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Bespoke Fund Passporting

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The Capital Markets Union is an ever-ambitious endeavour of the European Commission to create a seamlessly integrated cross-border capital market in Europe. In light of increasing constraints faced by banking institutions, traditionally the exclusive avenue utilised in Europe to source capital by SMEs, the European Commission is set on a journey to provide new sources of financing to SMEs and, at the same time, new investment opportunities for retail savers.

It is within such context that in March 2018 a set of proposals were issued by the European Commission for a Directive and a Regulation, both impacting with a package of varied measures the cross-border fund distribution arena. The rationale for the proposals is twofold. On the one hand, support further growth of cross-border fund distribution activities across Europe and, on the other, bolster competition and allow for a more diversified offer of products to investors. The measures envisaged in the European Commission proposals aim at enhancing and facilitating European cross-border fund distribution with specific provisions to amend, amongst other things, both the UCITS and the AIFM directives. These amendments are tabled with a view to reduce regulatory barriers currently faced by fund managers as well as related costs for them to be able to offer their funds cross-border in Europe.

However, having taken a close look at these proposed measures, we notice that the intent of the European Commission to foster competition in the cross-border fund market does not equate per se to a liberalisation of that specific market. Especially when it comes to the so called third-country (i.e. non-European) managers and funds, in AIFMD parlance. In fact, the piecemeal approach now adopted by the European Commission to amend the AIFMD as part of the Capital Markets Union legislative endeavour, when an ad-hoc overhaul of the same directive was intended to have taken place already in 2017 per se, has inevitably some side effects. Be it unintentional or not, one of the consequences of these proposed amendments is to restrict even further the ability of non-EU fund managers to offer their strategies to European investors.

US fund managers need to pay attention to the proposed amendments to AIFMD, so as to have a

clear strategy in place, well ahead of the enactment thereof, to either obtain or retain access to investor base in Europe for their strategies.

One of the most relevant provisions part of the package proposed by the European Commission is the one introducing a new concept of *pre-marketing* within the AIFMD ecosystem. We expect that in certain European domiciles this newly introduced concept will alter substantially the existing dynamics that govern the way foreign and US fund managers approach European investors. We encourage US fund managers to pay particular attention to the implications that pre-marketing will have on how their non-EU funds will be offered going forward to investors in certain parts of Europe. This analysis becomes even more important in a current scenario where the extension of the AIFMD passport to non-EU AIFMs apparently will take longer than initially envisaged in the text of AIFMD to be enacted, if at all.

Third-country AIFMD Passport

The whole spectrum of the European regulation on financial services provides for mechanisms of recognition of market participants from third-countries. AIFMD of course also caters for such third-country recognition process by means of an extension to non-EU AIFMs of the marketing passport. The implementation of this recognition process though has been delayed so far, leaving the private placement regimes - provided at local level by national legislation of certain European domiciles – the only feasible option for third-country AIFMs to access European investors.

Two main events were scheduled in the AIFMD space for 2017 but none of these have occurred. The first one was the overhaul of AIFMD and the second, instead, the extension of the passport to third-country AIFMs. Yet, despite this delay, AIFMD indeed contained specific set deadlines for enactment of the extension of the passport, respectively 2015 for completion of the assessment to be carried out by ESMA on third-country domiciles and 2018 for the implementation of the actual extension of the passport, further to delegated acts from the European Commission. As at today, whilst the vetting process of third-countries has been exhausted and there are two sets of advice rendered by ESMA on the point, there is no single delegated act from the European Commission. Instead, the European Commission decided to adopt a piecemeal approach towards the revision of AIFMD and table an ad hoc set

of amendments as part of a different exercise and within a different context. The newly introduced concept of pre-marketing, for instance, seems also to go in the exact opposite direction of a more liberal stance towards third-country managers and funds as originally envisaged in the AIFMD – and generally across the board of all the European financial services regulation - with the extension of the passport to third-country AIFMs.

The Current Status of Marketing and Pre-Marketing

AIFMD defines marketing - for the first time in the European financial services regulation - as the direct or indirect offering or placement at the initiative of, or on behalf of, an AIFM of units or shares of an AIF it manages to or with investors domiciled or with a registered office in the European Union.

It is noteworthy to mention that one of the gaps in the European regulation on financial services is currently found around the concept of marketing of investment products. In fact, there seems to have been for the time being no real endeavour initiated by European institutions to regulate this topic and stipulate what marketing of investment products should be at a more general level in Europe. Accordingly, marketing is governed at a local national level in very different ways, sometimes on the basis of obscure local administrative practices of national regulatory authorities, not better codified nor easily accessible to the public. AIFMD in this sense made a first step in the right direction by providing for a definition of marketing, aimed at creating consistency in Europe around this concept. The intent underpinning the introduction of such definition was to ensure that there was more clarity around the activities that would have triggered the requirement for a marketing notification under AIFMD versus other activities that would not necessarily amount to marketing as such. In consideration of the nature of directive of the AIFMD and the consequent ability for Member States to retain some wiggle room in the actual implementation of directives in local legislation, the concept of marketing so introduced has been adapted to current local practices existing in the various European domiciles on the subject.

The premise for the introduction of a concept of pre-marketing, as part of the recent proposal of the European Commission, lies in a very common practice in the alternative investment fund ecosystem, whereby fund managers are used to test

with perspective investors the interest and appetite for certain strategies before proceeding with the establishment of an alternative investment fund.

According to the European Commission, whilst the concept of pre-marketing is again very varied across Europe, there are also some European domiciles where no pre-marketing activities are allowed whatsoever. The introduction of this concept then, at least prima facie, may seem to be welcome news especially in light of the fact that pre-marketing activities will now be allowed also in European domiciles where these was not a possibility before. On the flipside to this, however, considering the standard conditions for pre-marketing identified in the European Commission proposal, we notice that a more restrictive benchmark for pre-marketing activities has been adopted than the one currently applicable in certain European domiciles.

The proposal at issue for the amendment of AIFMD defines the below as the information that, once shared with investors, exclude the pre-marketing:

- relates to an established AIF;
- contains reference to an established AIF;
- enables investors to commit to acquiring units or shares of a particular AIF;
- amounts to a prospectus, constitutional documents of a not-yet-established AIF, offering documents, subscription forms or similar documents whether in a draft or a final form allowing investors to take an investment decision.



Considerations on the New Concept of Pre-Marketing

We must note that the approach underpinning the new definition of pre-marketing is not entirely divergent from the common practice currently in place in the European domiciles where pre-marketing is already possible at the moment. In fact, even before this definition was proposed, in order for certain activities towards investors to be characterised as pre-marketing, the fact that fund documentation was not in final form has always played a pivotal role. If nothing else, a marketing notification with any regulatory authority requires fund documentation in final form to be provided as part of the notification package.

The whereas of the proposal for a Directive give some further grounds of analysis on the concept of pre-marketing. There is firstly a reference to the fact that pre-marketing concerns exclusively an investment idea or strategy and that, consequently, an alternative investment fund should not be in existence or established already in order for any approach towards investors to fall under this category. Also, it is pointed out in the whereas that, in the course of pre-marketing activities, investors cannot subscribe to an alternative investment fund and no fund documentation, even in draft form, can be circulated with investors is also pointed out.

Whilst on the one hand we see that the proposal of the European Commission may have some value, especially when we consider that the concept of pre-marketing will be now available also in European domiciles where this didn't exist per se before, on the other, there are some consequences, be unintended or not, that one must take into account.

If the proposal is implemented in its current form, the fact that circulation of fund documentation in draft form to investors will not be allowed without a marketing authorisation obtained will alter substantially the way deals in the alternative investment fund ecosystem will be carried out and will make even more problematic the approach to investors in domiciles where the national private placement regime has longer gestational periods.

It is noteworthy to mention that one of the gaps in the European regulation on financial services is currently found around the concept of marketing of investment products. In fact, there seems to have been for the time being no real endeavour initiated by European institutions to regulate this topic and stipulate what marketing of investment products is supposed to be at a more general level in Europe.

Accordingly, marketing is governed at a local national level in very different ways, sometimes on the basis of obscure local administrative practices of national regulatory authorities, not better codified nor easily accessible to the public. AIFMD in this sense made a first step in the right direction by providing for a definition of marketing, aimed at creating consistency in Europe around this concept.

The intent underpinning the introduction of such definition was to ensure that there was more clarity around the activities that would have triggered the requirement for a marketing notification under AIFMD versus other activities that would not necessarily amount to marketing as such. In consideration of the nature of directive of the AIFMD and the consequent ability for Member States to retain some wiggle room in the actual implementation of directives in local legislation, the concept of marketing so introduced has been adapted to current local practices existing in the various European domiciles on the subject.



How to Manage European Fund Distribution

(<http://www.venezianoandpartners.co.uk/manage-fund-distribution/>)

Whether you are planning to start a European fund distribution project or you are already successfully distributing your funds in Europe – or in between the two – and you are dedicated to **SUCCESS** and **GROWTH** you are just in the right place. We worked with a multitude of fund managers already and know exactly what are the hurdles hindering the **GROWTH** of European fund distribution projects. We have also seen that these obstacles increase and inefficiencies and costs amplify as the projects evolve.

Think about it – the biggest fund management houses, the ones with pan-European reach for their fund products, all have a dedicated fund registration and distribution team. This is not by chance. The uninterrupted pace of new European regulation, affecting various aspects of European Fund Distribution, as well as the multitude of different solutions offered today in the market for various reporting and ensuing data management needs makes the task of distribution a very burdensome one, needing a dedicated team of hands-on professionals.

On the one hand, having an in-house dedicated fund registration and distribution team is an expensive commitment and holds back many fund managers. Seconding this function to an existing internal department, on the other hand, or else outsourcing it entirely, in a non-centralised manner to external counsels for each jurisdiction, could be a very expensive mistake. And this is exactly why so many otherwise great fund managers, with appealing strategies and stories, will never actually be able to let their European Fund Distribution grow.

At Veneziano & Partners we are a niche in the niche firm in this sense. We function for our clients as an Outsourced Fractional Fund Registration and Distribution Team. Because it is impossible to have a successful European Fund Distribution if you don't have a dedicated team.



Veneziano & Partners

Veneziano & Partners is an international consulting boutique specialised in the European regulation of cross-border fund distribution. In catering to a selected group of investment managers, hedge fund managers and financial institution worldwide, the firm offers a custom-made global fund registration services, enabling its clients to gain competitive advantage in an ever increasingly regulated environment.

Attilio Veneziano is a dual qualified lawyer with more than 15 years international experience. Attilio began his career as a practitioner in European extradition law and then moved in-house at major financial institutions with a focus on the offshore investment funds industry. Veneziano & Partners was founded in London in 2013 to respond to the rising demand by global fund managers for centralised compliance solutions, in the aftermath of AIFMD implementation, for European cross-border fund distribution.

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