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Gide Loyrette Nouel



November 2010

The Alternative Investment Fund Managers Directive – What Does The Future Hold?

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Application: Where

- All EU AIFM irrespective of where the Alternative Investment Fund (“AIF”) is established;
- All non-EU AIFM which manage an EU AIF; and
- All non-EU AIFM which market an EU or non-EU AIF in the EU.



Application: What

- Management of AIF means at least providing investment management services of portfolio and risk management.
- May also include administration, marketing and activities relating to assets of the AIF and, subject to authorisation under the UCITS directive, additional management of UCITS.
- Member States may permit AIFM to also manage individual portfolios, provide investment advice, safe-keeping and administration in relation to shares or units of collective investment undertakings and reception and transmission of orders for financial instruments.



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Application: Who

- AIFM includes any legal or natural person whose regular business is to manage one or more AIFs.
- AIF defined as any "collective investment undertaking" which raises 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 is not a UCITS. Family offices not considered AIFs.
- Broadly, definition includes all funds except UCITS, so managers of hedge funds, private equity funds, commodity funds, venture capital funds, real estate funds and investment trusts are within scope.



Application: Exemptions

- Holding companies (save that this will not exclude managers of private equity funds, nor managers of alternative investment funds whose shares are admitted to trading on a regulated market)
- Management of pension funds, employee participation or savings schemes
- Supranational institutions
- National central banks
- National, regional and local governments and bodies or institutions which manage funds supporting social security and pension systems
- Securitisation special purpose vehicles
- Insurance contracts and joint ventures
- AIFM which manage AIFs whose only investors are the AIFM

Application: Smaller AIFMs

- AIFMs with assets under management:
 - ↳ including any acquired using leverage, not above EUR 100 million; or
 - ↳ not above EUR 500 million when portfolio of AIF consists of AIF that are not leveraged and which have no redemption rights exercisable during a period of 5 years following the date of initial investment in each AIF
- Smaller AIFMs subject only to certain provisions regarding registration and information to home state competent authorities.
- Smaller AIFMs do not benefit from rights, including passport, under Directive but can opt in, in which case full Directive becomes applicable.

Main proposals

- Require all AIFM to be **authorised** in order to manage one or more AIF (Chapter II)
- Make AIFM subject to **supervision** by home state competent authority (Chapter II)
- Impose **capital requirements** of at least EUR125,000, plus additional own funds or insurance to cover negligence liability risk, on AIFMs (Art. 9)
- Ensure AIFMs subject to **conduct of business standards**, with **systems in place to manage risks, liquidity and conflicts of interest** (Arts 12, 14, 15, 16,)
- Require AIFMs to have **remuneration** policies and practices (Art. 13)
- Set out procedures for independent **valuation** of AIF assets (Art. 19)
- Impose restrictions on the **delegation** of AIFM functions (Art. 20)
- Impose requirements regarding **depositories** (Art. 21)
- Enhanced **transparency** (of AIFMs and AIFs (Chapters IV and V)

Main proposals - continued

- Introduce special provisions relating to AIFMs managing **leveraged AIFs** and **AIFs which acquire control** of non-listed companies and issuers (Chapter V)
- Introduce EU **passport** under which AIFMs can manage and market AIFs to professional investors throughout the EU, subject to compliance with demanding regulatory standards (Chapters VI and VII)
- Imposes conditions on management and marketing of non-EU AIFs and on marketing in the EU by non-EU AIFMs (commonly known as the "**third country issue**") (Chapter VII)
- Afford **supervisors** wide powers of inspection and intervention, including wider role for the new European Securities and Markets Authority ("ESMA") (Chapter IX)

Implementation: timetable going forward

- The Committee of Permanent Representatives (COREPER) – comprising government officials from each of the EU Member States - will meet 3 November to approve text agreed at last Trialogue and invite European Parliament to pass it.
- On 11 November, the European Parliament will vote on the text during its plenary session. There seems to be a majority support within the Parliament and the vote is expected to pass comfortably.
- EU finance ministers will then formally approve text on behalf of Council once passed in Parliament plenary; that meeting is expected to be held on either 17 November or 7 December.
- Text will then be translated into the languages of the EU Member States, tidied and published in the Official Journal of the European Union, marking its assent as a legally binding act (probably Q1 or Q2 2011).
- Secondary rule making, known as Level II, overseen by ESMA during 2011 and 2012.
- Deadline for transposition of legislation in Member States two years from publication in the Official Journal (Q1 or Q2 2013).

Key issues: third country issues

- **Authorised EU-AIFM** can benefit from an EU passport to market EU AIFs in Member States other than those where EU-AIFM is established, subject to compliance with full Directive.
- Two years, in principle, after transposition date of Directive (so in 2015) **EU AIFM marketing non-EU AIF** and **non-EU AIFM managing and marketing AIFs in the EU** should be allowed to do so **with a passport** subject to requirements of Directive (see table). This regime shall co-exist for three years with national placement regimes.
- During transitional period lasting, in principle, to 2018, national regimes for **EU AIFM intending to market non-EU AIF without a passport** and **Non-EU AIFMs intending to manage EU AIFs or market AIFs without a passport** may continue to be permitted by the relevant Member States subject to requirements of Directive (see table).
- National private placement regimes optional for Member States: some may choose not to implement them.
- Individual Member States able to add additional conditions as part of their own private placement regimes to those in Directive.
- Anticipated that UK FSA will maintain a sensible and workable regime.

Entities	Authorisation	Management	Marketing with EU passport	Marketing without EU passport/private placement
EU AIFM/EU AIF	EU AIFM must be authorised in and comply with full Directive.	Comply with full Directive	Comply with full Directive	N/A
EU AIFM/Non-EU AIF		Article 34: Comply with full Directive except Articles 21 (Depositary) and 22 (Annual Report). Condition 1.	Article 35: Comply with full Directive. Conditions 1, 2 and 3.	Article 36: Comply with full Directive except Article 21 (Depositary) but one or more entities must be appointed to carry out certain depositary duties. Conditions 1 and 2.
Non-EU AIFM/EU AIF	Article 37: Non-EU AIFM intending to use passport under Articles 38 or 39 must be authorised and comply with full Directive (unless impossible to do so and instead comply with equivalent local rules). Conditions 1, 2, 3 and 4.	Article 39 bis: Authorised non-EU AIFM may also manage AIF established in other Member States directly or through branch.	Article 38: Under authorisation conditions, must comply with full Directive. Conditions 1, 2, 3 and 4.	Article 40: Comply only with Articles 22 (Annual Report), 23 (Disclosure to investors) and 24 (Reporting to competent authorities) and, where relevant, the Portfolio Company requirements under section 2 of Chapter V (notification of acquisition of control, content of the annual report of the AIF, exercising control and asset stripping). Conditions 1 and 2.
Non-EU AIFM/Non-EU AIF			Article 39: Comply with full Directive. Conditions 1, 2, 3 and 4.	

This table is intended as an outline only of the proposals in the 27 October 2010 draft text. Please refer to the full text of the draft AIFMD for details of the full provisions or contact Lucy Frew at Gide Loyrette Nouel LLP.



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Key issues: third country conditions

- (1) Co-operation arrangements in order to allow exchange of information between the relevant EU competent authorities and third country supervisory authorities;
- (2) The third country where the non-EU AIF and/or non-EU AIFM is established is not listed as a non-cooperative country and territory by the Financial Action Task Force on anti-money laundering and terrorist financing;
- (3) The third country where the non-EU AIF is established has signed tax information sharing agreement with each of the competent authorities of the AIFM and the competent authorities where the AIF is marketed which fully complies with the standards laid down in Article 26 of the OECD Model Tax Convention and ensures an effective exchange of information in tax matters.
- (4) Non-EU AIFM seeking authorisation to manage EU AIF / market EU and non-EU AIF under a passport must have a legal representative established in its Member State of reference to be:
 - ➔ the contact person of the non-EU AIFM for the investors of the relevant AIF, for ESMA and for the competent authorities; and
 - ➔ jointly responsible with the AIFM for the compliance function with this Directive in relation to the management and marketing activities performed by the AIFM.

Other key issues

- Role of ESMA
- Member State of reference for non-EU AIFMs
- Delegated acts
- Marketing
- Transparency
- Acquisition of non-listed companies and issuers
- Asset stripping



Other key issues - continued

- Delegation
- Depositories
- Prime brokers
- Valuation
- Leverage
- Securitisation positions
- Remuneration



Impact of the AIFMD

- Is the text now workable?
- Can the investment fund industry still have a say in implementation?
- Challenges for regulators.
- National private placement preserved until 2018 – so is it business as usual?
- Non-EU AIFMs able to passport – so are the third country issues resolved?
- Will AIFMs relocate or change business model?
- Will non-EU funds be brought “on-shore” as “Newcits”?
- Depositary issues.

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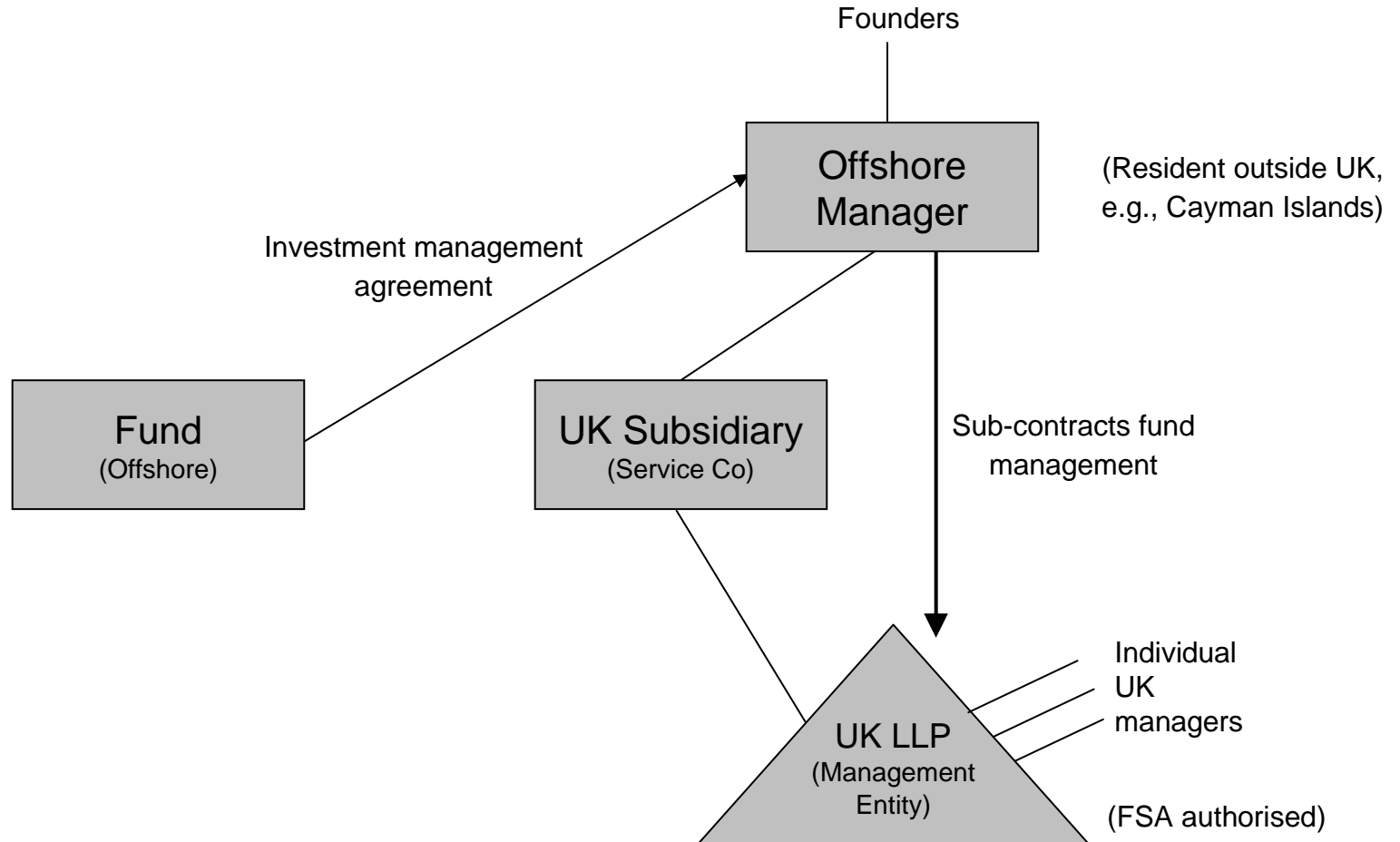
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Typical UK management structure



Non-UK domiciliaries – the remittance basis

- Outline of benefits of remittance regime
 - ↳ UK income tax / capital gains tax apply only to income / assets remitted onshore
 - ↳ Offshore income and gains can be sheltered
 - ↳ Appealing for individuals with material offshore assets and income
- What is a remittance?
- Entitlement to remittance basis
 - ↳ Non-UK domicile
 - ↳ Automatic application for first 7 out of 9 years of residence
 - ↳ £30,000 annual charge thereafter

Aspects of remittance regime

- Income tax
 - ↳ Maximise offshore profits; keep UK profits to level required for expenditure
 - ↳ Employment structuring – dual contracts – strict conditions
 - ↳ Deferral structures
- Capital gains
 - ↳ Offshore trust arrangements
- IHT
 - ↳ Deemed domicile
- Changes made in 2008
- What does the future hold for the UK tax regime for non-doms?

The UK as a hedge fund domicile

- Traditionally UK not seen as viable option
- Increased incentives for using an onshore vehicle
- Much improved tax regime for funds domiciled in UK
 - ↳ “TEF” regime
 - ↳ “White list”
- But:
 - ↳ Complexity
 - ↳ Uncertainty

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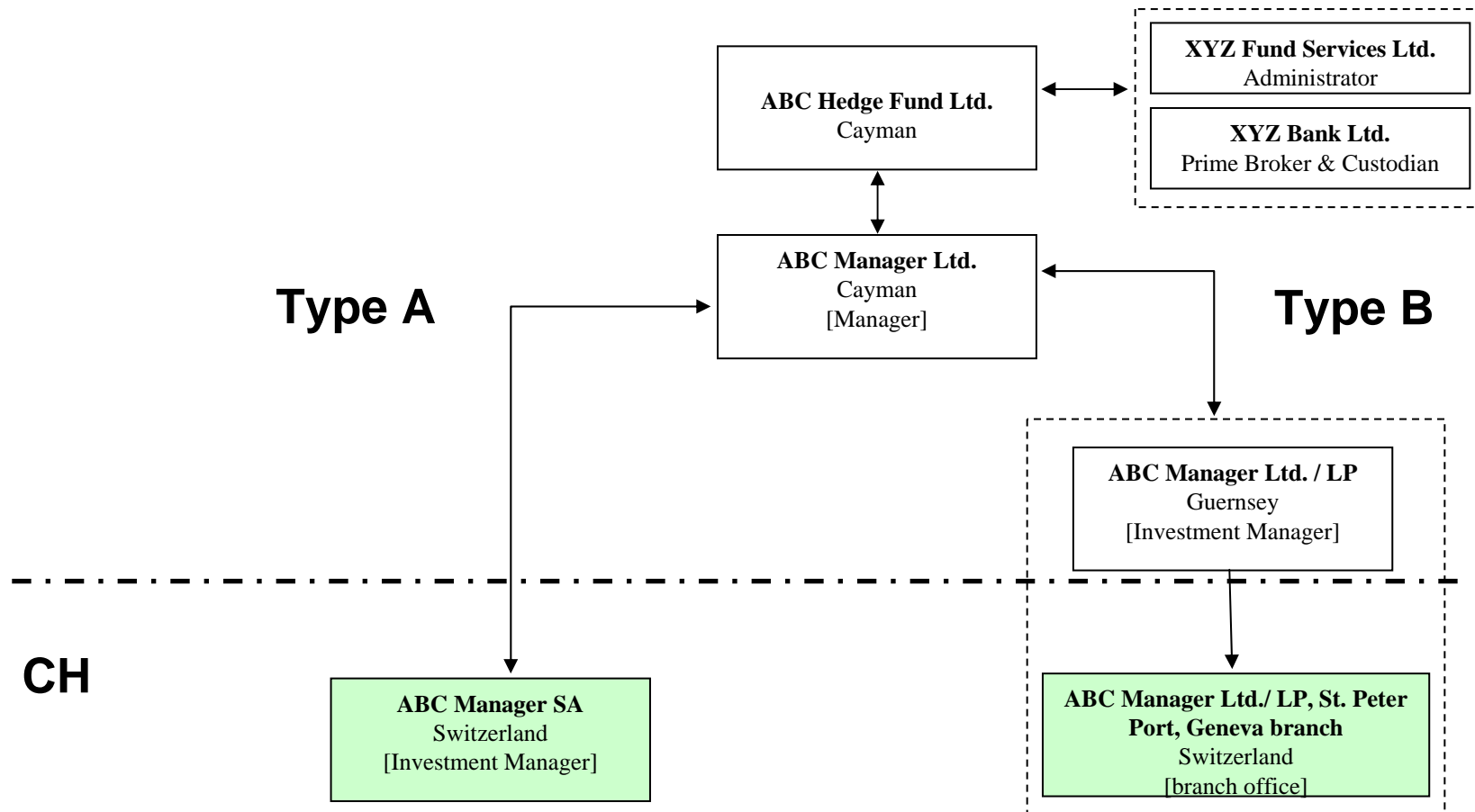


AIFM Directive – the Swiss angle

London, 5 November 2010

Fedor Poskriakov
Frédéric Neukomm

Swiss AIFM setup – typical structures



Swiss regulatory regime – current requirements

- Swiss manager (AIFM)
 - Unregulated activity
 - » (except for asset managers of Swiss collective investments, or non-Swiss UCITS – optional)
 - Financial intermediary (if decision making authority)
 - » under the Swiss Anti Money Laundering Act – Art. 2 (3): SRO registration or approval by the FINMA
 - “Opt-in” licensing with FINMA
 - » Limited to managers of UCITS
 - » Only available to Swiss companies (N/A for Swiss branches)
 - Portfolio management only
 - » important to avoid central administration of the AIF in Switzerland

Swiss regulatory regime – current requirements

- Alternative investment fund - AIF (non-Swiss)
 - Prohibition of any public offering in or from Switzerland, unless AIF registered for public offering with FINMA
 - » Approval for public distribution in Switzerland not available in Switzerland for typical AIF because of their features
 - Private placement only
 - » Regulated entities / corporates with professional treasury management
 - » High net worth individuals
 - » Independent asset managers (for their managed clients)

Regulatory regime – post-AIFMD

- “Passport” required in order to manage EU AIFs / market AIFs managed by AIFM
 - **How will Swiss AIFMs be able to comply?**
 - Conditions for EU “passport”:
 - Full compliance with AIFMD (exceptions & limitations?)
 - Representative in Member State of reference
 - Cooperation arrangements between regulators
 - AIF & AIFM jurisdictions not being on the FATF’s NCCT list
 - Tax information sharing agreement in place
 - Effective exercise of supervisory powers not limited by local laws applicable to AIFM (impact in practice?)
- **Swiss law will need to be adapted**

Regulatory regime – post-AIFMD

- Review of Swiss regulatory regime by FINMA is under way
 - Internal consultation process – no visibility / feedback so far
 - Expected outcome:
 - Some form of “opt in” regime to be AIFMD eligible
 - FINMA may go beyond and seek to impose compulsory licensing for all AIFMs (possibly with a *de minimis* threshold)
- Uncertainties / open issues:
 - Scope of requisite compliance with AIFMD (full requirements / organisational & transparency requirements)?
 - Implementation of supervision by Swiss regulator?
 - Recognition by ESMA / Member States...
 - Cost of compliance

Regulatory regime – post-AIFMD

- Alternatives to EU “passport” ?
 - **Marketing**
 - Private placement to professional investors only
 - Temporary solution (until ~ 2018, but may be extended beyond)
 - Conditions:
 - » Transparency requirements
 - » Co-operation arrangements with AIFM regulator & AIF regulator
 - » AIF & AIFM jurisdictions not being on the FATF’s NCCT list
 - Reverse solicitation
 - Market to non-EU investors...
 - **Management**
 - Delegation from an authorised EU AIFM:
 - Swiss manager subject to supervision
 - Co-operation arrangements between regulators in place

Swiss taxation

- Swiss resident AIFM principals
 - As a rule, taxation of Swiss resident individuals on worldwide wealth and income
 - Exceptions: income from real estate abroad, income from foreign partnership operating a business abroad
 - Ordinary regime at par with other similar jurisdictions
 - No taxation on capital gains realized on the disposal of items of private (as opposed to business) wealth
 - Tax planning to be made prior to taking up Swiss residence
 - Applicable rates depend largely on the canton

Tax status in Switzerland: applicable rates

	Corporate income tax	Individual income tax	Indi. income tax (dividends)	Wealth tax
Geneva	24.2%	44.9%	27%	1%
Zurich	21.2%	40%	21%	0.7%
Zug	15.8%	24%	13%	0.3%
Schwytz	14.6%	19%	9%	0.1%

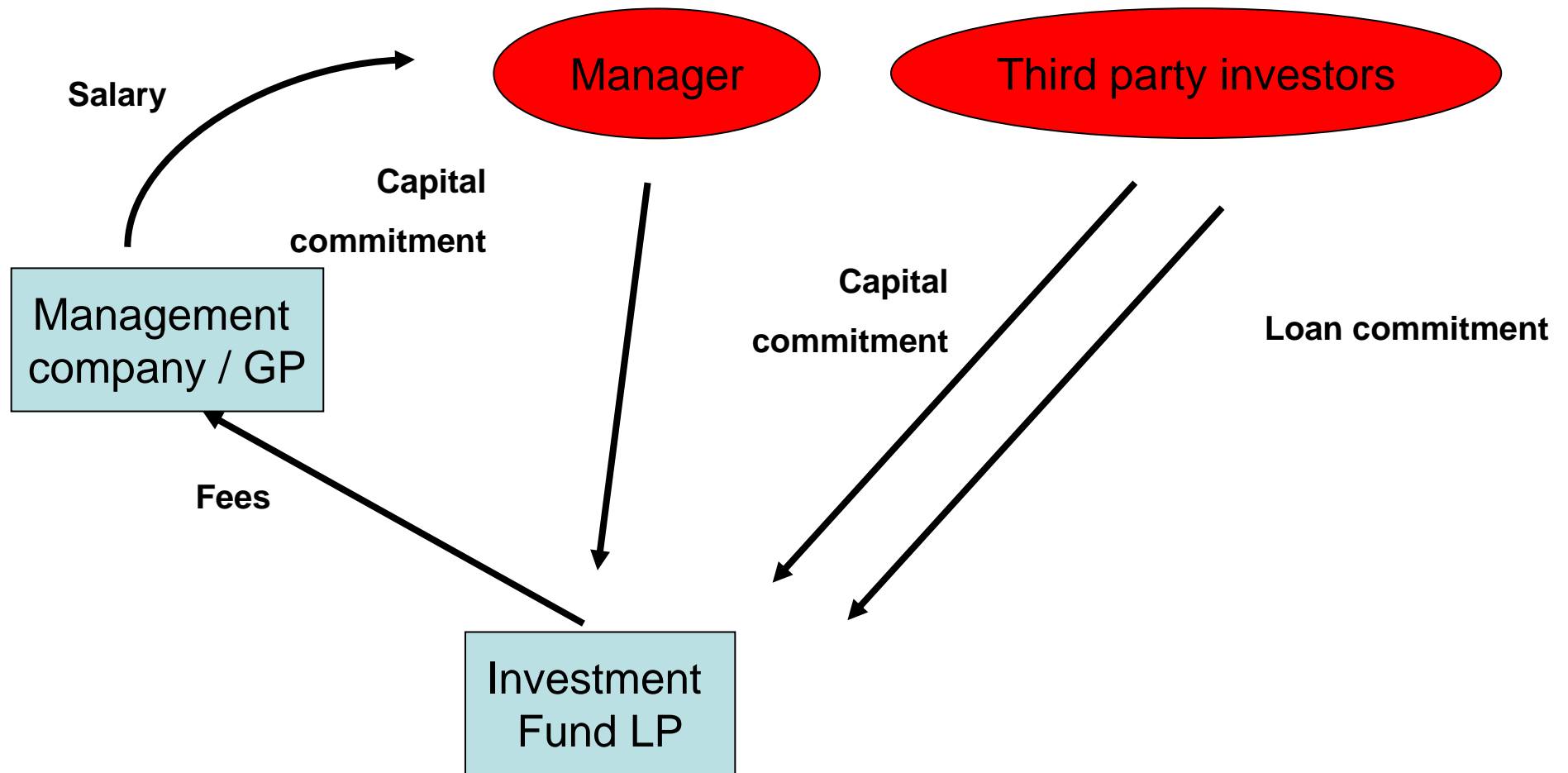
Tax status in Switzerland

- No « flat rate ruling » available
- Managers can typically not qualify for the « forfait » regime because it requires that the person does not engage in a gainful activity in Switzerland
- Investment management companies can typically not qualify for the auxiliary company regime, respectively for a tax holiday or the like
- There is a political desire to attract HF – PE managers in Switzerland
- The tax authorities have developed a circular indicating certain structuring possibilities for both HF and PE structures
- This circular is still in draft form and is not expected to ever be finalized. It is however applied in practice by tax authorities.

Tax status in Switzerland: Private equity

- The draft circular refers to the HMRC/EVCA memorandum of understanding
- Managers holding an investment in the fund may be treated as private investors. This holds true even if other investors have to make a loan commitment in addition to the capital commitment. Managers will thus realize tax exempt capital gains. This is subject to the requirements
 - That the management company receives an arm's length share of fees
 - That the managers receives an arm's length salary

Tax status in Switzerland: Private equity



Tax status in Switzerland: Private equity

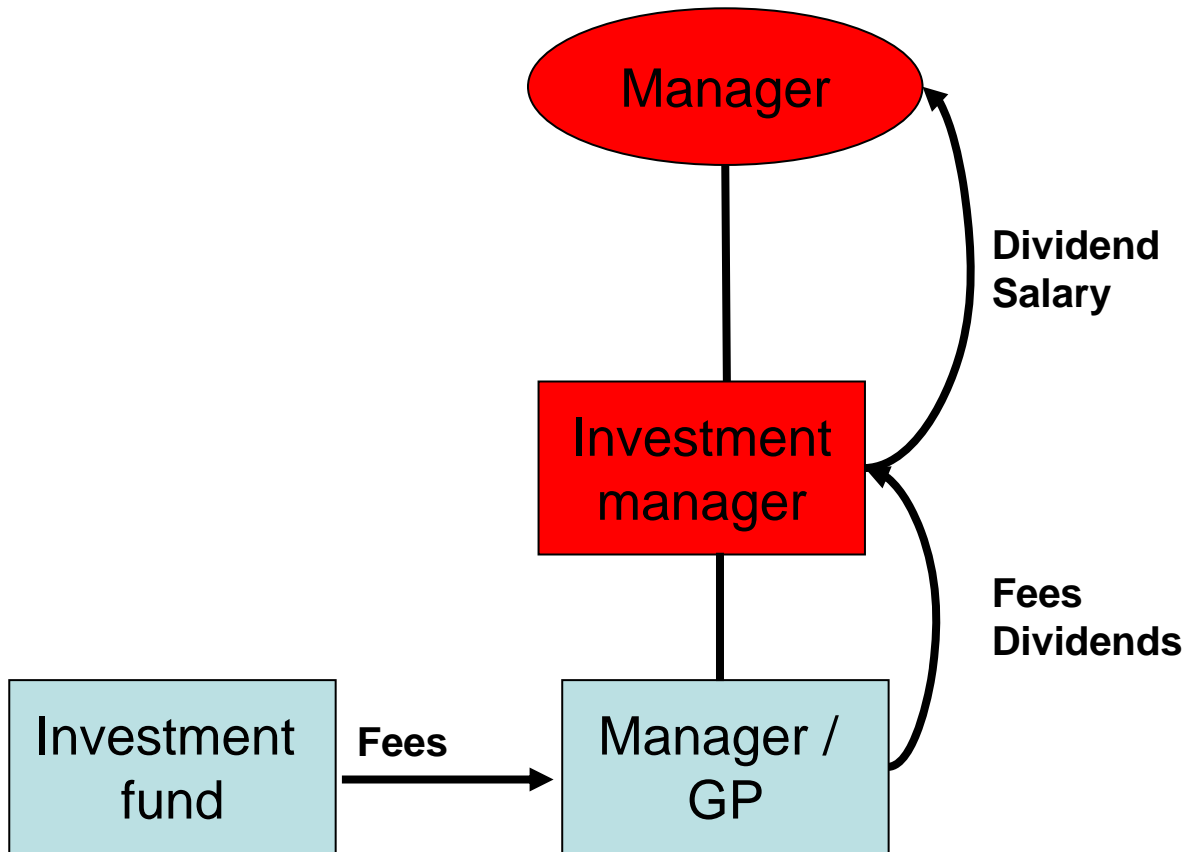
	Manager Capital	Investor Capital	Investor Loan	Total
Nominal value	1'000	4'000	95'000	100'000
Total investment	1%	4%	95%	100%
Liquidation				295'000
Reimbursement			(95'000)	
Split of the gain	(40'000) 20%	(160'000) 80%		

Tax status in Switzerland: Hedge funds

- It is typically not possible to have a loan/capital commitment structure in a hedge fund context
- The main ways to achieve an attractive tax result are the international tax allocation of fees, the good selection of the canton of residence of the company/manager, etc
- Transfer pricing analysis for the determination of income attributable to the Swiss advisor/investment manager (tax ruling)
 - depending on effective substance outside of Switzerland

Tax status in Switzerland: Hedge funds

	Total	Country 1 Offshore	Country 2	Country 3 Suisse
Total of fees	210			
Split				
Back Office	10	-	10	-
Investment management 50%	100	-	-	100
Asset allocation / Risk management 17%	34	34	-	-
Marketing 33%	66	66	-	-
Total	210	100	10	100



Tax treatment

	Net income	Corporate income tax	Remaining profit	Dividend	Dividend tax
Investment Manager (Zug)	100	16	84		
Manager (Wollerau)				84	7.4
Total tax	23.4				
Net income after tax	76.6				

Tax treatment

	Net income	Corporate income tax	After corporate income tax	Dividend	Dividend tax
Investment manager (GE)	100	24	76		
Manager (GE)				76	21
Total tax	45				
Net income after tax	55				

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