

The draft AIFM Directive

This Autumn will determine its fate and its shape

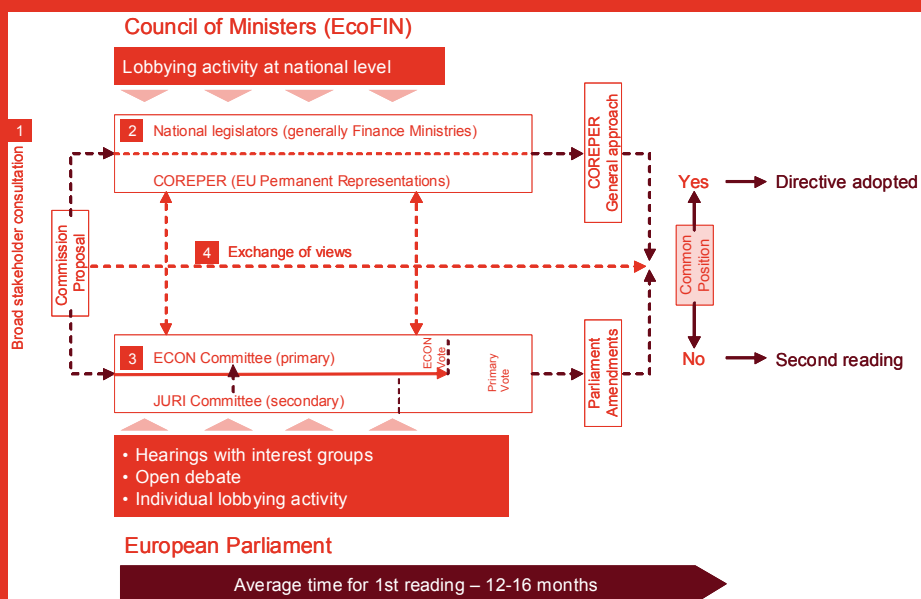
September 2009 | Edition 1



Introduction

Released on 29 April, the European Commission's draft Alternative Investment Funds Management Directive (AIFM Directive) has caused waves of consternation across the industry in Europe and further afield. However, the key issues are likely to be addressed during the co-decision negotiations between the Council of Ministers and the European Parliament over the coming weeks.

Clearly, this Autumn will determine the shape of the legislation that eventually comes into play. What this will be is, as yet, far from clear. But what is clear is that some form of legislation - impacting the alternative investment industry very broadly - will be introduced.



Progress of the legislation

In terms of discussions on the draft text proposed by the European Commission, the Council of Ministers has had a head start over the European Parliament and has held some five meetings to date. Discussions to date have enabled the Council to home in on some difficult areas of the proposals, as demonstrated by a recently released 'issues note' by the Swedish Presidency whose role is to facilitate and guide discussions in Council in order to reach consensus. More meetings will be scheduled for September and, at this stage, it seems possible that the Council may develop its compromise position by October.

The Swedish issues note focuses on key areas for further study and debate in the Council, including:

- The scope of the Directive and how alternative investment funds caught by it should be defined. The Presidency believes the discussions should start from the 'notion of a collective investment undertaking'.
- Exemptions (currently extremely limited) generally and further clarification or removal of the proposed de minimis thresholds.
- The need for double authorisation as established in the proposal (e.g. in terms of UCITS management companies).

- Key definitions to be used such as those for 'management services', 'marketing' and 'leverage'.
- Capital requirements and the possibility of better aligning the requirements with those in the UCITS IV Directive.
- Enhanced clarity over the responsibility for valuation depending on the business model (and business sector) involved.
- Restrictions on and role of depositaries (considering not least the issue of liability).
- The approach to delegation, not least in terms of business outside the European Union.
- The definition and calculation of leverage.
- The obligations (proposed under Articles 26-30 of the draft directive) for AIFMs which manage investment funds which take controlling stakes in companies.
- Third country issues, with a view to avoiding barriers to the global capital flows.
- Supervision in terms of powers of a host supervisory authority.

Adhering to its facilitator role, the Swedish issues note puts forward various options for consideration without (often) stating its own preference. Although it is not clear what the outcome of the discussions in Council will be at this stage, it does appear that some of the more contentious issues will be considered fully. The Swedish Presidency's transparent approach, in making this document public, demonstrates its desire to keep the wide group of stakeholders informed (as there can be no formal consultation with stakeholder groups at this stage in the legislative process), and also to provide the Economic and Monetary Affairs Committee (ECON) of a clear indication of the progress made in the Council.

It is worth noting that there is another important issue, flagged by industry, which is not explicitly addressed in the issues note - that of private placement. There are doubts whether current private placement practices would be permitted were the Directive to be introduced as currently proposed. Because of the potential implications for European investor access to global capital, this is also an area which warrants further attention.

In terms of the European Parliament, following the elections in June 2009, the key Parliamentary committee to conduct the negotiations - ECON - was constituted over the summer. Allocation of the AIFM dossier was only confirmed at the first exchange of views in ECON on 2 September 2009 when Jean-Paul Gauzès, a French MEP representing the EEP party, was assigned the role of lead rapporteur. As such, M. Gauzès will be responsible for developing an initial report and then pulling together amendments proposed by members of ECON to formulate the Parliamentary position to be discussed with the Council. A veteran of the European Parliament, M. Gauzès has proven his ability to guide controversial proposals through the co-decision procedures in first reading, acting as rapporteur on the recently adopted directive on credit rating agencies.

What should you be doing?

- **Don't sit back.** The 'one-size-fits-all' approach adopted by the Commission does create significant possibilities for 'unintended consequences' for different business models. While the Council has evidentially identified some of the key issues, there may still be other issues in the detail which need further attention.
- **Engage in the debate.** The co-decision makers – the Council and the European Parliament – are keen to engage with industry to develop workable solutions. As the first exchange of views in Parliament shows, there is a recognition that this legislation cannot be allowed to jeopardise European investors access to global capital flows. It is still important for all parts of the industry to engage in the debate directly or through industry associations. And not just market participants themselves, the voice of institutional investors – such as the Association of British Insurers and a combination of Dutch pension funds and institutional investors which have spoken out recently – has a strong weight in the debate.
- **Begin to consider your future options.** Just because your business model works today may not be enough to justify its preservation 'as is' under the new regime. Begin to consider the possible impact of the different options outlined by the Swedish Presidency, and the reaction to the legislation by other players, not least those operating in third countries.

Key considerations

There is still time to contribute.

From our discussions with stakeholders, it is clear that there is a strong commitment by many in Brussels and elsewhere to 'get this right' and to ensure the European alternative investment industry is made safer but that the interests of European investors are not damaged in the process.

Don't be complacent, talk to us, engage with MEPs, regulators and your own clients and share your concerns.

If you like to discuss any of the areas covered in this paper as well as the implication for your business, please speak with your local PricewaterhouseCoopers contact or one of our AIFM specialists listed below:

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