation required to maintain passport. It is really about managing a network of authorities for the ease of the fund distribution. ■