Advice

ESMA's advice to the European Parliament, the Council and the Commission on the application of the AIFMD passport to non-EU AIFMs and AIFs

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Data protection

Information on data protection can be found at www.esma.europa.eu under the heading 'Legal Notice'.

Who should read this paper

This document will be of interest to EU and non-EU investors and fund managers, and their related parties.

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Acronyms used

AIFMD	Alternative Investment Fund Managers Directive (2011/61/EU)
AIFM	Alternative Investment Fund Manager
AIF	Alternative Investment Fund
ESMA	European Securities and Markets Authority
EU	European Union
IOSCO	International Organization of Securities Commissions
MoU	Memorandum of Understanding
NCA	National Competent Authority
NPPR	National Private Placement Regime
UCITS	Undertaking for Collective Investment in Transferable Securities
UCITS Directive	Directive 2009/65/EC

I. Executive summary

Reasons for publication

In accordance with Articles 36 and 42 of the Directive 2011/61/EU on Alternative Investment Fund Managers (AIFMD), non-EU alternative investment fund managers (AIFMs) and non-EU alternative investment funds (AIFs) managed by EU AIFMs are subject to the national private placement regime (NPPR) of each of the Member States where the AIFs are marketed or managed.

However, the AIFMD makes provision for the passport, which is currently reserved to EU AIFMs and AIFs, to be potentially extended in future. Article 67(1) of the AIFMD establishes that, by 22 July 2015, ESMA shall issue to the European Parliament, the Council and the Commission advice on the application of the passport to non-EU AIFMs and AIFs in accordance with the rules set out in Article 35 and 37 to 41 of the AIFMD.

This document sets out ESMA's advice on the application of the passport to six non-EU countries: Guernsey, Hong Kong, Jersey, Switzerland, Singapore and the United States.

Contents

Section 1 of the advice sets out the background to ESMA's work, while the detailed assessment of each of the aforementioned non-EU countries is contained in section 2. Annexes 1 to 7 contain a summary of the feedback to the call for evidence that ESMA launched in November 2014. Annex 8 gives a detailed breakdown by non-EU country of the number of non-EU AIFs and non-EU AIFMs active in Member States in accordance with Articles 36 and 42 of the AIFMD.

Next Steps

ESMA will continue to work on its assessment of other non-EU countries not covered in this advice with a view to delivering further submissions to the European Parliament, the Council and the Commission in the coming months. For those non-EU jurisdictions with which there are currently no supervisory cooperation arrangements in place for the purposes of the AIFMD, ESMA will continue its efforts to agree a MoU with the authorities concerned.

1 Background

1.1 AIFMD and the request to ESMA for advice

1. In accordance with Articles 36 and 42 of the AIFMD, non-EU AIFMs and non-EU AIFs managed by EU AIFMs are subject to the NPPR of each of the Member States where the AIFs are marketed or managed. However, the AIFMD makes provision for the passport, which is currently reserved to EU AIFMs and AIFs, to be potentially extended in future. Article 67(1) of the AIFMD establishes that, by 22 July 2015, ESMA shall issue to the European Parliament, the Council and the Commission the following:

   - An opinion on the functioning of the passport for EU AIFMs pursuant to Articles 32 and 33 of the AIFMD and on the functioning of the national private placement regimes set out in Articles 36 and 42 of the AIFMD.

   - Advice on the application of the passport to non-EU AIFMs and AIFs in accordance with the rules set out in Article 35 and Articles 37 to 41 of the AIFMD.

2. Within three months of receipt of positive advice and an opinion from ESMA, and taking into account the criteria of Article 67(2) and the objectives of the AIFMD, the Commission should adopt a delegated act specifying the date when the rules set out in Article 35 and 37 to 41 of the AIFMD become applicable in all Member States. As a consequence, the EU passport would be extended to non-EU AIFs and non-EU AIFMs.

3. In order to produce this opinion and advice, ESMA must look into the elements listed in Article 67(2) and (4) of the AIFMD[1], notably on the basis of the information provided by the national competent authorities (NCAs) about the EU and non-EU AIFMs under their supervision. Indeed, Article 67(3) of the AIFMD requires NCAs to provide information to ESMA quarterly as from 22 July 2013.

4. ESMA has received input from NCAs for the periods covering 22 July 2013 to 31 March 2014, 1 April to 30 June 2014, 1 July to 30 September 2014, 1 October to 31 December 2014, and 1 January to 31 March 2015.

5. Article 67(4) of the AIFMD states that, where ESMA considers that there are no significant obstacles regarding investor protection, market disruption, competition and the monitoring of systemic risk, impeding the application of the passport to the marketing of non-EU AIFs by EU AIFMs in the Member States and the management and/or marketing of AIFs by non-EU AIFMs in the Member States in accordance with the rules set out in Article 35 and Articles 37 to 41, it shall issue positive advice in this regard.

[1] This includes such aspects as the use made of the EU passport and any problems encountered in that context, the functioning of the NPPRs and, more generally, issues such as investor protection, market disruption, competition and the monitoring of systemic risk.

6. In order to supplement the input provided by NCAs via the quarterly surveys, ESMA launched a call for evidence[2] in November 2014 aimed at gathering information from EU and non-EU stakeholders on the functioning of the EU passport, the NPPRs and the potential extension of the EU passport to non-EU countries.

7. ESMA received 67 responses (including 15 confidential submissions), from 13 non-EU authorities, 21 EU and non-EU trade associations of asset managers, 17 EU and non-EU asset managers, and 16 other trade associations and private firms (e.g. providers of services for funds, law firms etc).

8. An important point mentioned in the call for evidence is that ESMA has decided to opt for a country-by-country assessment of the potential extension of the AIFMD passport. This allows for greater flexibility in the assessment and for a distinction to be made between the very different situations of non-EU countries in terms of the demand for the passport, the access to the market of these non-EU countries for EU funds and managers, and their regulatory framework as compared to the AIFMD.

9. Such an approach makes it necessary to assess the different non-EU countries on an individual basis, which requires an extensive information-gathering exercise.

1.2 Structure of the Advice

10. The advice is structured as follows:

   a. First, the criteria, methodology and data used to assess the potential extension of the AIFMD passport to non-EU countries is presented (section 2.1);

   b. The list of the non-EU countries to be assessed by ESMA for the purposes of the present advice under Article 67 of the AIFMD is then established (section 2.2);

   c. The different non-EU countries listed in section 2.2 are assessed against the methodology set out in section 2.1 (sections 2.3 to 2.8);

   d. Information on other non-EU countries is given (section 2.9); and

   e. A series of annexes detail the feedback received by ESMA via the responses to the call for evidence, and give a detailed breakdown by non-EU country of the number of non-EU AIFs and non-EU AIFMs active in Member States in accordance with Articles 36 and 42 of the AIFMD.

[2] http://www.esma.europa.eu/system/files/2014-esma-1340_call_for_evidence_aifmd_passport__3rd_country_aifms.pdf

2 Assessment of the different non-EU countries in light of the criteria set out in Article 67 of the AIFMD

2.1 Criteria, Methodology and Data to assess the potential extension of the AIFMD passport to non-EU countries

11. ESMA is of the view that the following criteria should be used to assess the situation of other non-EU countries in relation to the potential extension of the AIFMD passport to those non-EU countries. These criteria were identified both in the course of the surveys mentioned in the ESMA opinion on the EU passport and NPPRs, and in the responses of stakeholders to the call for evidence launched by ESMA on the AIFMD passport. These criteria are used in the following sections to assess the cases of the following six non-EU countries: Guernsey, Hong Kong, Jersey, Switzerland, Singapore and the United States. The same assessment methodology has been applied to all six countries based on the set of information gathered by ESMA (as detailed in paragraph 22).

12. The advice set out in the boxes in each section of this document represents ESMA's view of each non-EU country based on the information available at the time of publication. In some cases, the advice cannot be considered 'positive' in the sense of Article 67(4) of the Directive. The European Council, Parliament and the Commission to which this advice is submitted pursuant to Article 67 of the AIFMD may wish to consider whether to wait until ESMA has delivered positive advice on a sufficient number of non-EU countries before triggering the legislative procedures foreseen by Articles 67(5) and (6), taking into account such factors as the potential impact on the market that a decision to extend the passport might have.

<u>Level 1 text</u>

13. Article 35 sets down conditions for the marketing in the Union with a passport of a non-EU AIF managed by an EU AIFM. Articles 35(2) says that the following conditions shall be met:

    a) *appropriate cooperation arrangements must be in place between the competent authorities of the home Member State of the AIFM and the supervisory authorities of the third country where the non-EU AIF is established in order to ensure at least an efficient exchange of information, taking into account Article 50(4), that allows the competent authorities to carry out their duties in accordance with this Directive;*
    b) *the third country where the non-EU AIF is established is not listed as a Non-Cooperative Country and Territory by FATF;*
    c) *the third country where the non-EU AIF is established has signed an agreement with the home Member State of the authorised AIFM and with each other Member State in which the units or shares of the non-EU AIF are intended to be marketed, which fully complies with the standards laid down in Article 26 of the OECD Model Tax*

Convention on Income and on Capital and ensures an effective exchange of information in tax matters, including any multilateral tax agreements.

14. Equivalent requirements are set out in Article 37(7)(d-f) to cover the situation where the passport is granted to a non-EU AIFM.

15. Article 67(4) says (emphasis added):

Where ESMA considers that there are no significant obstacles regarding <u>investor protection</u>, <u>market disruption</u>, <u>competition</u> and the <u>monitoring of systemic risk</u>, impeding the application of the passport to the marketing of non-EU AIFs by EU AIFMs in the Member States and the management and/or marketing of AIFs by non-EU AIFMs in the Member States in accordance with the rules set out in Article 35 and Articles 37 to 41, it shall issue positive advice in this regard.

Criteria

16. ESMA notes the preconditions for an MoU with non-EU NCAs set out in Articles 35 and 37 and considers that there should be no doubt in relation to the <u>ongoing</u> satisfaction of these. As Article 35 is not yet in operation it is necessary to review the way in which the MoUs required under Articles 34(1)(b) and 36(1)(b) have been applied. In particular, in relation to the MoUs under Articles 34 and 36, there should be two tests:

    1. How has the existing MoU worked? Are there positive or negative experiences to report? For example:

        a) Is there efficient collaboration in accordance with the provisions of the MoU on supervisory cooperation?
        b) Is there timely and prompt collaboration in case of emergency situations?
        c) Is non-requested information shared with the EU authorities at the initiative of the non-EU authority?
        d) Have legal limitations been encountered in sharing information or performing on-site visits?
        e) Has there been a significant level of lack of cooperation from the non-EU AIFMs?
        f) Does the non-EU NCA recognise the role played by each EU NCA (as part of the network of EU securities supervisors) and is the non-EU NCA open to bilateral relationships with each EU NCA?

    2. In the absence of evidence in relation to the working of an existing MoU, does previous supervisory engagement provide support for the expectation of good supervisory cooperation, or not?

17. Second, in relation to Art 67(4), the following criteria should be used to assess the situation of other non-EU countries in relation to the potential extension of the AIFMD passport to those non-EU countries.

1) Investor protection:

Examples of information that may be relevant under this heading include:

i) Is there evidence that some investor complaints are not being adequately tackled by the non-EU NCA?

ii) What rules or mitigants does the non-EU country have in relation to (a) the safeguarding of assets, (b) the function of the depositary and management of conflicts of interest between the AIFM and the depository, (c) the prudential soundness of the AIFM, (d) the timeliness and accuracy of disclosures to investors, (e) the alignment of incentives between the AIFM and investors? Insofar as these rules or mitigants exist in the non-EU countries, to what extent do these rules or mitigants measure up to those in AIFMD?

iii) How does the regulatory regime in the third country measure up against the relevant IOSCO principles, in particular its level of regulatory and supervisory engagement as assessed against principles 10 to 12[3] (including whether the regime is assessed as being at least 'broadly implemented' under each of these principles)?

iv) What is the scope of the non-EU authority's regulatory oversight with respect to the range of intermediaries and vehicles operating in the relevant country?

18. Regarding investor protection and the information mentioned in 1) ii) above, ESMA notes that under the requirements of Article 37 non-EU AIFMs intending to market and/or manage AIFs in the EU using the AIFMD passport shall acquire prior authorisation by the NCA of their Member State of reference. This authorisation notably implies that this NCA will have to verify that the non-EU AIFM will comply with the requirements of the AIFMD. In that respect, criterion 1) ii) should not be seen as an equivalence assessment since, regardless of the existing regulatory framework in the non-EU country, the non-EU AIFM from that non-EU country wishing to market and/or manage its AIFs in the EU will have to comply with the AIFMD requirements, and these requirements will be verified by the NCA of the Member State of reference.[4]

[3] And the following IOSCO principles: 4, 13, 14, 15, 24, 25, 26, 27, 28 and 32.

[4] ESMA notes that the different steps described in Art 37 leading to the designation of the Member State of reference might lead to the need for supervisory convergence measures by ESMA in order to ensure consistency in the application of these requirements in the different Member States.

19. However, ESMA also notes that the abovementioned verification exercise may significantly differ depending on the extent to which the non-EU country has put in place a regulatory framework that is similar to the AIFMD (as regards notably some of the points mentioned in 1)ii) above). In the event of major gaps between the regulatory framework of the non-EU country and the AIFMD, the role of the NCA of the Member State of reference may be particularly challenging, and the extent to which the cooperation agreement with the non-EU Authority is efficient will matter significantly more than in the event of a non-EU regulatory framework that would be very similar to the AIFMD. The extent to which the interpretation of the role of the NCA of the Member State of reference differs across the Member States will also be a particularly relevant issue.

20. For these reasons, ESMA is of the view that, while it would not be appropriate to require (for the purposes of giving positive advice on the extension of the passport) that there be a minimum degree of equivalence between the regulatory framework of the non-EU country and the AIFMD, it is nevertheless relevant and necessary to investigate the extent to which the regulatory framework of the non-EU country differs from the AIFMD. However, this assessment will focus only on the most relevant elements of the regulatory framework of each non-EU country. This explains why the format of the assessments of these criteria in the following sections may differ slightly from one non-EU country to another.

21. ESMA notes that Article 21(6) of the AIFMD empowers the Commission to adopt implementing acts stating that the prudential regulation and supervision of third countries with respect to depositaries have the same effect as Union law and are effectively enforced. While there may be some elements of the assessment carried out for the purposes of this advice that are relevant to the assessment that will be done under Article 21(6), ESMA would like to underline that the present advice is a separate exercise and is without prejudice to the more detailed assessment that is likely to be appropriate in the context of the implementing acts.

2) <u>Market disruption</u>:

Examples of questions that may be applied under this heading include:

(a) To what extent would the granting of the passport to the non-EU AIFMs and AIFs unduly undermine the activity of existing EU AIFMs due to differences in the regulatory environment in the non-EU country and allow them to change their operating arrangements so as to circumvent the AIFMD?
(b) Is there evidence that the granting of the passport to non-EU AIFMs would reduce or improve investor choice (in the short-run or the long-run)?

3) Obstacles to competition:

Examples of questions that may be applied under this heading include:

(a) Is the process operated by the non-EU NCA to (a) authorise EU AIFMs or (b) allow marketing of EU AIFs in the non-EU country reasonable (in terms of clarity, predictability, cost and regulatory expectation)? Is there a level playing field between EU and non-EU AIFMs as regards market access, particularly in view of the procedures that would apply to non-EU AIFMs under Article 37 in the event that the passport is extended?

(b) Are EU AIFMs and EU AIFs treated in the same way as managers and collective investment undertakings of the non-EU country in terms of regulatory engagement (including regulatory fees and documentation to be provided prior to the authorisation)?

(c) Does the non-EU NCA treat all EU jurisdictions equally?

4) Monitoring of systemic risk:

Examples of questions that may be applied under this heading include:

a) Does there exist tangible evidence of adequate surveillance of market developments with a view to tracking potential (or actual) systemic risks[5] by the NCA in the non-EU country?

b) How does the regulatory regime in the non-EU country measure up against the IOSCO principle 6?

Sources of data to support methodological assessment

22. ESMA will carefully evaluate the following sources of information:

1) ESMA's research

2) The insights and understandings of EU NCAs

3) Experiences of EU NCAs in liaising with non-EU NCAs in formal and informal supervisory settings

4) Responses of non-EU countries to queries from ESMA

[5] Where the definition of 'systemic risk' is not simply confined to the local jurisdiction but also has regard for spillover effects of the AIFMs or AIFs operating outside of the borders of the local jurisdiction.

5) IMF assessments (Financial Stability Assessment Plans and Details Assessment Reviews against principles of international standard-setters)

6) Stakeholder responses to the Call for Evidence;

7) Non-EU authority responses to the Call for Evidence

8) Other relevant market intelligence

Quality of assessment

23. ESMA will require a reasonable body of evidence before considering the provision of a positive assessment against the criteria[6]. Particular emphasis will be put on the quality of supervisory liaison/engagement between EU NCAs and the non-EU NCA.

24. For the avoidance of doubt, and due to the amount of information needed to assess comprehensively each non-EU country against the different criteria set out in Article 67 and detailed above, ESMA will reserve judgement where there is insufficient evidence to provide a positive assessment.

Other potentially relevant issues not assessed by ESMA

25. ESMA is providing this advice based on a methodology which is grounded in the Level 1 text of AIFMD. ESMA is conscious that the assessment methodology focusses on regulatory issues. Other issues which the Commission and co-legislators may also wish to consider may include: (a) fiscal matters in the non-EU country and (b) latest intelligence on the Anti-Money Laundering and Counter-Terrorism Financing (AML/CTF) regime in the non-EU country (to the extent that this aspect is not covered under Articles 35(2)(b) and 37(7)(e)).

26. On a separate topic, ESMA notes that Article 42 of the AIFMD allows Member States to permit non-EU AIFMs to manage EU AIFs or market AIFs in their jurisdictions (NPPR). Article 37 (if and when it becomes applicable) indicates that Member States shall require non-EU AIFMs intending to manage EU AIFs or market AIFs in the Union with a passport to be authorised.

27. ESMA understands that, once Article 37 is switched on, non-EU AIFMs will be able to continue to operate under Article 42 notwithstanding that they could be authorised under Article 37, at least during the transitional period mentioned in Art 68. Nevertheless, ESMA sees merit in clarifying this issue.

28. ESMA also notes that Article 37 refers to “authorisation” of non-EU AIFMs but makes no mention of registration. Accordingly, if and when Article 37 is switched on it will be

[6] Although it should be understood that, in order for ESMA to arrive at a definitive view (positive or negative) it is not necessary that information be available from all sources and on all elements of the methodology.

important to ensure that Member States have a common understanding on the treatment of non-EU AIFMs which are below the thresholds set out in Article 3(2) of the AIFMD.

2.2 List of the non-EU countries to be assessed by ESMA for the purposes of the advice of Article 67 of the AIFMD

29. In view of the present advice on the possible extension of the AIFMD passport to non-EU AIFMs and AIFs, NCAs have reported to ESMA quarterly on the functioning of the EU passport, the NPPRs and the coexistence of both regimes, for the period between July 2013 and March 2015[7].

30. In that context, ESMA has sought feedback from the NCAs of those Member States that have reported a significant presence of non-EU AIFMs and AIFs in their jurisdictions. The authorities from these Member States have provided a detailed breakdown by third country of the number of non-EU AIFs and non-EU AIFMs active in their territories in accordance with Articles 36 and 42 of the AIFMD.

31. The results of this survey (full details of which are set out in Annex 8 of the advice) allowed ESMA to draw up a list of non-EU countries that should be assessed against the criteria of Article 67 of the AIFMD.

32. On the basis of an aggregation of the figures provided by the relevant NCAs, the following non-EU countries have been identified as the domicile of non-EU AIFMs that market AIFs in the Member States examined and/or domiciles of non-EU AIFs marketed in the Member States examined:

- Australia
- Bahamas
- Bermuda
- Brazil
- British Virgin islands
- Canada
- Cayman Islands
- Curacao
- Guernsey
- Hong Kong

[7] Please also see ESMA's opinion and responses to the call for evidence on the functioning of the AIFMD EU passport and of the National Private Placement Regimes: 2015/1235

- Isle of Man
- Japan
- Jersey
- Mexico
- Mauritius
- Singapore
- South Africa
- South Korea
- Switzerland
- Thailand
- USA
- US Virgin Islands

33. Linked to the issue of the assessment methodology and the list of abovementioned non-EU countries is the question of how best to organise the assessment overall given the country-by-country approach mentioned above and the deadline of 22 July indicated in Article 67 of the AIFMD. In essence, the assessment methodology relies on (i) a sufficient level of information about each relevant non-EU jurisdiction and (ii) a substantive assessment of the information having regard for Art 67(4) of AIFMD. At this stage, it is clear that ESMA does not have sufficient information in relation to many of the non-EU jurisdictions in order to make a substantive assessment which would underpin advice pursuant to Art 67(1)(b). Therefore, ESMA only considers it appropriate to issue advice for non-EU jurisdictions once it is satisfied that there is a sufficient level of information about that jurisdiction. At present, ESMA is in a position to issue such advice in respect of the following non-EU jurisdictions:

i) United States

ii) Guernsey

iii) Jersey

iv) Hong Kong

v) Switzerland

vi) Singapore

34. This list takes into account a number of factors including the amount of activity already being carried out by entities from these countries under the NPPRs, the existing knowledge and experience of EU NCAs with respect to their counterparts in these jurisdictions and the efforts made by stakeholders from these countries to engage with the process.

35. This would then be followed by assessments of other batches of non-EU countries beyond July 2015.

2.3 U.S

36. The present section includes the assessment by ESMA on the potential granting of the AIFMD passport to the US based on the methodology described in section 2.1. The feedback received from the responses to the call for evidence launched by ESMA in November 2014 in relation to the case of the US is presented in Annex 2.

Criteria, Methodology and Data to assess the potential extension of the AIFMD passport to the U.S

37. ESMA notes the preconditions for an MoU with non-EU NCAs set out in Articles 35 and 37 and considers that there should be no doubt in relation to the ongoing satisfaction of these. As Article 35 is not yet in operation it is necessary to review the way in which the MoUs required under Articles 34(1)(b) and 36(1)(b) have been applied. In particular, in relation to the MoUs under Articles 34 and 36, there should be two tests:

1. How has the existing MoU worked? Are there positive or negative experiences to report? For example:

   a) Is there efficient collaboration in accordance with the provisions of the MoU on supervisory cooperation?
   b) Is there timely and prompt collaboration in case of emergency situations?
   c) Is non-requested information shared with the EU authorities at the initiative of the non-EU authority?
   d) Have legal limitations been encountered in sharing information or performing on-site visits?
   e) Has there been a significant level of lack of cooperation from the non-EU AIFMs?
   f) Does the non-EU NCA recognise the role played by each EU NCA (as part of the network of EU securities supervisors) and is the non-EU NCA open to bilateral relationships with each EU NCA?

2. In the absence of evidence in relation to the working of an existing MoU, does previous supervisory engagement provide support for the expectation of good supervisory cooperation, or not?

Assessment in the case of the US

38. ESMA is of the view that the MoUs are in place and working well. Positive experiences have been reported by NCAs.

39. Second, in relation to Art 67(4), the following criteria should be used to assess the situation of other non-EU countries in relation to the potential extension of the AIFMD passport to those non-EU countries.

1) Investor protection:

Examples of information that may be relevant under this heading include:

i. Is there evidence that some investor complaints are not being adequately tackled by the non-EU NCA?

ii. What rules or mitigants does the non-EU country have in relation to (a) the safeguarding of assets, (b) the function of the depositary and management of conflicts of interest between the AIFM and the depository, (c) the prudential soundness of the AIFM, (d) the timeliness and accuracy of disclosures to investors, (e) the alignment of incentives between the AIFM and investors? Insofar as these rules or mitigants exist in the non-EU countries, to what extent do these rules or mitigants measure up to those in AIFMD?

iii. How does the regulatory regime in the third country measure up against the relevant IOSCO principles, in particular its level of regulatory and supervisory engagement as assessed against principles 10 to 12[8] (including whether the regime is assessed as being at least 'broadly implemented' under each of these principles)?

iv. What is the scope of the non-EU authority's regulatory oversight with respect to the range of intermediaries and vehicles operating in the relevant country?

Assessment in the case of the US

51. ESMA is of the view that overall, the rules in the US seem comparable to the rules in the EU (diversification, disclosure requirements, limitation in ability to borrow money etc.). Funds must value securities in accordance with US generally accepted accounting principles (GAAP) but foreign funds can use IFRS. The U.S Regulatory framework in relation to funds and their manager is therefore robust and comprehensive, and its enforcement guaranteed by the supervisory powers of the SEC and other relevant U.S regulators.

52. However, ESMA also notes that it could have benefited from having more time to assess the detailed information it received on the US regulatory framework and, in particular, to analyse the extent to which the differences between the US regulatory framework and the AIFMD are material to the present assessment.

53. As regards investor complaints the SEC created the Office of Investor Education and Advocacy to serve individual investors. The OIEA receives many types of complaints, including complaints against brokers, brokerage firms, investment advisers, transfer agents, mutual funds, and other market participants. However, their efforts are

[8] And the following IOSCO principles: 4, 13, 14, 15, 24, 25, 26, 27, 28 and 32.

informal and they cannot force a firm to resolve the complaint. On top of this, OIEA can advise investors on other ways to complain. Both federal and state securities laws provide important legal rights and remedies (as per SEC website). When OIEA receives a complaint, they may decide to pass it on to relevant parts of the SEC so that the SEC can use the information and launch investigations if they deem it to be appropriate. Investors can also turn to FINRA, which has a dispute resolution centre where arbitration and mediation can be used – both are less costly than going to the courts.

54. With regards to Custodians**,** a Mutual fund must place and maintain its assets with a qualified custodian as per the rules under the ICA. This is typically a US bank meeting certain capital requirements or a broker dealer but the ICA also permits the use of regulated foreign banks or foreign securities depositaries. Under certain conditions, the fund can act as its own custodian. Under the requirements of the AIFMD, because the Member State of reference has to authorize the non-EU AIFM wishing to market AIFs in the EU, and that the non-EU AIFM has to comply with the AIFMD requirements, including depositary rules, the system with self-custody would not be accepted for AIFMs and AIFs that intend to use the EU-passport[9].

55. In relation to the regulatory scope**,** there are several regulatory bodies responsible for the regulation of retail funds in the USA: the SEC which is the principal regulatory body; FINRA which is a self-regulatory organisation overseeing securities firms doing business in the US (Regulation promulgated by the FINRA govern FINRA members' sales and marketing of fund shares.). FINRA is overseen by the SEC and must report to it in order to ensure compliance. Finally, the CFTC regulates futures, options and swaps markets in the US (and mutual funds that invest in these markets) and their advisers. Funds regulated by the SEC may therefore also be subject to regulation from the CFTC. The SEC also shares information relating to private funds with the OFR (Office of Financial Research).

56. As regards authorisation and supervision**,** at registration stage, the SEC requires a mutual fund to file a notification of registration and a registration statement. This statement, which must be updated annually, requires disclosure, inter alia, of:

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[9] SEC registered investment advisers are neither permitted to deal on behalf of clients nor to hold client assets, unless they are separately regulated to perform such functions (*e.g.*, an investment adviser that is also registered and regulated as a broker-dealer). If an investment adviser has "custody" (as defined) and is subject to the custody rule, such an investment adviser must use a "qualified custodian" to hold client assets. In particular, under the Investment Advisers Act of 1940, an investment adviser may not legally hold its clients assets (unless the adviser also is a broker-dealer, bank or other entity that meets the definition of a "qualified custodian" and is regulated as such). An investment adviser also cannot hold client assets indirectly by putting them in a bank account or broker-dealer account in the adviser's own name (except if the assets are held in the name of the adviser as agent or trustee for clients). Client assets are required to be kept with qualified custodians, such as banks or broker-dealers, because those institutions are regulated specifically for the safekeeping of assets. The Advisers Act nonetheless deems an adviser to "have custody," and be subject to additional regulation (e.g. an annual surprise exam by an independent accountant to verify client assets), in certain situations, such as when the adviser is authorized or permitted to direct client assets to a third party (such as being able to instruct a bank to pay bills) or the adviser is authorized or permitted to obtain possession of client assets, such as when an adviser acts in a capacity (such as trustee of a trust) that gives that adviser or any of its supervised persons legal ownership of or access to client assets. In other words, an adviser can "have custody" in certain circumstances under the very broad definition in the Advisers Act (and be subject to additional regulation for the protection of investors), even though it does not "hold custody" in the more common way that custody is understood.

- The fund's investment objectives, strategies and related risks;
- Fees and annual fund operating expenses;
- Performance information;
- The fund's adviser;
- How to purchase shares.

57. Mutual funds may offer their shares through a distributor registered with the SEC as a broker-dealer under the Exchange Act. Distributors are also members of FINRA and subject to its rules and regulations. The distributor purchases shares from the fund and then sells them to the public directly or indirectly through intermediaries.

58. As regards the alignment of incentives between the AIFM and investors, similar remuneration rules as set out in the AIFMD do not seem to be currently applied in the US. ESMA notes that some stakeholders mentioned that the implementation of such rules in the case of US managers wishing to market their funds in the EU using the AIFMD passport might be an obstacle to the success of the AIFMD passport. This might tend to show that AIFMD-like rules on remuneration do indeed not exist at the moment in the US, and that the AIFMD rules on remuneration are significantly different from what is being applied in the US[10].

59. Regarding principle 24 IOSCO**,** on the regulatory regime in the US, the FSAP report on the US[11] indicates that Principle 24 of the IOSCO principles is only Partly Implemented. The FSAP report states that the reasons for the partly implemented grade were "the limited examination coverage of IAs and investment companies" and "the absence of express eligibility requirements for CPO and IAs in particular in relation to internal controls and risk management". In relation to the latter the FSAP team noted that, in practice, many elements that a risk management framework would entail are covered by the existing obligations. These include the compliance rule, the record keeping rules, the custody rules, the obligation to supervise and the segregation requirements. The assessors considered that, as such, the current framework broadly achieves the objectives of the principle, but encouraged the authorities to add an explicit rule so as to comply with IOSCO Principles and ensure their expectations in this area are well understood by the market.

[10] Section 205(a)(1) of the Advisers Act includes some rules on performance fees for registered funds. In addition, In terms of remuneration of investment advisers to registered funds, the fund's board of directors, particularly the independent directors, and the fund's shareholders bear primary responsibility for assessing the remuneration of the fund's asset manager. Section 15(a) of the Investment Company Act prohibits a person from serving as an investment adviser to a registered fund except pursuant to a written advisory contract that has been approved by a vote of the majority of the fund's independent directors and by a vote of the majority of the holders of the fund's outstanding voting securities. In addition, section 15(c) requires fund directors to request and evaluate such information as may be reasonably necessary to evaluate the continuing terms of the advisory contract and requires investment advisers to furnish this information to the registered fund's directors. In certain cases, material changes to an existing advisory contract require shareholder approval. When shareholder approval of the adviser's contract is sought under section 15, certain information regarding the adviser and the contract, including the compensation to be paid under the contract, must be provided in the shareholder proxy statement provided to shareholders. Section 36(b) of the Investment Company Act imposes on investment advisers of registered investment companies a specific fiduciary duty with respect to the receipt of any compensation for services, or of payments of a material nature, paid by the fund or its shareholders to the adviser or an affiliate. It authorizes the Commission or any security holder of the investment company, on behalf of the investment company, to sue for breach of that duty.

[11] Detailed assessment of implementation of the IOSCO objectives and principles of securities regulation in the US: https://www.imf.org/external/pubs/ft/scr/2015/cr1591.pdf

2) Market disruption:

Examples of questions that may be applied under this heading include:

a) To what extent would the granting of the passport to the non-EU AIFMs and AIFs unduly undermine the activity of existing EU AIFMs due to differences in the regulatory environment in the non-EU country and allow them to change their operating arrangements so as to circumvent the AIFMD?
b) Is there evidence that the granting of the passport to non-EU AIFMs would reduce or improve investor choice (in the short-run or the long-run)?

Assessment in the case of the US

60. Please see the following assessment of questions related to the “obstacles to competition” criteria.

3) Obstacles to competition:

Examples of questions that may be applied under this heading include:

a) Is the process operated by the non-EU NCA to (a) authorise EU AIFMs or (b) allow marketing of EU AIFs in the non-EU country reasonable (in terms of clarity, predictability, cost and regulatory expectation)? Is there a level playing field between EU and non-EU AIFMs as regards market access, particularly in view of the procedures that would apply to non-EU AIFMs under Article 37 in the event that the passport is extended?
b) Are EU AIFMs and EU AIFs treated in the same way as managers and collective investment undertakings of the non-EU country in terms of regulatory engagement (including regulatory fees and documentation to be provided prior to the authorisation)?

Assessment in the case of the US

61. ESMA is of the view that as of today, it is possible to market funds in the US for EU-AIFMs. The easiest way for EU-AIFMs to publicly market and sell issues/shares in the USA is to organize a fund in the USA and register this fund under the Investment Company Act of 1940 the so-called ‘1940 Act’. The 1940 Act imposes the same regulatory standards on all funds, regardless of whether they are managed by a domestic or foreign manager. The funds can be managed and administered outside of the USA. A foreign or an American manager to a fund is required to register under the Investment advisers Act of 1940. This Act does not require a U.S place of business requirements. EU managers can therefore establish wholly-owned affiliates in the USA or decide to provide services from Europe.

62. However, it remains generally more difficult to market foreign funds in this jurisdiction, especially to retail investors. A foreign manager that does not want to establish funds in the U.S but want to market its existing foreign funds in the USA has two options.

1. Under Section 7(d) of the 1940 Act, an investment company organized in a foreign jurisdiction may offer publicly its securities if the SEC finds that ‘it is both legally and practically feasible to effectively enforce the provisions of the 1940 Act’ against the fund. Section 7(d) represents a prudential standard to ensure that US investors receive the same investor protections whether they acquire shares in a foreign fund or in a US-domiciled fund. Only a few foreign funds use this approach because the requirements of Section 7(d) imposes constraints on their ability to sell their shares in the USA because of differences in business and regulatory environments between the USA and the country of origin;

2. A foreign manager can sell its foreign fund shares privately without registering the fund or receiving approval to sell the fund from the SEC under Section 7(d) of the 1940 Act.
3. The manager, in this instance, is required to
    a. Claim an exception for the fund itself under the 1940 Act;
    b. Claim an exemption for the shares of the fund under the Securities Act;
    c. Register or claim an exemption for itself and the fund under the commodity Exchange Act;
    d. qualify the fund under state blue sky laws (make a notice filing and pay a fee in each state in which an investor in the fund resides).

63. Overall only a few non-US funds have used the process under Section 7(d) to sell to U.S. retail investors. Most firms use the following: (1) organize funds in the U.S.; (2) set up master-feeder structures in the U.S. and non-U.S. funds pool their assets in a U.S. master fund: (3) create mirror funds in which a U.S. fund pools their assets in a U.S. master fund; or (4) privately offer securities of a non-U.S. fund in the U.S.

64. The implications of the Volcker rule could also be considered as part of the evaluation under these criteria. The Volcker Rule was published in December 2013 by the five US financial authorities (Federal Reserve, CFTC, SEC, FDIC, OCC). It provides different obligations/restrictions regarding proprietary trading and investment in "covered funds" by "banking entities". ESMA’s current understanding is that the Volcker Rule might have implications for European actors in the asset management industry notably in relation to the scope of the entities that might qualify as “banking entities” or “covered funds”.

65. ESMA is of the view that in the context of a potential extension of the AIFMD passport towards the US, there is the risk of an unlevel playing field between EU and non-EU AIFMs as regards market access.[12]

66. ESMA is of the view that the market conditions of U.S funds dedicated to professional investors in the EU in the event that the AIFMD passport is extended to the U.S

[12] It is the understanding of ESMA that there exists a more favourable regime for the marketing of funds domiciled in certain jurisdictions (e.g. Canada).

would be different from the market access conditions of EU funds dedicated to professional investors in the U.S, notably due to registration requirements under the U.S regulatory framework (which generate additional costs).

67. As a consequence, ESMA considers that if similar conditions in terms of access to the market is to be considered by the European Parliament, the Council and the Commission as a predominant criterion in relation to competition in order to decide on the potential extension of the AIFMD passport to non-EU countries, the decision to extend the AIFMD passport to the U.S should be delayed until better conditions of market access are granted by the US Authorities to EU AIFMs/AIFs, as abovementioned.

4) Monitoring of systemic risk:

Examples of questions that may be applied under this heading include:

a) Does there exist tangible evidence of adequate surveillance of market developments with a view to tracking potential (or actual) systemic risks[13] by the NCA in the non-EU country?

b) How does the regulatory regime in the non-EU country measure up against the IOSCO principle 6?

Assessment in the case of the US

68. ESMA is of the view that the reporting obligations for US Managers are extensive, but differs from the requirements in the AIFMD to some extent. The FSAP report indicates that IOSCO Principle 6 is Broadly Implemented.

[13] Where the definition of 'systemic risk' is not simply confined to the local jurisdiction but also has regard for spillover effects of the AIFMs or AIFs operating outside of the borders of the local jurisdiction.

General advice on the potential extension of the passport to the U.S

Having regard to the above assessment by ESMA regarding the extent to which there would be significant obstacles regarding investor protection, competition, market disruption and the monitoring of systemic risk impeding the application of the AIFMD passport to the U.S, ESMA advises the European Parliament, the Council and the Commission to delay their decision on the application of the passport to the U.S until such time as conditions which might lead to a distortion of competition are addressed, as explained in the previous paragraphs.

As regards the investor protection criterion, ESMA also notes that it could have benefited from having more time to assess the detailed information it received on the U.S. regulatory framework and, in particular, to analyse the extent to which the differences between the U.S. regulatory framework and the AIFMD are material to the present assessment.

2.4 Guernsey

69. The present section includes the assessment by ESMA on the potential granting of the AIFMD passport to Guernsey based on the methodology described in section 2. 1. The feedback received from the responses to the call for evidence launched by ESMA in November 2014 in relation to the case of Guernsey is presented in Annex 3.

70. **Criteria, Methodology and Data to assess the potential extension of the AIFMD passport to Guernsey**

71. First, ESMA notes that the preconditions, including that for an MoU with non-EU NCAs set out in Articles 35 and 37 and there should be no doubt in relation to the <u>ongoing</u> satisfaction of these. As Article 35 is not yet in operation we need to review the way in which the MoUs required under Article 34(1)(b) and Article 36(1)(b) have been applied. In particular, in relation to the MoUs under Articles 34 and 36, there should be two tests:

1. How has the existing MoU worked? Are there positive or negative experiences to report? For example:

   1. Is there efficient collaboration in accordance with the provisions of the MoU on supervisory cooperation?
   2. Is there timely and prompt collaboration in case of emergency situations?
   3. Is non-requested information shared with the EU authorities at the initiative of the non-EU authority?
   4. Have legal limitations been encountered in sharing information or performing on-site visits?
   5. Has there been a significant level of lack of cooperation from the non-EU AIFMs?
   6. Does the non-EU NCA recognise the role played by each EU NCA (as part of the network of EU securities supervisors) and is the non-EU NCA open to bilateral relationships with each EU NCA?

2. In the absence of evidence in relation to the working of an existing MoU, does previous supervisory engagements provide support for the expectation of good supervisory cooperation, or not?

<u>Assessment in the case of Guernsey</u>

72. ESMA is of the view that there have been positive experiences in terms of cooperation between NCAs and the Authority of Guernsey.

73. One NCA explicitly indicated they are of the opinion that the existing MoU has worked well. The Guernsey NCA has responded within 15 days when this NCA has asked for assistance. This NCA has performed on-site visits together with the Authority of Guernsey and has good experiences from this. As regards other NCAs, there is limited experience when it comes to the criteria in 1. e). It is therefore difficult for them to evaluate the possible lack of cooperation from non-EU AIFMs.

74. Second, in relation to Art 67(4), the following criteria should be used to assess the situation of other non-EU countries in relation to the potential extension of the AIFMD passport to those non-EU countries.

1) <u>Investor protection</u>:

Examples of information that may be relevant under this heading include:

i) Is there evidence that some investor complaints are not being adequately tackled by the non-EU NCA?

ii) What rules or mitigants does the non-EU country have in relation to (a) the safeguarding of assets, (b) the function of the depositary and management of conflicts of interest between the AIFM and the depository, (c) the prudential soundness of the AIFM, (d) the timeliness and accuracy of disclosures to investors, (e) the alignment of incentives between the AIFM and investors? Insofar as these rules or mitigants exist in the non-EU countries, to what extent do these rules or mitigants measure up to those in AIFMD?

iii) How does the regulatory regime in the third country measure up against the relevant IOSCO principles, in particular its level of regulatory and supervisory engagement as assessed against principles 10 to 12[14] (including whether the regime is assessed as being at least 'broadly implemented' under each of these principles)?

iv) What is the scope of the non-EU authority's regulatory oversight with respect to the range of intermediaries and vehicles operating in the relevant country?

<u>*Assessment in the case of Guernsey*</u>

75. ESMA first notes that the Jersey and Guernsey Authorities indicated that the Joint Channel Islands (Jersey and Guernsey) Financial Services Ombudsman scheme will be open to all individual/small businesses and is not limited to retail clients. It will be able to look at complaints from individual customers and small businesses, wherever they reside in the world. Complaints will be able to be made about financial services provided by a business in Jersey or Guernsey involving: banking; lending; money services; insurance; pensions; and investments. The ombudsman will be able to award compensation of up to £150,000. This is similar to the scheme in place in the UK.

76. In Guernsey, ESMA also notes that professional clients usually use the Courts although there is also the possibility to use alternative dispute resolution through mediation mechanisms. The Commission also has an official complaint handling

[14] And the following IOSCO principles: 4, 13, 14, 15, 24, 25, 26, 27, 28 and 32.

procedure and openly and publically welcomes information regarding unsolved complaints from professional investors and institutions. Based on such information, the Commission may decide to instigate its own investigation into matters connected with a complaint which could lead to supervisory or enforcement actions against the entity in question. Whilst the Commission has no power to adjudicate in a dispute they actively use the information about unresolved complaints as intelligence to highlight potential shortcomings in policies and/or procedures at regulated firms and determine that a complaint raises conduct, financial crime or prudential concerns about a regulated firm which the Commission can then act to correct.

77. As for the criteria in 1 ii), Guernsey has put in place an AIFMD-like regime which is an opt-in regime for Guernsey AIFMs wishing to market their AIFs in the EU under the AIFMD passport requirements. The current framework applicable in Guernsey (i.e. not the aforementioned opt-in regime) includes certain differences with the AIFMD, especially regarding the custody and the remuneration requirements. However, the AIFMD-like rules will apply under the abovementioned opt-in regime for Guernsey AIFMs wishing to market their AIFs in the EU under the AIFMD passport requirements.

78. On depositaries, ESMA is of the view that Guernsey's traditional and current approach to trustee oversight of open-ended funds is to a certain extent similar to AIFMD requirements and was in essence based on the UK's regulatory framework. Designated Custodian/Trustees are required to perform oversight of valuations, share dealing and investment restriction functions, in addition to providing safe custody of assets. Prudential requirements are stringent: designated Custodian/Trustees are also required to maintain net assets of £4,000,000. Under the law (The Protection of Investors (Bailiwick of Guernsey) Law, 1987, as amended ("the POI Law")), the requirement is for a locally licensed Designated Custodian/Trustee to be appointed to an authorised or registered open-ended collective investment scheme, and this Designated Custodian/Trustee to provide safe custody and trustee oversight, where applicable. However there is no obligation in the case of a closed-ended authorised or registered fund to appoint a custodian as long as it is clear in the prospectus of the Fund who is responsible for safe-keeping of the assets. This service may be carried out by the Designated Manager of the relevant fund and in such circumstances the Designated Manager of the scheme must be licensed to provide custody services under the POI Law. Historically, there was no requirement for separate trustee oversight over closed-ended funds. This was addressed in the AIFMD equivalent regime and the regime for Article 36 business. During 2014 a document was issued to provide guidance on how Article 36 of AIFMD interacts with the Bailiwick of Guernsey's existing regime[15]. Therefore, the AIFMD depositary rules will apply under the abovementioned opt-in regime for all Guernsey AIFMs wishing to market their AIFs in the EU under the AIFMD passport requirements.

[15] These guidance notes can be found at: http://www.gfsc.gg/The-Commission/Policy%20and%20Legislation/Article%2036%20of%20AIFMD%20-%20Depositary%20Requirements%20Guidance%20Notes%20Post-Consultation.pdf

79. In regards to remuneration, the Guernsey Authority explained that they follow an impact and risk based supervision model. The current regime contains eleven discrete risk categories. Whilst they have no set quantitative remuneration rules, management remuneration is a component factor of the evaluation of supervised entities' business model risk; governance risk; and conduct risk.

80. However the Guernsey AIFMD regime is identical to the EU regime. Article 13 of AIFMD was transposed verbatim into section 8.1 of The AIFMD Rules, 2013:

"*Guernsey AIFMs must have remuneration policies and practices for those categories of staff, including senior management, risk takers, control functions, and any employees receiving total remuneration that takes them into the same remuneration bracket as senior management and risk takers, whose professional activities have a material impact on the risk profiles of the AIFMs or of the AIFs they manage, that are consistent with and promote sound and effective risk management and do not encourage risk-taking which is inconsistent with the risk profiles or AIF constitutional documents of the AIFs they manage*"

81. As regards IOSCO principles in Guernsey, there is only one NCA in Guernsey with oversight duties. The IOSCO FSAP on Guernsey dates back to 2009 and Guernsey received positive outcomes at the time.

2) Market disruption:

Examples of questions that may be applied under this heading include:

(a) To what extent would the granting of the passport to the non-EU AIFMs and AIFs unduly undermine the activity of existing EU AIFMs due to differences in the regulatory environment in the non-EU country and allow them to change their operating arrangements so as to circumvent the AIFMD?

(b) Is there evidence that the granting of the passport to non-EU AIFMs would reduce or improve investor choice (in the short-run or the long-run)?

Assessment in the case of Guernsey

82. ESMA is of the view that the granting of the passport to non-EU AIFMs would probably result in more Guernsey AIFs on the EU market. Especially, more hedge funds are likely to be marketed in the EU. It is difficult to predict the impact on investor choice from the increased number of funds made available on the EU market in the long term.

3) Obstacles to competition:

Examples of questions that may be applied under this heading include:

(a) Is the process operated by the non-EU NCA to (a) authorise EU AIFMs or (b) allow marketing of EU AIFs in the non-EU country reasonable (in terms of clarity, predictability, cost and regulatory expectation)? Is there a level playing field between EU and non-EU AIFMs as regards market access, particularly in view of the procedures that would apply to non-EU AIFMs under Article 37 in the event that the passport is extended?

(b) Are EU AIFMs and EU AIFs treated in the same way as managers and collective investment undertakings of the non-EU country in terms of regulatory engagement (including regulatory fees and documentation to be provided prior to the authorisation)?

Assessment in the case of Guernsey

83. ESMA is of the view that EU-AIFMs that wish to establish business in Guernsey have to comply with the same rules as national AIFMs. ESMA is of the view that there are no identified competition issues on that aspect.

4) Monitoring of systemic risk:

Examples of questions that may be applied under this heading include:

1) Does there exist tangible evidence of adequate surveillance of market developments with a view to tracking potential (or actual) systemic risks[16] by the NCA in the non-EU country?

2) How does the regulatory regime in the non-EU country measure up against the IOSCO principle 6?

Assessment in the case of Guernsey

84. ESMA is of the view that Guernsey has frameworks in place for addressing systemic risks. Reporting obligations in Jersey are similar to the AIFMD reporting obligations.

General advice on the potential extension of the passport to Guernsey

Having regard to the above assessment ESMA is of the view that there are no significant obstacles regarding investor protection, competition, market disruption and the monitoring of systemic risk impeding the application of the AIFMD passport to Guernsey**.**

[16] Where the definition of 'systemic risk' is not simply confined to the local jurisdiction but also has regard for spillover effects of the AIFMs or AIFs operating outside of the borders of the local jurisdiction.

2.5 Jersey

85. The present section includes the assessment by ESMA on the potential granting of the AIFMD passport to Jersey based on the methodology described in the section 2. 1. The feedback received from the responses to the call for evidence launched by ESMA in November 2014 in relation to the case of Jersey is presented in Annex 4.

Criteria, Methodology and Data to assess the potential extension of the AIFMD passport to Jersey

86. First, ESMA notes that the preconditions, including that for an MoU with non-EU NCAs set out in Articles 35 and 37 and there should be no doubt in relation to the ongoing satisfaction of these. As Article 35 is not yet in operation we need to review the way in which the MoUs required under Article 34(1)(b) and Article 36(1)(b) have been applied. In particular, in relation to the MoUs under Articles 34 and 36, there should be two tests:

1. How has the existing MoU worked? Are there positive or negative experiences to report? For example:

a) Is there efficient collaboration in accordance with the provisions of the MoU on supervisory cooperation?
b) Is there timely and prompt collaboration in case of emergency situations?
c) Is non-requested information shared with the EU authorities at the initiative of the non-EU authority?
d) Have legal limitations been encountered in sharing information or performing on-site visits?
e) Has there been a significant level of lack of cooperation from the non-EU AIFMs?
f) Does the non-EU NCA recognise the role played by each EU NCA (as part of the network of EU securities supervisors) and is the non-EU NCA open to bilateral relationships with each EU NCA?

2. In the absence of evidence in relation to the working of existing MoU, does previous supervisory engagements provide support for the expectation of good supervisory cooperation, or not?

Assessment in the case of Jersey

87. ESMA is of the view that there have been positive experiences in terms of cooperation between NCAs and the Authority of Jersey. The Jersey Authority

indicated that they have provided assistance to 21 European authorities – both in the funds sector and in other sectors (including the Spanish tax authority).

88. One NCA explicitly indicated they are of the opinion that the existing MoU has worked well. The Jersey NCA has responded within 15 days when this NCA has asked for assistance. This NCA has performed on-site visits together with the Authority of Jersey and has good experiences from this. As regards other NCAs, there is limited experience when it comes to the criteria in 1. e), it is therefore difficult for them to evaluate the possible lack of cooperation from non-EU AIFMs.

89. Second, in relation to Art 67(4), the following criteria should be used to assess the situation of other non-EU countries in relation to the potential extension of the AIFMD passport to those non-EU countries.

1) Investor protection:

Examples of information that may be relevant under this heading include:

i) Is there evidence that some investor complaints are not being adequately tackled by the non-EU NCA?

ii) What rules or mitigants does the non-EU countries have in relation to (a) the safeguarding of assets, (b) the function of the depositary and management of conflicts of interest between the AIFM and the depository, (c) the prudential soundness of the AIFM, (d) the timeliness and accuracy of disclosures to investors, (e) the alignment of incentives between the AIFM and investors? Insofar as these rules or mitigants exist in the non-EU countries, to what extent do these rules or mitigants measure up to those in AIFMD?

iii) How does the regulatory regime in the third country measure up against the relevant IOSCO principles, in particular its level of regulatory and supervisory engagement as assessed against principles 10 to 12[17] (including whether the regime is assessed as being at least 'broadly implemented' under each of these principles)?

iv) What is the scope of the non-EU authority's regulatory oversight with respect to the range of intermediaries and vehicles operating in the relevant country?

Assessment in the case of Jersey

90. ESMA first notes that the Jersey and Guernsey Authorities indicated that the Joint Channel Islands (Jersey and Guernsey) Financial Services Ombudsman scheme will be open to all individual/small businesses and is not limited to retail clients. It will be

[17] And the following IOSCO principles: 4, 13, 14, 15, 24, 25, 26, 27, 28 and 32.

able to look at complaints from individual customers and small businesses, wherever they reside in the world. Complaints will be able to be made about financial services provided by a business in Jersey or Guernsey involving: banking; lending; money services; insurance; pensions; and investments. The ombudsman will be able to award compensation of up to £150,000. This is similar to the scheme in place in the UK.

91. In Jersey, ESMA also notes that there is also a complaints process through the Jersey Commission although, as in Guernsey and the UK, institutional clients usually tend to resort to the courts in relation to their disputes. The complaints process is the same for all clients/investors. In relation to Jersey public funds, under the CIF Codes of Practice and in relation to Jersey fund service providers to public funds, under the FSB Codes of Practice there are also Codes of Practice requirements setting out the minimum complaints handling standards.

92. As for the criteria in 1 ii), Jersey has put in place an AIFMD-like regime which is an opt-in regime for Jersey AIFMs wishing to market their AIFs in the EU under the AIFMD passport requirements. The current framework applicable in Jersey includes certain differences with the AIFMD, especially regarding the requirements on custody and remuneration. However, the AIFMD-like rules will apply under the abovementioned opt-in regime for Jersey AIFMs wishing to market their AIFs in the EU under the AIFMD passport requirements.

93. On depositaries, ESMA is of the view that the requirements are similar to those under AIFMD but are based on IOSCO principles rather than AIFMD requirements. The requirement for a custodian relates to open-ended Jersey funds rather than closed-ended Jersey funds whereas AIFMD, although there is some provision for closed-ended funds, focuses on the type of assets, custody or record-keeping (i.e. transferrable and non-transferrable assets). For the purposes of a Jersey AIF Depositary then such depositary will need to comply with the AIFMD requirements in additional to the Jersey requirements. The Jersey requirements do show the level of functional independence which is similar to AIFMD. The requirements for retail funds (Recognized Funds / OCIF Funds) are more detailed than for expert funds, however all expert funds under the Expert Fund Guide ("EFG"), be they closed or open-ended funds, are required (again similar to AIFMD) to have an independent Jersey monitoring functionary in relation to the actions of the Investment Manager.

94. In regards to remuneration, the Jersey Authority indicated that they follow the ESMA guidance in relation to third countries (disclosure) but they have no other specific requirements currently. They are however keeping this under review and would be able to implement specific AIFMD remuneration requirements if required.

95. As regards IOSCO principles in Jersey, there is only one NCA with oversight duties. The IOSCO FSAP on Jersey dates back to 2009 but Jersey received positive outcomes at the time.

2) Market disruption:

Examples of questions that may be applied under this heading include:

(a) To what extent would the granting of the passport to the non-EU AIFMs and AIFs unduly undermine the activity of existing EU AIFMs due to differences in the regulatory environment in the non-EU country and allow them to change their operating arrangements so as to circumvent the AIFMD?
(b) Is there evidence that the granting of the passport to non-EU AIFMs would reduce or improve investor choice (in the short-run or the long-run)?

Assessment in the case of Jersey

96. ESMA is of the view that the granting of the passport to non-EU AIFMs would probably result in more Jersey AIFs on the EU market. Especially, more hedge funds are likely to be marketed in the EU. It is difficult to predict the impact on investor choice from the increased number of funds made available on the EU market in the long term.

3) Obstacles to competition:

Examples of questions that may be applied under this heading include:

a) Is the process operated by the non-EU NCA to (a) authorise EU AIFMs or (b) allow marketing of EU AIFs in the non-EU country reasonable (in terms of clarity, predictability, cost and regulatory expectation)? Is there a level playing field between EU and non-EU AIFMs as regards market access, particularly in view of the procedures that would apply to non-EU AIFMs under Article 37 in the event that the passport is extended?
b) Are EU AIFMs and EU AIFs treated in the same way as managers and collective investment undertakings of the non-EU country in terms of regulatory engagement (including regulatory fees and documentation to be provided prior to the authorisation)?

Assessment in the case of Jersey

97. ESMA is of the view that EU-AIFMs that wish to establish business in Jersey have to comply with the same rules as national AIFMs. ESMA is of the view that there are no identified competition issues on that aspect.

4) Monitoring of systemic risk:

Examples of questions that may be applied under this heading include:

a) Does there exist tangible evidence of adequate surveillance of market developments with a view to tracking potential (or actual) systemic risks[18] by the NCA in the non-EU country?

b) How does the regulatory regime in the non-EU country measure up against the IOSCO principle 6?

Assessment in the case of Jersey

98. ESMA is of the view that Jersey has frameworks in place for addressing systemic risks. Reporting obligations in Jersey are similar to the AIFMD reporting obligations.

General advice on the potential extension of the passport to Jersey
Having regard to the above assessment ESMA is of the view that there are no significant obstacles regarding investor protection, competition, market disruption and the monitoring of systemic risk impeding the application of the AIFMD passport to Jersey

[18] Where the definition of 'systemic risk' is not simply confined to the local jurisdiction but also has regard for spillover effects of the AIFMs or AIFs operating outside of the borders of the local jurisdiction.

2.6 Hong Kong

99. The present section includes the assessment by ESMA on the potential granting of the AIFMD passport to Hong Kong based on the methodology described in the section 2. 1. The feedback received from the responses to the call for evidence launched by ESMA in November 2014 in relation to the case of Hong Kong is presented in Annex 5.

Criteria, Methodology and Data to assess the potential extension of the AIFMD passport to Hong Kong

100. First, ESMA notes the preconditions for an MoU with non-EU NCAs set out in Articles 35 and 37 and considers there should be no doubt in relation to the <u>ongoing</u> satisfaction of these. As Article 35 is not yet in operation it is necessary to review the way in which the MoUs required under Article 34(1)(b) and Article 36(1)(b) have been applied. In particular, in relation to the MoUs under Articles 34 and 36, there should be two tests:

1. How has the existing MoU worked? Are there positive or negative experiences to report? For example:

   a) Is there efficient collaboration in accordance with the provisions of the MoU on supervisory cooperation?
   b) Is there timely and prompt collaboration in case of emergency situations?
   c) Is non-requested information shared with the EU authorities at the initiative of the non-EU authority?
   d) Have legal limitations been encountered in sharing information or performing on-site visits?
   e) Has there been a significant level of lack of cooperation from the non-EU AIFMs?
   f) Does the non-EU NCA recognise the role played by each EU NCA (as part of the network of EU securities supervisors) and is the non-EU NCA open to bilateral relationships with each EU NCA?

2. In the absence of evidence in relation to the working of existing MoU, does previous supervisory engagement provide support for the expectation of good supervisory cooperation, or not?

<u>Assessment in the case of Hong Kong</u>

101. Based on the feedback received from NCAs, ESMA is of the view that the experiences of cooperation with the Hong Kong Authorities are, in general terms, positive. Previous supervisory engagements provide support for the expectation of good supervisory cooperation.

102. Second, in relation to Art 67(4), the following criteria should be used to assess the situation of other non-EU countries in relation to the potential extension of the AIFMD passport to those non-EU countries.

1) <u>Investor protection</u>:

Examples of information that may be relevant under this heading include:

i) Is there evidence that some investor complaints are not being adequately tackled by the non-EU NCA?

ii) What rules or mitigants does the non-EU countries have in relation to (a) the safeguarding of assets, (b) the function of the depositary and management of conflicts of interest between the AIFM and the depository, (c) the prudential soundness of the AIFM, (d) the timeliness and accuracy of disclosures to investors, (e) the alignment of incentives between the AIFM and investors? Insofar as these rules or mitigants exist in the non-EU countries, to what extent do these rules or mitigants measure up to those in AIFMD?

iii) How does the regulatory regime in the third country measure up against the relevant IOSCO principles, in particular its level of regulatory and supervisory engagement as assessed against principles 10 to 12[19] (including whether the regime is assessed as being at least 'broadly implemented' under each of these principles)?

iv) What is the scope of the non-EU authority's regulatory oversight with respect to the range of intermediaries and vehicles operating in the relevant country?

Assessment in the case of Hong Kong

103. As regards investor complaints, based on the feedback received from NCAs, ESMA is of the view that there is no evidence of complaints not being adequately tackled by the non-EU NCA of Hong Kong.

104. In relation to question 1) ii) ESMA notes that detailed information on the Hong Kong regulatory framework remains incomplete[20]. Therefore, more time is needed to analyse the extent to which the potential differences between the Hong Kong regulatory framework and the AIFMD are material to the assessment on the potential application of the AIFMD passport to Hong Kong.

105. There is not enough evidence in relation to the Hong Kong regulatory framework in relation to funds and their managers to assess how it compares to the AIFMD framework. However, ESMA notes that the enforcement of the framework is guaranteed by the supervisory powers of the Hong Kong Securities and Futures Commission. Some of the differences between the AIFMD and the Hong Kong regulatory framework should be further analysed, considering that Hong Kong has not implemented the AIFMD or a similar framework in its national law.

106. With respect to question 1) iii) ESMA notes that according to the 2014 IMF financial sector detailed assessment of implementation on IOSCO objectives and principles of

[19] And the following IOSCO principles: 4, 13, 14, 15, 24, 25, 26, 27, 28 and 32.
[20] At the time this advice was finalized, ESMA was still in contact with the Securities and Future Commission with a view to gathering more comprehensive information on the Hong Kong regulatory framework.

securities regulation on Hong Kong[21], Hong Kong was assessed as “Fully Implemented” with most of the principles referred to (except principle 12, with which it is “Broadly Implemented”).

107. With respect to question 1) iv), based on the 2014 IMF financial sector detailed assessment of implementation on IOSCO objectives and principles of securities regulation on Hong Kong and the answers provided by the SFC to the questions asked by ESMA, ESMA is of the view that a positive opinion can be expressed regarding the non-EU authority’s regulatory oversight with respect to the range of intermediaries and vehicles operating in Hong Kong.

2) Market disruption:

Examples of questions that may be applied under this heading include:

(a) To what extent would the granting of the passport to the non-EU AIFMs and AIFs unduly undermine the activity of existing EU AIFMs due to differences in the regulatory environment in the non-EU country and allow them to change their operating arrangements so as to circumvent the AIFMD?

(b) Is there evidence that the granting of the passport to non-EU AIFMs would reduce or improve investor choice (in the short-run or the long-run)?

Assessment in the case of Hong Kong

108. Please see the following assessment of questions related to the “obstacles to competition” criteria.

3) Obstacles to competition:

Examples of questions that may be applied under this heading include:

(a) Is the process operated by the non-EU NCA to (a) authorise EU AIFMs or (b) allow marketing of EU AIFs in the non-EU country reasonable (in terms of clarity, predictability, cost and regulatory expectation)? Is there a level playing field between EU and non-EU AIFMs as regards market access, particularly in view of the procedures that would apply to non-EU AIFMs under Article 37 in the event that the passport is extended?

(b) Are EU AIFMs and EU AIFs treated in the same way as managers and collective investment undertakings of the non-EU country in terms of regulatory engagement (including regulatory fees and documentation to be provided prior to the authorisation)?

[21] https://www.imf.org/external/pubs/cat/longres.aspx?sk=41750.0

Assessment in the case of Hong Kong

109. ESMA is of the view that based on the information provided in the answers of the Hong Kong Authority to ESMA's questions, that the procedures seem similar to the authorisation procedures for EU AIFMs.

110. ESMA is of the view that taking into consideration the responses to the call for evidence launched by ESMA and the answers of the Hong Kong Authority to ESMA questions, and because some EU Member States, but not all of them are considered as "acceptable inspection regimes" by the Hong Kong Authority, it is not clear whether there is a level playing field between EU and non-EU AIFMs as regards market access and whether EU AIFMs and EU AIFs are treated in the same way as managers and collective investments schemes of Hong-Kong in terms of regulatory engagement.

4) Monitoring of systemic risk:

Examples of questions that may be applied under this heading include:

g) Does there exist tangible evidence of adequate surveillance of market development with a view to tracking potential (or actual) systemic risks[22] by the NCA in the non-EU country?

b) How does the regulatory regime in the non-EU country measure up against the IOSCO principle 6?

111. The regulatory regime of Hong Kong was assessed as "Broadly Implemented" in the 2014 IMF financial sector detailed assessment of implementation on IOSCO objectives and principles of securities regulation on Hong Kong, with respect to principle 6. The responses of Hong Kong Authority to ESMA's questions are in line with this assessment.

[22] Where the definition of 'systemic risk' is not simply confined to the local jurisdiction but also has regard for spillover effects of the AIFMs or AIFs operating outside of the borders of the local jurisdiction.

General advice on the potential extension of the passport to Hong Kong

112. Having regard to the above assessment by ESMA regarding the extent to which there would be significant obstacles regarding investor protection, competition, market disruption and the monitoring of systemic risk impeding the application of the AIFMD passport to Hong Kong, ESMA notes that detailed information on the Hong Kong regulatory framework remains incomplete[23]. Therefore, more time is needed to analyse the extent to which the potential differences between the Hong Kong regulatory framework and the AIFMD may be material to the assessment on the potential application of the AIFMD passport to Hong Kong.

113. ESMA also notes that some EU Member States are considered as "acceptable inspection regimes" by the Hong Kong Authorities, but most of them are not. It is therefore not clear whether there is a level playing field between EU and non-EU AIFMs as regards market access (that is, there is uncertainty as to whether all EU AIFMs benefit from the same market access conditions in Hong Kong, and whether they would benefit from the same market conditions as Hong Kong managers in the EU if Hong Kong were to be granted the AIFM passport) and whether EU AIFMs and EU AIFs are treated in the same way as managers and collective investment schemes of Hong Kong in terms of regulatory engagement.

[23] At the time this advice was finalized, ESMA was still in contact with the Securities and Future Commission with a view to gathering more comprehensive information on the Hong Kong regulatory framework.

2.7 Switzerland

114. The present section includes the assessment by ESMA on the potential granting of the AIFMD passport to Switzerland based on the methodology described in section 2.1. The feedback received from the responses to the call for evidence launched by ESMA in November 2014 in relation to the case of Switzerland is presented in Annex 6.

Criteria, Methodology and Data to assess the potential extension of the AIFMD passport to Switzerland

115. First, ESMA notes the preconditions for an MoU with non-EU NCAs set out in Articles 35 and 37 and considers that there should be no doubt in relation to the <u>ongoing</u> satisfaction of these. As Article 35 is not yet in operation it is necessary to review the way in which the MoUs required under Article 34(1)(b) and Article 36(1)(b) have been applied. In particular, in relation to the MoUs under Articles 34 and 36, there should be two tests:

1. How has the existing MoU worked? Are there positive or negative experiences to report? For example:

a) Is there efficient collaboration in accordance with the provisions of the MoU on supervisory cooperation?
b) Is there timely and prompt collaboration in case of emergency situations?
c) Is non-requested information shared with the EU authorities at the initiative of the non-EU authority?
d) Have legal limitations been encountered in sharing information or performing on-site visits?
e) Has there been a significant level of lack of cooperation from the non-EU AIFMs?
f) Does the non-EU NCA recognise the role played by each EU NCA (as part of the network of EU securities supervisors) and is the non-EU NCA open to bilateral relationships with each EU NCA?

2. In the absence of evidence in relation to the working of existing MoU, does previous supervisory engagement provide support for the expectation of good supervisory cooperation, or not?

<u>Assessment in the case of Switzerland</u>

116. Although evidence is scarce on these points, ESMA notes that generally positive experiences have been reported by NCAs on the cooperation with the Swiss Authority.

117. However in respect to question 2, one NCA reported that the cooperation process set out by article 38 of the Federal Act on Stock Exchanges and Securities Trading (SESTA) envisages some requirements for the transmission of information by the Swiss Authority to foreign National Competent Authorities. ESMA considered that the extent to which these requirements may affect the effectiveness of the entire cooperation process in terms of complexity and length merited further investigation.

118. ESMA notes that a process is under way in Switzerland to amend SESTA, including the provisions on cooperation. The process is at a relatively advanced stage and the new version of SESTA adopted by the Swiss Parliament in June is due to enter into force on 1 January 2016. One provision of the previous version of the Act that was potentially problematic related to the possibility for the decision of FINMA on the transmission of information to a foreign financial market supervisory authority to be challenged by a client before the Federal Administrative Court within ten days. The new version of the Act adopted by the Swiss Parliament introduces the possibility for FINMA to choose not to inform the client in advance of information being shared with a foreign regulator in cases where such prior information would undermine the purpose of the request and adversely affect the objectives of the requesting authority.

119. Second, in relation to Art 67(4), the following criteria should be used to assess the situation of other non-EU countries in relation to the potential extension of the AIFMD passport to those non-EU countries.

1) Investor protection:

Examples of information that may be relevant under this heading include:

i) Is there evidence that some investor complaints are not being adequately tackled by the non-EU NCA?

ii) What rules or mitigants does the non-EU countries have in relation to (a) the safeguarding of assets, (b) the function of the depositary and management of conflicts of interest between the AIFM and the depository, (c) the prudential soundness of the AIFM, (d) the timeliness and accuracy of disclosures to investors, (e) the alignment of incentives between the AIFM and investors? Insofar as these rules or mitigants exist in the non-EU countries, to what extent do these rules or mitigants measure up to those in AIFMD?

iii) How does the regulatory regime in the third country measure up against the relevant IOSCO principles, in particular its level of regulatory and supervisory engagement as assessed against principles 10 to 12[24], having regards to whether the

[24] And the following IOSCO principles: 4, 13, 14, 15, 24, 25, 26, 27, 28 and 32.

regime is assessed as being 'broadly' or 'fully' implemented' under each of these principles?

iv) What is the scope of the non-EU authority's regulatory oversight with respect to the range of intermediaries and vehicles operating in the relevant country?

Assessment in the case of Switzerland

120.On depositaries, ESMA is of the view that the requirements are overall similar to those under AIFMD. However these requirements differ on some specific points notably related to the situations where the appointment of a depositary is not mandatory (this is possible for some contractual funds in the Swiss regulatory framework if FINMA authorizes it, although it has never granted such an authorization thus far).

121.On remuneration rules, ESMA notes that FINMA has issued a Circular which sets out minimum standards for remuneration schemes of financial institutions („Circular 2010/1 Remuneration schemes"). The Circular, which entered into force on 1. January 2010, applies to banks, securities traders, financial groups and insurance companies, but also to fund management companies and other persons and firms authorized under the Collective Investment Schemes Act („CISA"). The minimum standards set out in the Circular are more simple than the ones required by the AIFMD but are comparable. [25]

122.Furthermore, the Swiss Funds & Asset Management Association SFAMA has issued a Code of Conduct (7. October 2014) which requires CISA Institutions to „*apply a salary and remuneration policy that is appropriate in accordance with the principle of proportionality, their size and their risk profile, and that motivates their employees to promote the long-term success of the collective investment schemes (in keeping with the minimum standards set out in FINMA Circular 2010/1 „Remuneration schemes")*."[26]

123. With specific reference to Switzerland (2014 IMF financial sector detailed assessment of implementation on IOSCO objectives and principles of securities regulation on Switzerland[27]), ESMA notes that there are "Partially Implemented" ratings on principles 12 (effective and credible use of powers) and 32 (dealing with failure). According to the IMF report, **the rating on principle 12** "*is primarily due to the fact that FINMA is still in the process of implementing its new supervisory approach regarding a more proactive engagement with audit firms and increased use of FINMA own supervisory reviews*." The IMF **comments on principle 32** refer to the need for FDF (Federal Department of Finance) to "*introduce appropriate legal requirements for the segregation of clients' funds by securities dealers that apply on*

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[25] http://www.finma.ch/e/regulierung/Documents/finma-rs-2010-01-e.pdf
[26] https://www.sfama.ch/en/self-regulation-model-documents/codes-of-conduct
[27] https://www.imf.org/external/pubs/cat/longres.aspx?sk=41882.0

ongoing basis and in bankruptcy". Moreover, the Swiss authorities "*should consider introducing an investor compensation scheme or equivalent regime to protect clients' securities in case of non-compliance with the segregation requirements*."

124. On principle 12, FINMA indicated that following these ratings its Asset Management Division had elaborated a new policy on how on-site supervisory reviews should be carried out in order to match the quality of supervisory reviews in the Banking and Insurance divisions. In addition, FINMA mentioned that a general reform of the supervisory audits was concluded in 2014 to give more guidance to external auditors when conducting work on behalf of FINMA. In preparation for the upcoming implementation of a new "Financial Services Act", that will significantly strengthen conduct rules for financial service providers, a cross-divisional working group has also been established to develop consistent processes to supervise new investment suitability rules.

125. As regards principle 32, FINMA indicated that an improvement in the segregation of client assets is under consideration for an upcoming amendment of insolvency law.

2) <u>Market disruption</u>:

Examples of questions that may be applied under this heading include:

(a) To what extent would the granting of the passport to the non-EU AIFMs and AIFs unduly undermine the activity of existing EU AIFMs due to differences in the regulatory environment in the non-EU country and allow them to change their operating arrangements so as to circumvent the AIFMD?
(b) Is there evidence that the granting of the passport to non-EU AIFMs would reduce or improve investor choice (in the short-run or the long-run)?

<u>*Assessment in the case of Switzerland*</u>

126. Please see the following assessment of questions related to the "obstacles to competition" criteria.

3) <u>Obstacles to competition</u>:

Examples of questions that may be applied under this heading include:

(a) Is the process operated by the non-EU NCA to (a) authorise EU AIFMs or to (b) allow marketing of EU AIFs in the non-EU country reasonable (in terms of clarity, predictability, cost and regulatory expectation)? Is there a level playing field between EU and non-EU AIFMs as regards market access, particularly in view of the procedures that would apply to non-EU AIFMs under Article 37 in the event that the passport is extended?

(b) Are EU AIFMs and EU AIFs treated in the same way as managers and collective investment undertakings of the non-EU country in terms of regulatory engagement (including regulatory fees and documentation to be provided prior to the authorisation)?

Assessment in the case of Switzerland

127. ESMA is of the view that there is no evidence of significant obstacles regarding competition and market disruption impeding the application of the AIFMD passport to Switzerland. However, the extent to which there could be different treatments of EU funds and managers depending on the existence of bilateral agreements between the Swiss Authority and the authority of some Member States could be relevant to the assessment of whether there are obstacles to competition.

128. In that respect, FINMA indicated that the distribution of EU CIS to retail clients in Switzerland is subject to approval by FINMA and requires, inter alia, an agreement on cooperation and the exchange of information between FINMA and the relevant foreign supervisory authorities. FINMA indicated that Switzerland has already concluded bilateral agreements (MoUs) with all interested EU Member States.

4) Monitoring of systemic risk:

Examples of questions that may be applied under this heading include:

a) Does there exist tangible evidence of adequate surveillance of market development with a view to tracking potential (or actual) systemic risks[28] by the NCA in the non-EU country?

b) How does the regulatory regime in the non-EU country measure up against the IOSCO principle 6?

Assessment in the case of Switzerland

129. ESMA is of the view that it does not have evidence of major issues in relation to the monitoring of systemic risk. The IMF assessment on the implementation of IOSCO Principle 6 (2014 IMF financial sector detailed assessment of implementation on IOSCO objectives and principles of securities regulation on Switzerland[29]) qualifies it as Broadly Implemented.

130. ESMA is of the view that there are no significant obstacles regarding the monitoring of systemic risk impeding the application of the passport to the Switzerland.

General advice on the potential extension of the passport to the Switzerland

[28] Where the definition of 'systemic risk' is not simply confined to the local jurisdiction but also has regard for spillover effects of the AIFMs or AIFs operating outside of the borders of the local jurisdiction.
[29] https://www.imf.org/external/pubs/cat/longres.aspx?sk=41882.0

Having regard to the above assessment by ESMA regarding the extent to which there would be significant obstacles regarding investor protection, competition, market disruption and the monitoring of systemic risk impeding the application of the AIFMD passport to Switzerland, ESMA advises the European Parliament, the Council and the Commission that there will be no significant obstacles impeding the potential application of the AIFMD passport to Switzerland, upon the enactment of the amendments to SESTA described in paragraph 118.

2.8 Singapore

131. The present section includes the assessment by ESMA on the potential granting of the AIFMD passport to Singapore based on the methodology described in section 2.1. The feedback received from the responses to the call for evidence launched by ESMA in November 2014 in relation to the case of Singapore is presented in Annex 7.

Criteria, Methodology and Data to assess the potential extension of the AIFMD passport to Singapore

132. ESMA notes that the preconditions for an MoU with non-EU NCAs set out in Articles 35 and 37 and considers there should be no doubt in relation to the <u>ongoing</u> satisfaction of these. As Article 35 is not yet in operation it is necessary to review the way in which the MoUs required under Article 34(1)(b) and Article 36(1)(b) have been applied. In particular, in relation to the MoUs under Articles 34 and 36, there should be two tests:

1. How has the existing MoU worked? Are there positive or negative experiences to report? For example:

   a) Is there efficient collaboration in accordance with the provisions of the MoU on supervisory cooperation?
   b) Is there timely and prompt collaboration in case of emergency situations?
   c) Is non-requested information shared with the EU authorities at the initiative of the non-EU authority?
   d) Have legal limitations been encountered in sharing information or performing on-site visits?
   e) Has there been a significant level of lack of cooperation from the non-EU AIFMs?
   f) Does the non-EU NCA recognise the role played by each EU NCA (as part of the network of EU securities supervisors) and is the non-EU NCA open to bilateral relationships with each EU NCA?

2. In the absence of evidence in relation to the working of an existing MoU, does previous supervisory engagement provide support for the expectation of good supervisory cooperation, or not?

<u>Assessment in the case of Singapore</u>

133. ESMA notes that the information regarding the cooperation between NCAs and the Monetary Authority of Singapore (MAS) is scarce and difficult to assess.

134. Second, in relation to Art 67(4), the following criteria should be used to assess the situation of other non-EU countries in relation to the potential extension of the AIFMD passport to those non-EU countries.

1) <u>Investor protection</u>.

Examples of information that may be relevant under this heading include:

i) Is there evidence that some investor complaints are not being adequately tackled by the non-EU NCA?

ii) What rules or mitigants does the non-EU countries have in relation to (a) the safeguarding of assets, (b) the function of the depositary and management of conflicts of interest between the AIFM and the depository, (c) the prudential soundness of the AIFM, (d) the timeliness and accuracy of disclosures to investors, (e) the alignment of incentives between the AIFM and investors? Insofar as these rules or mitigants exist in the non-EU countries, to what extent do these rules or mitigants measure up to those in AIFMD?

iii) How does the regulatory regime in the third country measure up against the relevant IOSCO principles, in particular its level of regulatory and supervisory engagement as assessed against principles 10 to 12[30] (including whether the regime is assessed as being at least 'broadly implemented' under each of these principles)?

iv) What is the scope of the non-EU authority's regulatory oversight with respect to the range of intermediaries and vehicles operating in the relevant country?

Assessment in the case of Singapore

135. ESMA is of the view that overall the requirements in terms of investor protection seem to be fulfilled. According to the 2013 IMF financial sector detailed assessment of implementation on IOSCO objectives and principles of securities regulation on Singapore (FSAP Report), all the relevant IOSCO principles are at least "broadly implemented".

136. A conclusion of the FSAP Report is that MAS is very strict when it comes to the market entry and that the authorization process is very detailed. According to the FSAP Report the follow up in regards of ongoing supervision does not keep those high standards. MAS is seen as a good gatekeeper which does not follow up at the same level once funds or managers are authorized. This might lead to difficulties with reporting and monitoring of systemic risk.

137. ESMA is of the view that there is not enough evidence to assess the extent to which there would be significant obstacles regarding investor protection impeding the application of the AIFMD passport to Singapore.

138. ESMA also notes that detailed information on the Singapore regulatory framework remains incomplete[31]. Therefore, more time is needed to analyse the extent to which the potential differences between the Singapore regulatory framework and the AIFMD may affect the assessment on the potential application of the AIFMD passport to Singapore.

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[30] And the following IOSCO principles: 4, 13, 14, 15, 24, 25, 26, 27, 28 and 32.

[31] At the time this advice was finalized, ESMA was still in contact with MAS with a view to gathering more comprehensive information on the Singapore regulatory framework.

2) Market disruption:

Examples of questions that may be applied under this heading include:

a) To what extent would the granting of the passport to the non-EU AIFMs and AIFs unduly undermine the activity of existing EU AIFMs due to differences in the regulatory environment in the non-EU country and allow them to change their operating arrangements so as to circumvent the AIFMD?
b) Is there evidence that the granting of the passport to non-EU AIFMs would reduce or improve investor choice (in the short-run or the long-run)?

Assessment in the case of Singapore

139. Please see the following assessment of questions related to the “obstacles to competition” criteria.

3) Obstacles to competition:

Examples of questions that may be applied under this heading include:

a) Is the process operated by the non-EU NCA to (a) authorise EU AIFMs or (b) allow marketing of EU AIFs in the non-EU country reasonable (in terms of clarity, predictability, cost and regulatory expectation)? Is there a level playing field between EU and non-EU AIFMs as regards market access, particularly in view of the procedures that would apply to non-EU AIFMs under Article 37 in the event that the passport is extended?
b) Are EU AIFMs and EU AIFs treated in the same way as managers and collective investment undertakings of the non-EU country in terms of regulatory engagement (including regulatory fees and documentation to be provided prior to the authorisation)?

Assessment in the case of Singapore

140. ESMA notes that the FSAP report mentions that managers should have a “sufficient nexus with Singapore” and therefore should have at least SGD 500 Mio AuM in Singapore (~EUR 335 Mio) to be authorised – this requirement should be investigated further as it could create a barrier to market access in the context of making the AIFM passport available to Singapore managers.

141. Reflecting on the current relationships with Singapore in the UCITS context, it seems that at the moment only UCITS from LU, IE, FR, UK and DE are recognised in Singapore. It is not clear if this is because no managers of other Member States sought authorisation before, or if Singapore does not recognise UCITS from other Member States as equivalent.

4) Monitoring of systemic risk:

Examples of questions that may be applied under this heading include:

a) Does there exist tangible evidence of adequate surveillance of market development with a view to tracking potential (or actual) systemic risks[32] by the NCA in the non-EU country?

b) How does the regulatory regime in the non-EU country measure up against the IOSCO principle 6?

Assessment in the case of Singapore

142. ESMA is of the view that there is not enough evidence to assess the extent to which there would be significant obstacles regarding the monitoring of systemic risk impeding the application of the AIFMD passport to Singapore

General advice on the potential extension of the passport to Singapore
Having regard to the above assessment by ESMA regarding the extent to which there would be significant obstacles regarding investor protection, competition, market disruption and the monitoring of systemic risk impeding the application of the AIFMD passport to Singapore, ESMA advises the European Parliament, the Council and the Commission to delay their decision on the potential application of the AIFMD passport to Singapore.

[32] Where the definition of 'systemic risk' is not simply confined to the local jurisdiction but also has regard for spillover effects of the AIFMs or AIFs operating outside of the borders of the local jurisdiction.

2.9 Other non-EU countries

143. In addition to the non-EU jurisdictions on which a detailed assessment was carried out and to the non-EU jurisdictions identified in section 2.2, ESMA gathered intelligence (notably from the responses to the call for evidence) on investor protection, competition, potential market disruption and monitoring of systemic risk with respect to the following non-EU countries:

    a. Malaysia

    b. Egypt

    c. Chile

    d. Peru

    e. India

    f. China

    g. Taiwan

144. Although some of these countries have been viewed by market participants as countries where the access to the market for EU UCITS and AIFs is less difficult than in the rest of the world, they have not been assessed in detail by ESMA at this stage because:

    a. no MoU has been agreed between these non-EU supervisory authorities and ESMA (acting on behalf of the national authorities within the EU); or

    b. the current level of activity by entities from these countries within the EU (i.e. the marketing of AIFs from these countries in the EU by EU AIFMs and/or the management/marketing of AIFs in the EU by AIFMs from these countries) did not justify a detailed assessment at this stage (please refer to section 2.2).

145. Regarding the first aspect noted above, ESMA will continue its efforts to agree an MoU with the authorities of the relevant jurisdictions. Regarding the second aspect, ESMA will monitor the evolution of the level of activity in order to determine whether a particular jurisdiction should be assessed in detail.

Annex 1 Summary of the responses to the call for evidence on transversal views on the impact of the possible extension of the passport to non-EU AIFMs on competition, market disruption, investor protection and the monitoring of systemic risk

A. Competition and market disruption

<u>Overall summary of the feedback</u>

Timing of the potential extension of the AIFMD passport to non-EU countries

146. A large number of respondents indicated that due to the limited experience in relation to the EU AIFMD passport, it was premature to decide on the possibility to extend it to non-EU countries, and that ESMA should advise the Commission to delay its decision, notably in order to confer to the AIFMD the possibility to develop into a true "AIFMD" brand, as in the case of UCITS.

147. These respondent encouraged ESMA and the Commission conduct a longer review period before making any recommendations on the functioning of the private placement and passport regimes, to better ensure there is sufficient information on which to base such recommendations.

Impact of the extension of the AIFMD passport while switching off the NPPR

148. Several respondents were of the view that an extension of the passport to non-EU AIFMs if the full requirements of the AIFMD were imposed on AIFMs had the potential to lead to significant market disruption if this was a precursor to switching off the NPPR. They were of the view that moving the regime in this direction would limit market access to only those AIFM able to comply with the full AIFMD requirements and that this would threaten to exclude non-EU AIFM/AIFs where non-EU jurisdictions were not prepared to adopt the detailed requirements of AIFMD. They indicated that this would potentially disrupt international capital market flows and raise precisely the same risks to EU markets and investors which were identified when the Directive was first debated.

NPPRNPPRs and the non-EU AIFMD passport

149. Therefore a vast majority of respondents indicated they were of the view that keeping the NPPRNPPRs in all non-EU countries that would not benefit from the passport, and even, in the view of some respondents, in those non-EU where the passport would have been established is of a paramount importance. They indicated that this NPPR allows Member States to set the standards imposed according to the needs of their national market, and that they should remain for an indefinite period.

150. Several respondents also pointed out that there is no urgent need to change the current regime in relation to the NPPR.

151. However, other respondents emphasized that the NPPR was burdensome because of the fragmentation of the rules applied by the different Member States (in that respect, please also see the Opinion on the functioning of the NPPR).

152. Other respondents indicated that as long as NPPR and the non-EU AIFMD passport would be available at the same time, and considering that the requirements set by the AIFMD are usually more burdensome compared to what is required by NPPRs, there would be an unlevel playing field from a perspective of an EU AIFM, because most non-EU managers would presumably not take the first option (passport regime).

153. Considering the country-by-country approach envisaged by ESMA, some respondents indicated that it was also worth noting that if NPPRs were to remain in force in those countries that would not be selected for the passport, this would result in market distortion between those non-EU countries taking advantage of the AIFMD passport and those still using the NPPRNPPRs.

Equivalent market access

154. A large number of respondents were also of the opinion that the elements of reciprocity in terms of access to the market and regulatory framework should be deemed requisite because the eventual extension of the AIFM passport to non-EU AIFM would have significant implications on the competitive landscape of investment funds within Europe. In their view, an unconditional opening of the EU Single Market to third country providers should be avoided, since it could put EU AIFMs at a competitive disadvantage, particularly in case of lighter regulatory regimes outside the EU. Some of these respondents were of the opinion that the EU single market for funds was already very opened compared with the majority of external non-EU markets.

155. In addition, these respondents underlined that if the regulatory constraints (linked to asset management regulation itself, but also to the depository- or custodian- one, taxation etc.) in a specific country are less important than in the EU, the competition would be unfair. In that respect, some respondents mentioned that that Europe in general has put in place a very comprehensive regulatory set of rules which, by far, differ from what is existing in most non-European countries.

156. In that respect, some respondents indicated that light-touch regulatory regimes in certain non-EU AIF domiciles facilitates the charging of lower initial and ongoing costs for the establishment and operation of AIFs in those domiciles. Failure to ensure that equal levels of regulation are applied to EU and non-EU AIFs which avail of the AIFMD passport could result in EU domiciles being undercut on price by non-EU domiciles, with a likely ensuing distortion of the market.

157. In relation to the regulatory framework, these respondents also emphasized that the enforcement of the regulatory framework was as important as the regulatory framework in itself.

158. In that context, some respondents indicated that in the vast majority of third countries, mutual recognition does not apply and therefore a European player would have to comply with the local rules (including local tax rules) in addition to its own home rules – making the cost to entry too high, and thus deterring it to enter the market. This respondent mentioned that as a result, only the biggest EU players would have the financial means to buy local firms or to launch local subsidiaries, managing local funds sold to local investors.

159. Against this background, these same respondents greatly welcomed the announcement made by ESMA not to treat all non-EU countries as a single block.

160. Some respondents indicated that an extension of the AIFMD passport should be subject to an assessment of the regulatory, supervisory and enforcement framework in the third country in question which should aim for equivalence of outcome in terms of regulatory environment. They saw this as a significant possibility to create further market access for EU AIFMs into non-EU countries that are not yet broadly accessible from a European perspective and therefore would encourage ESMA and the Commission to make use of this opportunity.

161. However, other respondents (notably from the private equity sector) indicated that would be in their view no particular non-EU country where, as a consequence of the regulatory environment (financial regulation, supervision, tax and anti-money laundering provisions), an eventual extension of the AIFMD passport would put EU AIFMs and UCITS management companies at a disadvantage vis-a-vis the AIFMs from that country. Some of these respondents were also of the view that from a legal point of view, having regards to the requirements under the AIFMD, it was unclear whether ESMA could even take into account the reciprocity criteria in its assessment.

Circumvention of the AIFMD

162. Several respondents mentioned that in the event that the AIFMD passport were extended to non-EU countries, ESMA and the Commission should carefully ensure that the EU AIFMD passport regime and its consequences (e.g. stricter rules on remuneration and on the depositary) is not circumvented by the creation of a new entity in the non-EU country that would not properly enforce or regulate these same requirements.

Assessment country by country

163. Several respondents provided input on the regulatory frameworks and potential barriers to entry in some non-EU countries in relation to EU funds and managers. These comments are included in the following part of the advice that assesses the situation of each non-EU country.

Increase of the competition within the asset management sector

164. Several respondents were of the view that any opening of the market to non EU providers and/or to non EU AIFs will increase competition especially where the NPPRs did not exist or were strict enough to prevent an easy market access. Furthermore, these respondents mentioned that as the AIFM and AIF passport will make very easy the marketing of non EU AIFs and/or EU AIFS managed by non EU AIFMs in all and every country of EU after one first registration, the competition would be increased.

165. These same respondents indicated that the impact is all the more sensitive that one of the features of asset management is to get important economies of scale; therefore the non EU passport which would give an advantage to big non EU players which would make use of it (of whatever type).

166. Several respondents outlined the fact that such an increase in competition would be in general positive for investors, because it would improve the need for efficiency of asset managers, and therefore the reduction of their fees.

167. Some respondents pointed out that competition between non–EU AIFM would also increase due to it becoming more realistic to market an AIF across Europe and this would be to the benefit of European institutional investors as these would be presented with a wider/ more complete set of investment opportunities.

168. However, other respondents were of the view that the provisions of the AIFMD are so burdensome compared to the local non-EU regulatory framework that it is unlikely non-EU managers would willingly subject themselves to AIFMD requirements unless doing business in the EU is unavoidable. These respondents were of the view that competition may increase slightly in NPPR jurisdictions where non-EU AIFMs/AIFs are currently absent, but they were of the view that the AIFMD itself imposes such onerous requirements that the impact of removing from this situation would likely be minimal.

Increase of investor choice

169. A large number respondents were of the view that one the main consequences of the potential extension of the AIFMD passport to non-EU AIF/AIFMs was that the range of possible investment opportunities for EU investors, more especially EU institutional investors, would be subsequently extended. Some respondents pointed out that it is often the case that these professional investors are pension funds or similar bodies that invest money received from EU retail customers.

Specific case of private equity AIFs

170. Some respondents mentioned that as private equity is concerned the competition aspect of the AIFMD passport could be more modest as private equity AIFM tend to

be geographically focused and the investment decision is to a large extent driven by sectorial or geographical investment considerations.

171. These respondents noted that in the private equity sector more specifically the larger funds rely more on international client bases and EU managers also need to fundraise in non EEA countries. Therefore some of these respondents would like to extend the passport to non-EU countries while maintaining a balance between the requirement of third country passport and the possibility for European AIF to fundraise in third country.

Issues raised in relation to the functioning of the potential non-EU AIFMD passport

172. Some respondents raised issues in relation with the functioning of the potential non-EU AIFMD passport. These issues are related to the existing issues in relation with the EU AIFMD passport (please see the related part of the Opinion on the functioning of the EU passport), namely the definition of "marketing" under the AIFMD requirements, etc. These issues are also related to determining of the 'Member State of reference'. The location of the depositary was one of the concerns mentioned. These respondents indicated that the determining of the 'Member State of reference' is potentially subject to change and uncertainty as the process of determining is complex, particularly where distribution is envisaged in several EU Member States.

173. Other respondents indicated that the extension of the passport to non-EU AIFMs should be accompanied by appropriate transitional and grandfathering provisions, particularly for funds which are already in the process of being marketed at the time of the implementation date for Article 37. Otherwise, the marketing process for such funds would need to be suspended in order to allow the AIFM to obtain authorisation or be terminated early (if the AIFM is unable or chooses not to become authorised)

174. As regards the OECD Model Tax Convention-compliant agreements, one respondent was of the view that ESMA should publish a table summarising which third countries have entered into OECD Model Tax Convention-compliant agreements with EEA Member States, and that they noted that there appear to be a number of Member States which have not entered into compliant Tax Information Exchange Agreements with important third countries, limiting the usefulness of the passport for third country fund managers, and continuing the existing fragmentation of the EU market.

Distinction between the extension of the passport to non-EU AIFs and non-EU AIFMs

175. Some respondents were of the view that the passport should be extended to non-EU AIFs, while it should not be in relation to non-EU AIFMs, because it would be unlikely anyway that a non-EU manager intends to comply with the different AIFMD requirements, especially those in relation with remuneration policy and depositaries. Given that an EU AIFM is subject to the full provisions of the Directive, these respondents were of the view that there seems little justification for the passport not being available in such circumstances. These respondents indicated that extending the passport to EU AIFMs marketing non-EU AIFs would benefit EU AIFMs by

enabling them to provide greater investment choice for EU investors and to access a wider investor base.

176. For historical reasons, one respondent indicated that the vast majority of the EU-managed hedge funds in existence today have been established in non-EU jurisdictions, principally the Cayman Islands. As a result, this respondent indicated that hedge funds are disproportionately underrepresented among the population of AIFs (especially when judged against the population of private equity funds and real estate funds) currently potentially available to EU investors as a result of the operation of the passport. Consequently, this respondent indicated that the availability (or not) of many AIFs managed by EU AIFMs is dependent on the availability and terms of NPPRs which vary substantially from Member State to Member State in respect of their conditions and ease of access and use.

177. These respondents also indicated that if the passport is extended to non-EU AIFMs, those AIFMs which utilise the passport will become authorised AIFMs for the purposes of other pieces of EU regulation, such as the European Market Infrastructure Regulation (EMIR) and many other existing and pending pieces of legislation, which contain detailed provisions on how third countries are to be dealt with. These respondents indicated that if a non-EU AIFM becomes an authorised AIFM within the context of such legislation, there will be instances where it becomes impossible for that AIFM to comply with all legislation that is applicable to it in its home jurisdiction and in the EU.

Detailed summary of the feedback

178. One respondent indicated that it anticipated that there could only be an extension of the passport to non-EU AIFMs if the full requirements of the AIFMD were imposed on AIFMs benefiting from this level of market access. This respondent was of the view that this has the potential to lead to significant market disruption if this was a precursor to switching off the NPPRs. Moving the regime in this direction would limit market access to only those AIFMs able to comply with the full AIFMD requirements. This would threaten to exclude non-EU AIFMs/AIFs where non-EU jurisdictions were not prepared to adopt the detailed requirements of AIFMD. This would potentially disrupt international capital market flows and raise precisely the same risks to EU markets and investors which were identified when the Directive was first debated.

179. This same respondent indicated that the NPPR represents a sensible compromise to avoid these problems. It allows full, passported access where the full requirements of the regime are imposed. It also allows individual Member States to allow access to their own jurisdictions for non-EU AIFs/AIFMs which do not apply the full rules. These Member States are able to set the standards imposed according to the needs of their national market. Article 42 explicitly provides that Member States may impose stricter rules than imposed by the NPPR if they wish.

180. This same respondent also mentioned that in the absence of a passport for non-EU AIFM, the AIFMD does allow a non-EU provider wanting ‘passported’ access to the

EU to establish an EU entity (and funds) to then benefit from cross-border market access. This requires the adoption of the full AIFMD rules, but accepting this trade-off is a matter for the provider's own commercial judgement.

181. Finally, this same respondent conclude that the current regime creates a balanced approach which, to date, has operated effectively, and that there is no pressing need to change the regime.

Another respondent indicated that in their view, the extension of the AIFM passport should be contingent upon the existence of a regulatory environment in the relevant non-EU jurisdiction which is broadly equivalent to the AIFM framework. Moreover, access to the EU Single Market on the passport basis should be granted only if the relevant third country allows marketing of EU AIFs into the national market subject to broadly equivalent conditions. They indicated that these elements of reciprocity should be deemed requisite because the eventual extension of the AIFM passport to non-EU AIFM will have significant implications on the competitive landscape of investment funds within Europe. Thus, an unconditional opening of the EU Single Market to third country providers should be avoided, since it could put EU AIFMs at a competitive disadvantage, particularly in case of lighter regulatory regimes outside the EU.

182. Against this background, this respondent greatly welcomed the announcement made by ESMA not to treat all non-EU countries as a single block. Indeed, we believe that ESMA should conduct individual assessments of non-EU jurisdictions and issue advice to the Commission on a country-by-country basis. Moreover, they would encourage ESMA and the Commission to perceive the upcoming review of the AIFMD passporting regime as an important opportunity to create or widen market access of EU AIFMs into non-EU countries that are yet not fully accessible from the European perspective.

183. In this context, this respondent was also of the view that it is important that the national private placement regimes do not automatically cease to exist once the AIFM passport is put into force in relation to certain third countries. This respondent believed that the evaluation procedure foreseen in Article 68 AIFMD should allow for sufficient flexibility to terminate the existing private placement regimes only in case these are being replaced by the passport rules for a specific non-EU jurisdiction. In other instances, the national frameworks for private placement should be allowed to remain in place for an indefinite time.

184. This respondent also mentioned that some its members have reported on their experience in several non-EU countries where the regulatory and tax environment present obstacles such as lengthy processes for authorisation, tax barriers, limited possibilities for direct distribution or other operational hindrances. These obstacles may result in a disadvantageous treatment of EU AIFM and UCITS managers compared to the AIFM from those countries in case the AIFM passport rules were to be extended.

185. Another respondent indicated that it believes that the only possible impacts of an eventual extension of the passport to non-EU AIFMs on competition would arise if such managers were given passport rights under less stringent requirements, and if such rights were granted to them without reciprocal opportunities for EU AIFMs to manage and market funds in those non-EU AIFMs' home countries.

186. This respondent supported the extension of the passport to non-EU AIFMs so long as there are equivalent regulatory oversight and investor protection measures that are designed to achieve the same goals as the AIFM Directive, leading to a level playing field for the managing and marketing of AIFs in the EU, regardless of the domicile of the manager or the fund. Reciprocal opportunities for EU AIFMs and AIFs are also a critically important pre-requirement to the extension of such rights insofar as opening the EU market to non-EU entities should not be a one-way street that they can take advantage of.

187. Another respondent indicated that the reasons for their quite wide footprint (40 companies in about 25 countries worldwide) are directly in relation with the questions ESMA is raising about the non-EU AIFMs or non-EU AIFs Passports. Basically, for regulatory reasons, they indicated they could not operate from Europe - in particular it would be impossible to manage funds from Europe, and it would be impossible in most cases to sell European Funds there; and it explains why they decided to establish (or buy) local subsidiaries in most of these non-EU countries. Therefore, this respondent was of the view that granting a Passport to non-EU asset managers where the counterpart markets would remain subject to the same regulations that today prohibit by law or in fact direct competition from European players would put them at competitive disadvantage.

188. This respondent also indicated that any opening of the market to non EU providers and/or to non EU AIFs will increase competition especially where the NPPRs did not exist or were strict enough to prevent an easy market access. Furthermore, this respondent mentioned that as the AIFM and AIF passport will make very easy the marketing of non EU AIFs and/or EU AIFS managed by non EU AIFMs in all and every country of EU after one first registration, the competition would be for sure increased.

189. This same respondent indicated that the impact is all the more sensitive that one of the features of asset management is to get important economies of scale; therefore the non EU passport which would give an advantage to big non EU players which would make use of it (of whatever type).

190. This respondent added that if, in addition, the regulatory constraints (linked to asset management regulation itself, but also to the depository- or custodian- one, to AML, taxation etc...) in a specific country are less important than in the EU, the competition would be unfair.

191. Finally, this respondent indicated that the same issue would appear if the market access is not in practice possible in some jurisdictions: the players operating in those

jurisdictions would benefit from size advantages whereas EU players would not be in a position to benefit from the same advantage.

192. This same respondent also mentioned that Europe in general – and in particular the European countries where this respondent operates as regulated asset managers (France, Belgium, Netherlands, Ireland , Lux, UK, Sweden, Finland, Italy)- has put in place a very comprehensive regulatory set of rules which, by far, differ from what is existing in most non-European countries, with perhaps the exception of the US, HK, Australia and Canada, even though in some areas –for example the depositary regime- the local framework is less protective for investors than what they know in Europe. In most countries, the level of requirements and the level of supervision is lacking behind Europe, not for everything, but for some aspects, leading to less compliance costs, allowing more leeway or more flexibility, if not taxation advantages.

193. Further detailing some if its views, this respondent indicated that the difficulties or limitations in establishing or marketing AIFs or UCITS in non-EU country is the main reason why they decided to establish asset management companies – alone or through JVs- in many non-European countries: India, China, Malaysia, Indonesia, Taiwan, Japan, South Korea, Mexico, Brazil, Argentina, Turkey, Morocco, Russia, Canada, and last but not least USA.

194. This respondent indicated that these markets are closed to non-local AIFs or UCITS – except if, in some countries like the US, the asset managers fully applies the US regulations and recognize they are subject to the US regulation and to the US regulator's supervision, including on-site inspections: in those situations, extraterritorial reach is the rule, which is a very different situation from what is contemplated by the EU regulation if a passport is granted to non EU AIFMS. Giving a passport to US AIFs or AIFMs would not oblige the US asset managers to fully apply the European legislation as this respondent indicated they are obliged to do if they want to establish or market funds in the US.

195. Another respondent indicated that the eventual extension of the passport to non-EU AIFMs will likely have a considerable impact on competition within the Union. In order to avoid that such an impact would put EU AIFMs in a possible disadvantageous position vis-à-vis some non-EU players, their view was that the assessment on the extension of the passport should be realized on the basis of an evaluation of the existence of equivalent regulatory, supervisory and enforcement conditions in the third country in question, which aim to equivalence of outcomes for both regulation and enforcement purposes. This respondent mentioned that such an assessment should be duly realized, in order to avoid that EU-AIFMs could suffer from competitive disadvantages, e.g. vis-à-vis cases of less strict regulatory regimes, and is highly welcome as it should be seized as an opportunity by ESMA and the Commission to improve those conditions which render market access to some non-EU markets still not broadly feasible for non-EU AIFMs.

196. Another respondent indicated that there are two aspects to be considered:

197. Competition of non-EU AIFM with EU AIFM: this respondent indicated that as far as private equity is concerned the competition aspect is modest as private equity AIFM tend to be geographically focused and the investment decision is to a large extent driven by sectorial or geographical investment considerations. I.e. whilst a US buy out fund competes for capital with a German buy out fund in theory, in practice this competition is less relevant as an investor would not commit to these from the same pool of capital (the one would come from a US allocation , the other from a European allocation);

198. Competition between non–EU AIFM. This respondent indicated this type of competition would increase due to it becoming more realistic to market an AIF across Europe and this would be to the benefit of European institutional investors as these would be presented with a wider/ more complete set of investment opportunities.

199. Another respondent, indicated that appropriate grandfathering and transition rules would be necessary as well as predictability around what constitutes "marketing" within the Member State of Reference. This respondent also expressed concern that ESMA not delay passport expansion while trying to resolve the international policy and complexity surrounding "tax compliant" regime determinations.

200. This respondent also indicated that there is no particular non-EU country where, as a consequence of the regulatory environment (financial regulation, supervision, tax and anti-money laundering provisions), an eventual extension of the AIFMD passport would put EU AIFMs and UCITS management companies at a disadvantage vis-a-vis the AIFMs from that country. This respondent indicated that the reverse may be true. This respondent mentioned that Non-EU funds have been freely able to solicit investment in most other countries except the EU and EU funds have been able to freely solicit investment in the non-EU jurisdictions. This respondent indicated that the EMPEA Guidelines setting out the key elements of legal and tax regimes optimal for the development of private equity have served as a framework in emerging economies. These guidelines address a number of the numerous types of laws, including those EVCA has cited in operation to protect investors:

a. laws governing the vehicle(s) used to establish the fund, such as limited partnership laws;

b. in some cases, local product regulation (although this is the exception not the rule);

c. tax laws applicable to investors and/or fund vehicles;

d. tax reporting or filing obligations e.g. FATCA and the Common Reporting Standard;

e. laws concerning permissible investments by investors e.g. CRD IV, Solvency II, the Volcker rule and ERISA;

f. laws concerning the preparation, audit and publication of accounts e.g. the EU Accounting Directive; and

g. laws concerning the prevention of financial crime including the identification of investors and sanctions laws.

201.This respondent agreed that the AIFMD seeks to normalise (and to an extent harmonise) certain limited aspects of the operation of alternative investment funds, including the fitness and propriety of the non-EU AIFM (and its staff), its governance, certain aspects of the conduct of its business and transparency towards regulators (for the purposes of systemic risk oversight) and investors. This respondent was of the opinion that it would be beyond the scope of ESMA's review to seek to understand the various laws that affect the competitive landscape relevant to the extension of the passport and, that ESMA's mission is best achieved by removing barriers to entry and competitive distortions created by the AIFMD and described in the preceding sections of this response.

202.This respondent further indicated that their Members noted that the extension of the passport to non-EU AIFMs could improve the situation by increasing competition and investor choice, particularly if it is introduced in an efficient, common-sense way. Certain Members also expressed concerns that the AIFMD is being applied in a manner that gives rise to WTO issues under the EU's obligations for financial services under the General Agreement on Trade in Services ("GATS"), both as to market access and possible licensing, among other issues:

a. <u>Experience with current NPPRs:</u> This respondent indicated that for non-EU AIFMs from emerging markets the current NPPR has proven onerous and burdensome with the result that in practice non-EU AIFMs are generally limited to only the largest AIFMs and EU Member States. As a result, the AIFMD has limited competition and investor choice in the EU. Among concerns expressed are the legal uncertainty created by the AIFMD's mechanism for selecting the Member State of Reference and the absence of clear grandfathering and transition rules. Without clear grandfathering and transition rules EU Member States can further restrict or even eliminate private placement regimes. In addition some Member States have delayed and incomplete transposition to the AIFMD and there are Member States where no formal memorandum of understanding is yet in place between such Member State and the legal domicile of a non-EU AIFM and there appears to be little willingness to enter into one;

b. <u>Cost and resource commitment</u>: This respondent mentioned that the already non-harmonious and ambiguous NPPRs give rise to costs that are amplified when considering the wide variety and changeability of existing and new "fee" structures imposed by multiple Member States on a single fund. Advisory and support costs such as legal and compliance do not decrease and fall disproportionately on the smaller non-EU AIFMs. Even after incurring substantial costs in an effort to comply, there is often surprising uncertainty about whether the non-EU AIFM has, in fact, complied because some regulators are unfamiliar with the new AIFMD rules and are reluctant to interpret them. While some larger AIFMs may take the view that this is simply a cost of doing business, this respondent was of the view that it raises a spectre of being a market barrier and is inconsistent with the EU's obligations under the GATS. This respondent indicated that these costs also raise questions of the potential for unintended discrimination against newer AIFMs from emerging markets, which do not have long-standing investor relationships within the EU and precludes them from becoming better known and playing on a level field.

c. Asymmetrical impact with regulatory regimes in other countries: This respondent was of the view that other countries' regulatory regimes do not disadvantage or delay the offering of EU-based AIFs in the same way as the AIFMD impacts non-EU AIFs. Generally, this respondent was of the view that EU funds experience a freedom to solicit investments in non-EU countries and this has an asymmetrical impact on the financial service provider of the non-EU countries, for example the costs and requirement for the use of depositories (which are not required in the non-EU jurisdictions), and raises questions of whether the EU intends to create additional restrictions, requirements and fees to create a market access barrier.

203. Another respondent indicated that an extension of the passport to non-EU AIFMs will have a positive impact on competition within the EU internal market for professional investors in the EU who are seeking to access the best investment strategies, wherever located globally, to facilitate their long-term saving and retirement goals. This respondent mentioned that competition benefits investors and encourages efficient and well-functioning markets and that the European Commission competition policy website itself states that "*competition puts businesses under constant pressure to offer the best possible range of goods at the best possible prices, because if they don't, consumers have the choice to buy elsewhere. In a free market, business should be a competitive game with consumers as the beneficiaries*." (http://ec.europa.eu/competition/consumers/what_en.html)

204. This respondent further indicated that creating a level playing field for non-EU AIFM to passport into Member States will benefit EU professional investor choice whilst encouraging greater internal market competition and efficiency and improved pricing for investors.

205. This respondent added that they would also support the extension of the marketing passport to managers currently marketing non-EU funds under Article 36 AIFMD. This respondent mentioned that EU AIFMs using Article 36 for the marketing of non-EU funds are complying with almost all of AIFMD already – the exception being the strict liability requirement for financial instruments held by depositaries. An extension of the passport in these circumstances would encourage greater on-shoring of asset

management services (AIFM, depositary and administration) with economic benefits for Member States in the form of job creation and taxation.

206.This same respondent was not aware of any particular non-EU countries where an extension of the passport would result in a disadvantage for EU AIFMs and UCITS management companies. As both a European and global asset manager, this respondent indicated they have direct experience of marketing EU managed AIFs and/or UCITS into a number of third countries, including *inter alia* Hong Kong, Singapore, Switzerland, Jersey, Japan and the United States. Similarly they have also successfully established local fund management presence in a range of third countries. This respondent indicated that their experience demonstrates that such third countries do not impose excessively heavy requirements or restrictions on European asset managers and this respondent considered such countries as already granting market access under broadly equivalent conditions.

207.This respondent also wanted to emphasise that in their view AIFMD Level 1 does not contain any requirement for or consideration of reciprocal marketing access for either EU AIFMS or UCITS as a condition to extending the marketing passport to any third country.

208.Finally, this respondent wondered why ESMA has expanded its collection of evidence to UCITS management companies, particularly as the experiences of UCITS management companies and their retail investor UCITS might not generally correspond to the experiences of managers of AIFs generally aimed at professional investors. This respondent indicated that indeed there are a number of third country jurisdictions which already permit the distribution of UCITS to both local retail and professional investors without any requirement for EU reciprocity.

209.Another respondent indicated that an extension of the passport to non-EU managers was premature. This respondent was of the view that ESMA and the European Commission should confer to the AIFMD the possibility to develop into a true “AIFMD” brand. Both managers and regulators in the EU need more time to ensure a smooth functioning of the passport. They saw no need to rush for an extension if reliable experience is missing, and it is difficult to estimate at this stage how long this will take.

210.This respondent was of the opinion that abolishing NPPRs is a prerequisite for an extension of the passport to third countries. A parallel system would cause market distortion by putting EU AIFMs at a clear disadvantage. If the passport was extended to third countries already in autumn 2015 as suggested by the AIFMD, this respondent indicated that non-EU managers would with regard to many countries have three options for a period of at least three years: (i) using the passport regime; (ii) operating on the basis of the respective NPPR; or (iii) setting up an EU AIFM which delegates functions to the non-EU manager. Considering that the requirements set by the AIFMD are usually more burdensome compared to what is required by NPPRs there would be already at this stage an unlevel playing field from a perspective of an EU AIFM. As a result, most non-EU managers would presumably not take the first option (passport regime). This respondent mentioned that they actually do not consider the passport advantageous compared to existing NPPRs. This respondent further indicated that if an EU AIFM managing/marketing an EU or non-EU AIF was required to fully comply with the AIFMD, the same would in their view have to apply on a compulsory basis to a non-EU manager managing/marketing an EU AIF or marketing a non-EU AIF within the EU.

211. This respondent added that even if the passport was only extended to selected countries that meet certain criteria in terms of market access and investor protection, ESMA and the European Commission should ensure that the passport regime and its consequences (e.g. stricter rules on remuneration) were not circumvented by the creation of a new entity in the non-EU country concerned that – contrary to other entities of the same group – complies with the AIFMD for the purposes of the group entities' EU business. Considering the country-by-country approach envisaged by ESMA, this respondent was of the view that it is also worth noting that NPPRs will presumably remain in force at least in those countries that are not selected for the passport. This result would again cause undesirable market distortion.

212. <u>Another respondent</u> indicated that in principle, it is anticipated that the eventual extension of a Passport to non-EU AIFMs will be beneficial to competition. Decreased marketing activity among non-EU AIFMs due to the lack of a Passport has been damaging to European investors, who feel the sharp decrease in deal flow and the narrowed choice in managers puts them at a competitive disadvantage to their peers outside of Europe. *"Our investment program is facing a critical challenge; we used to have 400 to 500 opportunities per annum in deal flow, of which half were from non-EU GPs but now this has literally gone away" "Deal flow is reduced and access to information is significantly delayed, which has led us to be too late in the fundraising process and missing out on funds." "Bigger [European] LPs can avoid this disadvantage by incorporating a subsidiary in USA but smaller [European] investors lack this opportunity."*

213. <u>Another respondent</u> indicated that with regards to the management/marketing of AIFs by non-EU AIFMs in the EU and the marketing of non-EU AIFs by EU AIFMs, they supported the extension of the current EU passport regime. In their view, it is important to ensure that the EU is open and accessible to non- EU AIFMs and non-EU AIFs as this allows EU investors to choose from a broader range of investment funds and investment strategies. However, they indicated that a level-playing field between EU and non- EU domiciled AIFMs needs to be maintained by thoroughly assessing and ensuring that the relevant third country jurisdictions meet the requirements as set out in the AIFMD and in the relevant Level 2 measures. They mentioned that these assessments should be aimed at ensuring appropriate levels of investor protection and at the same time not be misused to prevent non-EU AIFMs from accessing the EU internal market and benefiting of the EU passport.

214.Furthermore, this respondent wanted to express its concern with regards to the concept of the Member State of Reference ("MSoR") in the context of the third country passport and its possible impact on the depositary market. As set out in Article 21.5 AIFMD, they indicated that a non-EU AIF, upon securing a marketing passport, would be required to appoint a depositary located in its home jurisdiction, in the home Member State of the AIFM, or in the MSoR. This location requirement for the depositary, in their view, causes a number of concerns. Firstly, they mentioned that the MSoR is potentially subject to change and uncertainty as the process of determining the MSoR is complex, particularly where distribution is envisaged in several EU Member States. Due to the lack of a single determining factor on the MSoR, they indicated that national competent authorities must come to an agreement and in the absence of such agreement, ESMA is empowered to arbitrate on the decision. They mentioned that the MSoR can also change subject to distribution and management activities in theEU. Consequently, they concluded that the MSoR concept does not provide a reliable basis for the selection and appointment of a depositary. Further and most significantly, they indicated that a recognised selection of depositaries might not be available in the home Member State of the AIFM as the provision of depositary services is a highly specialised activity, carrying with it significant responsibilities and liabilities. They were of the view that many AIFMs will want to maintain the appointment of depositaries with whom they have existing relationships and are comfortable with from a due diligence perspective. They added that specialist AIF depositaries with the required capabilities are not established in all EU markets and it is entirely possible that the home Member State of the AIFM may not have access to relevant depositaries. Therefore they suggested that sufficient flexibility in relation to the location of the depositary is needed, ultimately by changing the relevant wording of Article 21.5 AIFMD and clarifying that the depositary can also be appointed in any Member State, so long as it meets the criteria in Article 21.3 of the Directive.

215.Another respondent indicated that the EU single market for funds was already very opened compared with the majority of external market. For example they indicated it is very easy to create a subsidiary in Europe and to sell funds that are, in fact, managed in other countries. They saw this state of play as a major disadvantage to EU asset managers compared for example to US asset managers. They were of the view that the extension of the passport to non-EU AIFMs would create further competitive disadvantage, particularly in cases of lighter regulatory regimes or much larger internal markets that allow economies of scale which are impossible in the EU. In this context they fully supported ESMA's approach to conduct their assessments for each individual non-EU country and to issue advice to the Commission on a country-by-country basis, taking into account the reciprocity in terms of market access.

216.This respondent also mentioned that most non-EU countries impose heavier requirements for foreign funds in comparison with what would be required from non-EU AIFMs to get access to the EU market.

217. Another respondent indicated that competition will increase, to the benefit of investors, certainly in terms of the breadth of products offered (i.e. increasing the opportunity set to choose from), and maybe also in terms of fees. This respondent was of the view that typically, in case of a small open economy, opening up borders to foreign competitors is welfare increasing domestically, even if implemented unilaterally. However, this respondent mentioned that in case of the EU, it appears worthwhile considering to open up only to AIFMs from those countries granting reciprocity and meeting equivalence standards.

218. This respondent further indicated that the risk in relation to 'market disruption' is that EU AIFMs do not have good enough AIFs as compared to their non-EU peers and, therefore, will be squeezed out of the market. If that was the case, we should let it happen to the benefit of investors. If, however, the offering of EU AIFMs meets client's needs, it is hard to see a reason for market disruption when extending the passport to non-EU AIFMs.

219. Another respondent indicated that they would expect the extension of the passport to non-EU AIFMs to increase competition without undermining the competitive position of EU AIFMs. In their view, potentially the passport will enable more non-EU AIFMs to market AIFs in Member States, therefore increasing the number of AIFMs in the market and increasing investors' global choice of AIFMs and AIFs.

220. Another respondent indicated that they believe that there would be limited impact on competition of the potential extension of the AIFMD passport. In their view, the Article 22(2) provisions are so detached from any reasonable oversight or investor protection function that few privately-held investment managers would willingly subject themselves to AIFMD requirements unless doing business in the EU is unavoidable. Competition may increase slightly in NPPR jurisdictions that now overtly discriminate against non-EU AIFMs, but the AIFMD itself imposes such onerous requirements that the impact of removing overt discrimination would likely be minimal.

221. Another respondent indicated that the eventual extension of the passport to non-EU AIFMs will have a positive impact on competition for investors in Member States seeking to invest their money. They mentioned that competition is good for investors. They added that according to the EU Commission competition web-site competition 'encourages companies to offer consumers goods and services at the most favourable terms. It encourages efficiency and innovation and reduces prices'. The 'financial markets are the lifeblood of the real economy, giving businesses and consumers access to financial products. The better and more competitively they function, the better the economy will perform'. This respondent was of the view that opening member states to competition from non-EU AIFMs would increase choice for professional investors, while driving all AIFMs to be more efficient, offering better services to investors.

222. This respondent added that there is also the aspect of the improved standards of investor protection, provided under the AIFMD by EU AIFMs, and required under the

passport for non-EU AIFMs. They would specifically support the activation of Article 36 passports. They mentioned that AIFMs making use of the current NPPR under Article 36 are already compliant with almost all the AIFMD requirements – only exempting strict liability for depositaries. They mentioned that such a move would encourage more on-shoring, e.g. if a firm launched an Asian AIF, they could use their EU AIFM then delegate to Asian portfolio managers. They mentioned that there would be numerous benefits for the member state (e.g. economic, jobs, taxation).

223. In relation to market access, this respondent indicated that were not aware of any such non-EU countries that imposes heavier requirements for EU AIFMs or UCITS management companies in comparison to those that non-EU AIFMs have to comply with in order to do business in the EU. Indeed, they mentioned they have many members who have found it worthwhile setting up and operating in a range of non-EU countries, e.g. USA, Switzerland, Jersey, Hong Kong, Singapore. In their view, this should demonstrate that those non-EU countries do not impose excessively heavy requirements on EU asset managers.

224. This respondent added that in their view, the legal text of the AIFMD does *not* authorise ESMA to consider reciprocity (notwithstanding Article 67(2)(c)) as a factor when preparing its advice to the Commission.

225. This respondent finally added that feedback from members indicates that (at least) the following countries grant market access: USA, Switzerland, Jersey, Hong Kong, Singapore, Cayman Islands. They indicated that they understand that most Asian countries have a workable NPPR.

226. <u>Another respondent</u> indicated that an eventual extension of the passport to non-EU AIFMs would increase the choice of fund products available to professional investors in the EU, and in turn likely promote competition and efficiencies within the European funds industry. They indicated that a third country passport could therefore have a positive overall impact, but only if applied and enforced correctly. They mentioned that it is critically important that measures be taken to ensure that non-EU AIFMs/ AIFs would be subject to a level of regulatory scrutiny (both during the authorisation process and on an ongoing basis) which is at least equal to that imposed on EU AIFMs/ AIFs, so as to safeguard a genuine level playing field between EU and non-EU jurisdictions. For example, they indicated that light-touch regulatory regimes in certain non-EU AIF domiciles facilitates the charging of lower initial and ongoing costs for the establishment and operation of AIFs in those domiciles. Failure to ensure that equal levels of regulation are applied to EU and non-EU AIFs which avail of the AIFMD passport could result in EU domiciles being undercut on price by non-EU domiciles, with a likely ensuing distortion of the market.

227. For that reason, they indicated they endorse ESMA's proposal in its Call for Evidence to consider the validity of extending the passport on a country-by-country basis, and in particular would encourage ESMA to take into account reciprocity of market access for EU AIFMs into each such non-EU country.

228. Another respondent indicated that_the extension of the passport to non-EU AIFMs should increase competition, since extending the passport to non-EU AIFMs will encourage more non-EU AIFMs to market AIFs to the benefit of the investors. They mentioned that NPPRs should be kept in place during any transition and Member State of Reference rules clarified.

229. Another respondent indicated that in principle the extension of the passport to non-EU AIFMs should increase competition by providing additional flexibility to non-EU AIFMs seeking to raise money from EU investors. However, this respondent indicated that if the passport is to work in the way in which it is intended, a more coherent approach is required which will only be achieved if the existing difficulties under the EU passport are addressed. Otherwise the full benefit of extending the passport is unlikely to be realised.

230. This respondent indicated that additionally, it will be important, in achieving this objective, for ESMA to develop draft regulatory technical standards under Article 37(23) of the Directive which take a proportionate approach to the manner in which non-EU AIFMs must comply with the requirements in the Directive, reflecting the fact that EU investors are likely to have a smaller overall participation in funds raised by non-EU AIFMs.

231. This respondent indicated that further, in order to avoid undue disruption to the fund raising processes of non-EU AIFMs, the extension of the passport to non-EU AIFMs should be accompanied by appropriate transitional and grandfathering provisions, particularly for funds which are already in the process of being marketed at the time of the implementation date for Article 37. Otherwise, the marketing process for such funds would need to be suspended in order to allow the AIFM to obtain authorisation or be terminated early (if the AIFM is unable or chooses not to become authorised); in either case this is likely to be disadvantageous to the AIFM and any EU or other investors who have been admitted to the fund prior to that time.

232. This respondent indicated that although they are of the view that the extension of the passport to non-EU AIFMs would be beneficial, they urge ESMA to consider carefully the very real risks of damage to investor choice if the AIFMD passport is made available to non-EU AIFMs and, post 2018, its use becomes mandatory so that the use of the NPPRs is no longer possible. This respondent indicated that the likely market reaction to this, particularly from non-EU AIFMs seeking to raise capital from EU investors in only a selected number of member states, would be a reduction in competition as a result of fewer AIFMs choosing to market in the EU on the basis that the burden of meeting the requirements of the whole Directive as an authorised AIFM in order to use the passport would be significantly more onerous than meeting the disclosure and transparency requirements specified in Article 42 under NPPRs. They therefore strongly recommended that use of the passport should be an option, not mandatory, for non-EU AIFMs and that use of the NPPRs should continue to be possible post 2018. In this way, this respondent indicated that competition and investor choice will be maximised since non-EU AIFMs whose proposed fund raising

from EU investors would not justify the burden of authorisation will nonetheless be able to continue to utilise NPPRs on a selected basis.

233. This respondent indicated that as a separate matter, regardless of whether or not the passport is extended to non-EU AIFMs, they are strongly of the view that the passport should be extended to EU AIFMs marketing non-EU AIFs. Given that an EU AIFM is subject to the full provisions of the Directive, there seems little justification for the passport not being available in such circumstances. This respondent indicated that extending the passport to EU AIFMs marketing non-EU AIFs would benefit EU AIFMs by enabling them to provide greater investment choice for EU investors and to access a wider investor base. Further, this respondent indicated that if NPPRs are retained for non-EU AIFMs once the passport regime is also made available, Article 36 NPPRs should also remain an option for EEA AIFMs marketing non-EEA AIFs in order that they may continue to have the option to market AIFs subject to the lighter depositary requirements and/or AIFs established in jurisdictions which may not have tax exchange agreements in place with the EU member states into which they are marketed. This respondent indicated that otherwise those EEA AIFMs will be disadvantaged relative to non-EU AIFMs by no longer being able to have access to the dual regime.

234. Another respondent indicated indicated that to the extent that relevant third countries have adopted equivalent requirements and which are designed to achieve the goals of the AIFMD, then such extension would, subject to a workable application of Article 40 of the AIFMD, and combined with reciprocity for EU AIFMs and AIFs, lead to a positive impact on competition within the EU. This respondent indicated that this will also tend to lead to EU investors gaining access to a greater range of asset management opportunities.

235. This respondent considered that in order to maximise market stability and ensure effective competition, it will be necessary to rely upon the continued use of NPPRs in parallel with the introduction of third country passporting regimes.

236. Another respondent indicated that as noted by a recent Preqin study (The full text of the Preqin report is available at: https://www.preqin.com/docs/reports/Preqin-Special-Report-Hedge-Fund-Managers-Respond-to-AIFMD-July-14.pdf), a significant majority of non-EU managers do not intend to market to EU investors under national private placement regimes or establish an EU AIFM to take advantage of the AIFMD passport. Consistent with those survey results, they have heard anecdotally from their members that there is not significant interest from non-EU managers in becoming fully authorised AIFMs if the EU extended the AIFMD passport to non-EU managers.

237. In light of the remaining uncertainty and other concerns non-EU managers have with respect to the AIFMD, and the likelihood that many non-EU managers will not seek to market to EU investors under the passport, this respondent encouraged policy makers conduct a longer review period before making any recommendations on the functioning of the private placement and passport regimes, to better ensure there is

sufficient information on which to base such recommendations. They also encouraged EU and non-EU regulators and policy makers to continue to harmonize their regulatory requirements for managers and to facilitate compliance by deeming managers that comply with their home jurisdiction rules to be in compliance with similar rules in other jurisdictions; provided that the rules are designed to achieve equivalent outcomes. While they recognized that such an approach involves significant challenges for regulators, they believed that this approach to hedge fund manager regulation and oversight will best accomplish the policy goals of regulating managers and encouraging private capital participation in capital markets across borders.

238. Another respondent indicated that in relation to Art 35 of the AIFMD, it supports the extension of the passport to be applicable to non-EU AIFs managed by EU AIFMs. This respondent indicated that it represents members whose assets under management represent approximately 70% of the total hedge fund assets under management across Europe. For historical reasons, the vast majority of the EU-managed hedge funds in existence today have been established in non-EU jurisdictions, principally the Cayman Islands. As a result, this respondent indicated that hedge funds are disproportionately underrepresented among the population of AIFs (especially when judged against the population of private equity funds and real estate funds) currently potentially available to EU investors as a result of the operation of the passport. Consequently, this respondent indicated that the availability (or not) of many AIFs managed by EU AIFMs is dependent on the availability and terms of NPPRs which vary substantially from Member State to Member State in respect of their conditions and ease of access and use.

239. This respondent indicated that the implementation of Article 35 to allow EU AIFMs to market the non-EU AIFs they manage via a passport rather than having to rely on various Member State NPPRs will significantly reduce operational complexity and legal costs. Moreover, this respondent indicated that fully authorised EU AIFMs are already complying with the requirements of the AIFMD and the marginal additional cost of a full depositary service is not expected to outweigh the expected benefits. They believed that there are not any significant obstacles to the ability of Member States to regulate EU AIFMs with regard to the non-EU AIFs they manage. This respondent indicated that the competent authorities in major non-EU hedge fund jurisdictions (such as the Cayman Islands) are more than willing and able to cooperate with EU national competent authorities to the fullest extent necessary to ensure full implementation of the Directive. Finally, and most importantly, this respondent indicated that permitting EU AIFMs to use the passport to market their non-EU AIFs will substantially increase EU investor choice for AIFs pursuing hedge fund strategies. With respect to the operation of the internal EU passport, however, they believed that changes should be made to discontinue any existing fees or additional requirements being imposed as part of the passporting process and foreclose Member States from making any new requirements for fees or additional requirements for use of the passport, including, but not limited to, any fees or requirements that would apply differentially based on the home jurisdiction of the AIF.

240. In relation to Art 37-41, this respondent indicated that they also support the implementation of AIFMD Articles 37-41 to make the option of a passport available to non-EU AIFMs. However, they indicated that they acknowledged that the extension of the passport to non-EU AIFMs presents more difficulties than the extension of the passport to EU AIFMs of non-EU AIFs. In particular, this respondent indicated that if the passport is extended to non-EU AIFMs, those AIFMs which utilise the passport will become authorised AIFMs for the purposes of other pieces of EU regulation, such as the European Market Infrastructure Regulation (EMIR) and many other existing and pending pieces of legislation, which already contain detailed provisions on how third countries are to be dealt with. This respondent indicated that if a non-EU AIFM becomes an authorised AIFM within the context of such legislation, there will be instances where it becomes impossible for that AIFM to comply with all legislation that is applicable to it in its home jurisdiction and in the EU. In such instances, this respondent indicated that the provisions on the conflicts of laws that are present in Article 37(1) of the AIFMD would not be sufficient to address conflicts of laws which arise by virtue of 'authorised AIFMs' being included in the scope of other pieces of EU financial services law.

241. In addition, this respondent indicated that when the passport is extended to non-EU AIFMs, they would request that ESMA and the European Commission (Commission), in the context of the review under Article 67 of the AIFMD, consider the following suggestions in order to render the regime workable: i) Restrict the ability of individual Member States to impose additional requirements or fees in connection with the use of the passport, especially any such requirements or fees that would vary based on the home jurisdiction of the AIFM or the AIF concerned; ii) Construe the impossibility test in Article 37(1)(a) and the equivalence test in Article 37(1)(b) broadly and permit any AIFM that cannot market via the passport by reason of the test in Article 37 to continue to be able to access EU investors through an NPPR; and iii) If ESMA determines to extend the passport on a country-by-country basis, leave the NPPRs available for AIFs and AIFMs from any jurisdiction to which the passport has not been extended and adopt a clear methodology for the consideration in future of the extension of the passport to any such jurisdictions.

242. This respondent indicated that ideally, they would like to see Articles 37-41 implemented and the impossibility and equivalence tests construed broadly, focussing on outcomes rather than particular requirements. However, this respondent indicated that many consider that, to date, there has not been enough experience with the operation of the Directive in any Member State that might be a Member State of reference for a non-EU AIFM for people to make a full assessment of what aspects of third country laws are likely to impose an impossibility of the type contemplated in Article 37(1)(a) or to judge the likely outcome of an equivalence finding as contemplated by Article 37(1)(b).Given the current lack of experience with the operation of the AIFMD in practice, this respondent indicated that ESMA may consider delaying any determination about the extension of the passporting mechanism to third country AIFs. However, rather than delaying the implementation of Article 35 as well as Articles 37-41, they would suggest that ESMA consider

suggesting that the Commission proceed with setting a date for the implementation of Article 35 (assuming ESMA was otherwise going to provide a favourable opinion and advice to this effect anyway) but that it not proceed at this time with setting a date for the implementation of Articles 37-41, instead setting a date for further consideration of the topic in the future.

243. This respondent indicated that Article 67 requires the Commission to specify a date for Articles 35 and 37-41 of the AIFMD to become applicable but the provision need not be read to require that all of the relevant Articles would become applicable on the same date. This respondent indicated that the implementation of Article 35 to allow EU AIFMs to market the non-EU AIFs they manage via a passport rather than having to rely on various Member State NPPRs will significantly reduce operational complexity and legal costs arising because of the divergences among Members States in the availability of and requirements for NPPRs and the additional cost of a full depositary service is not expected to outweigh the expected benefits. This respondent indicated that Article 67 can be read to allow a date to be set for the applicability of Article 35 and a different date to be set for the applicability of Articles 37-41. They would therefore suggest that it would be prudent to set an earlier date for the applicability of Article 35 and to review the functioning of the passport and the possible extension to non-EU AIFMs in 2017 when the review of the Directive envisaged in Article 69 is undertaken.

244. This respondent indicated that either or both of the above suggestions would allow time for all of the entities involved (non-EU AIFMs, third country competent authorities, EU national competent authorities, ESMA and the Commission) to gain further experience with the operation of the Directive in various Member States and the operation of the various cooperation arrangements. They requested that ESMA confirm their understanding that the natural extension of this outcome would be that the three year period contemplated by Article 68 would not start to run at the date of the implementation of Article 35 alone, as Article 68 refers to Articles 35 and Articles 37-41 having become applicable in all Member States in the conjunctive. Thus this respondent indicated that if Article 35 has become applicable but Articles 37-41 have not, the three year period cannot begin. This respondent indicated that in the event that ESMA determines to consider the extension of the passport on a country by country basis as part of its advice, they would welcome ESMA making it clear what the procedure would be going forward for having additional countries approved and granted access to the passport. They would also welcome ESMA's confirmation that, if the passport is made available to AIFMs or AIFs from some non-EU jurisdictions but not others, the three year period in Article 68 would not start with respect to AIFMs or AIFs from any jurisdiction where the passport has not been made available and that the NPPRs would not be required to be discontinued with respect to any AIFMs or AIFs from any such jurisdictions unless and until the passport is made available to AIFMs and AIFs from such jurisdictions.

245. This respondent further indicated that they support the implementation of Articles 37-41 AIFMD to make the option of a passport available to non-EU AIFMs. However,

they also believed that the NPPRs should continue to remain available (and should not be shut down as contemplated in Article 68) to accommodate any non-EU AIFMs that are not able to utilise the passport as a result of the passport not being turned on with respect to the AIFM's home jurisdiction or as a result of the operation of the requirements in Article 37(2), especially if the impossibility and equivalence requirements are to be construed narrowly.

246. Another respondent indicated that they would like to mention a few figures confirming the importance of international fundraising for Private Equity and Venture Capital funds. The European Private Equity and Venture Capital, has experimented a dangerous contraction of its resources over the last five years, synonymous with short-term weakening of the own funds of SMEs.

247. This respondent further indicated that new regulatory requirements (Basel III and Solvency II) leave fear of a dangerous evolution both in direct funding of SMEs and in the allocation of assets destined of Private Equity and Venture Capital. They observed the withdrawal of some institutional investors (French Insurance companies and banks.

248. This respondent further indicated that they observe that the larger funds rely more on international client bases. For example, in 2013, the average size of vehicles having raising funds exclusively in France represented 23 M€, while the vehicles having raised funds in France, in Europe and outside of Europe presented an average size of 344 M€. Key figures demonstrate that significant-size funds involve raising funds on an international level. Opening up to the international level is therefore an issue for European private equity and venture capital industry.

249. In one hand, this respondent indicated that they need to fundraise in non EEA countries. This issue is fundamental to ensuring the development of private equity and venture capital significant-sized funds in Europe. They would like to maintain a balance between the requirement of third country passport and the possibility for European AIF to fundraise in third country. At this stage, this respondent indicated that they do not know what will be the consequences of the introduction of third country passport on the local legislation of non EEA countries.

250. On the other hand, this respondent indicated that some regional initiatives, particularly in Asia for passport proposals (i.e. Asia Funds Region Passport and ASEAN Proposal) are encouraged. Those initiatives will have an impact on competition that we cannot estimate.

251. For these reasons, this respondent would like to share with ESMA a pragmatic approach which acknowledges the realities of marketing of closed-ended AIF to international professional investors. In this approach, they also took into account similar AIFMD rules introduced by third country concerned. This respondent indicated that they identified three groups of third countries as described below:

a. First group: Implementation of third country passport. This group includes countries which have implemented AIFMD in their jurisdiction. The third countries concerned are mainly Switzerland and the Channel Islands (Jersey and Guernsey) with whom they have significant trade, economic exchanges or partnership relations. Those countries made an effort to adopt the AIFMD legislation in their national legal system. They believed this is important to promote their approach. This is the reason why this respondent supported for those third countries the implementation of third country passport in accordance with AIFMD on the basis of equivalent rules.

b. Second group: "*status quo*" approach. This group includes countries which have not implemented AIFMD in their jurisdiction but have developed on another basis a strong legislation on marketing. The third countries concerned are mainly USA, Canada and Singapore. This respondent indicated that they hope to implement the marketing passport in these jurisdictions one day but they believe that it is too early for this. All these countries have adopted a NPPR and are not ready yet to implement a legislation based on the same approach of AIFMD.

c. Third group: high level of barriers to market AIFs. This respondent indicated that this group includes third countries which have adopted highly protective regulations in terms of AIFs marketing. Some third countries have implemented rules which are difficult to apply for foreign managers to market AIF in their territory. The implementation of third country passport would be harmful. This respondent indicated that they identified Gulf countries.

252. Another respondent indicated that extension of the passport to non-EU AIFMs should, in theory increase competition. This respondent indicated that the passport will enable more non-EU AIFMs the ability to market AIFs in the EU, therefore increasing the number of AIFMs in the market and increasing investors choice of AIFMs and AIFs. This respondent indicated that the benefits of extending the passport to non-EU AIFMs would be maximised by addressing the current teething issues that have been experienced with the issuance of EU AIFM passports and ensuring that the passport regime is tailored to the specific circumstances of non EU AIFMs. This respondent indicated that in order to continue to provide market stability and to create effective increased competition the continuation of NPPRs in parallel to third country passport will be required.

253. Another respondent indicated that the answer to this question of the impact on competition of the potential extension of the AIFMD passport depends to a large extent on the manner in which the passport is extended to non-EEA AIFMs and whether and if so how Member States revise existing rules regarding marketing by non-EEA AIFMs without the passport.

254. This respondent indicated that in principle, extension of the passport to non-EEA AIFMs (while keeping in place national private placement regimes) should increase competition, since extending the passport to non-EEA AIFMs should encourage more non-EEA AIFMs to market interests in the AIFs they manage in more Member States than they would otherwise do. This respondent indicated that this development would be very welcome, since EU investors would benefit from more investment options and the AIFMs' cost savings realized by using the passport. This respondent indicated that the benefits of extending the passport to non-EEA AIFMs could be undermined, however, unless ESMA and the Commission: i) address problems that have emerged with the passport for EEA AIFMs; ii) take an efficient, common-sense (and tailored) approach to the special/specific requirements that will apply only to non-EEA AIFMs; and/or iii) clarify how certain AIFMD provisions whose full application to non-EEA AIFMs with a small proportion of EEA investors (e.g., those relating to remuneration and capital) would be disproportionate should apply to non-EEA AIFMs making use of the passport.

255. This respondent indicated that the benefits of extending the passport to non-EEA AIFMs would also be undermined if and to the extent Member States that currently allow non-EEA AIFMs to market AIF interests without the passport restrict or eliminate this possibility upon extension of the passport to non-EEA AIFMs. This respondent indicated that the result of such a restriction or elimination would be to reduce competition, especially if the problems discussed below are not solved. This is the case because some non-EEA AIFMs only market in one or two EU countries and such managers are likely to stop marketing their product in those countries if they had to go through the whole EU AIFMD process which would be too costly and not efficient given they had only a few investors in Europe and they are already subject to supervision in their home country.

256. Specifically in relation to non-EEA AIFMs, this respondent indicated that has identified four main issues that will need to be addressed for the passport to work as intended: appropriate grandfathering/transition rules; determination of the Member State of reference; the requirement for OECD model tax convention-compliant agreements; and the requirement for guidance on proportionate application of certain AIFMD provisions to non-EEA AIFMs. Each of these issues is discussed in more detail below.

257. *Appropriate Grandfathering / Transition Rules.* Articles 37 and 41 set out the requirements under which a non-EAE AIFM can manage an EEA AIF under the passport regime. This respondent indicated that it is crucial that appropriate grandfathering rules be in place if the passport is introduced for non-EEA AIFMs. For example, a transition rule will be required for funds which were marketed already prior to the introduction of the passport. This respondent indicated that as long as an AIFM has started marketing an AIF before the passport was introduced, it should be able to continue to market that fund until it has its final closing (which can sometimes be more than a year after first close). For example, such a transition rule could foresee that for two years after the introduction of the passport, any AIFs which were

marketed already prior to such date can continue to be marketed under the old rules until the expiration of this two-year period. This respondent indicated that this would mirror the transitional provisions under Article 61(1) when the AIFMD started to apply in July 2013.

258. This respondent indicated that a transitional provision is important for closed-ended funds such as private equity funds because, in the current market, it can sometimes even take between 18 to 24 months from the start of marketing (in the non-AIFMD sense) to reach final close. Without an appropriate transitional rule this respondent indicated that these non-EEA AIFMs are under pressure to finish their closing before the passport is introduced as they would otherwise have to interrupt their fundraising process until they have obtained the passport.

259. *Determination of Member State of Reference.* Another area of specific relevance to non-EEA AIFMs is the mechanism for designating a Member State of reference. This respondent indicated that the AIFMD and the Level 2 measures adopted so far do not provide a reasonable level of legal certainty where a non-EEA AIFM intends to market AIF interests in multiple Member States. In practice, this respondent indicated that any third country manager wishing to commit to the EU market and obtain authorisation is sure to want to market in more than one EU Member State. According to Article 37 AIFMD, this respondent indicated that the determination of Member State of Reference in many circumstances is linked to the concept of "effective marketing", i.e. the Member State of Reference is one of the Member States where the AIFM intends to develop effective marketing. This respondent indicated that it is important that regulatory authorities apply a reasonable and predictable approach in relation to the interpretation of that concept and, in particular, that they should respect the decision of a particular competent authority in the Member State of Reference to authorise the AIFM. This respondent indicated that since the AIFMD is a maximum harmonization measure, supported by the European Commission Delegated Regulation with direct effect and directly binding Regulatory Technical Standards and Implementing Technical Standards and which provides for very limited Member State discretion, there is no risk of regulatory arbitrage.

260. This respondent indicated that that ESMA needs to develop simple and practical criteria for determining when there is deemed to be an "intention to develop effective marketing" in a Member State, especially in those cases where a non-EEA AIFM intends to market interests in one or more non-EEA AIFs in several or even all Member States (Article 37(4)(f) and (h) AIFMD). This respondent indicated that a fund management group will often already have some EU entities and personnel even if they are not responsible for AIF portfolio management or risk management. For example, a PE/VC fund management group may:

(a) have one or more EU-headquartered portfolio companies or an investment strategy focusing on certain countries or regions;

(b) typically use, to organise its holdings, special purpose acquisition vehicles in an EU Member State; or

(c) have an affiliate providing advisory and transaction arrangement services to the non-EEA AIFM or AIF. These factors should be taken into account when confirming that the intention to develop effective marketing in a particular Member State exists.

261. This respondent indicated that furthermore, the procedures should also expressly recognize the possibility for an AIFM to request a change in its Member State of Reference, which may be appropriate for instance where the AIFM's marketing or investment strategy has evolved since the original request (as already contemplated in Article 37 AIFMD). On the other hand, this respondent indicated that the non-EEA AIFM should not be required to change its Member State of Reference because the criterion which was relevant for determining the Member State of Reference changes or does not pan out as expected (for example, if few or no prospective investors in the Member State of Reference ultimately decide to invest); This respondent indicated that ESMA should provide specific guidance clarifying that this should not be viewed as a 'change in marketing strategy' for the purposes of paragraph 11(a) of Article 37.

262. *Requirement for OECD Model Tax Convention-compliant agreements*. Several Articles of the Directive concerning non-EEA AIFMs and AIFs require that there should be in place between third countries and EU Member States OECD Model Tax Convention-compliant agreements. Examples include Article 35(2)(c) and Article 37(7)(f). This respondent indicated that it is important that as soon as possible ESMA collate and publish a table summarising which third countries have – in their view - entered into OECD Model Tax Convention-compliant agreements with EEA Member States, in much the same way as ESMA helpfully published the matrix of supervisory cooperation arrangements for the purposes of Articles 42 and 36. Alternatively, this respondent is aware of a list of agreements at http://eoi-tax.org/; this respondent indicated that ESMA could confirm that it regards this as an authoritative list. However, this respondent indicated that not all agreements listed on that website have been reviewed for OECD compliance, so the list is not a complete one and ESMA would need to supplement it. This respondent indicated that they also note that there appear to be a number of Member States which have not entered into compliant Tax Information Exchange Agreements with important third countries, limiting the usefulness of the passport for third country fund managers, and continues the existing fragmentation of the EU market.

263. *Requirement for guidance on proportionate application of certain AIFMD provisions to non-EEA AIFMs.* Even before the introduction of the AIFMD, EEA investors represented a small proportion of the investors in most global funds. This respondent indicated that the obstacles created by the NPPRs discussed above have likely reduced the proportion of EEA investors still further. This respondent indicated that the extension of the passport to non-EEA AIFMs has the potential to increase competition and investor choice if done in an effective way. However, this respondent

indicated that full application of certain AIFMD provisions that diverge significantly from global regulatory norms – in particular those relating to remuneration and capital requirements – would be disproportionate. This respondent indicated that ESMA and the European Commission have stressed in their delegated regulations and guidance under the AIFMD that the AIFMD should be applied in a proportionate, tailored way. This respondent submitted that this principle should also apply to the application of the AIFMD to non-EEA AIFMs in the event the passport is extended to them and we invite ESMA to provide guidance on these points. Otherwise, this respondent indicated that global AIFMs will be unlikely to make use of the AIFMD passport and EEA investors will continue to suffer from reduced competition and choice.

264. This respondent finally indicated that it is important that ESMA should keep in mind that most of the main international financial centres now operate in accordance with common international protocols and there are numerous types of laws (regulatory requirements and tax provisions across jurisdictions) relevant to the establishment, marketing and operation of private equity and venture capital funds. Such laws include: i) laws governing the vehicle(s) used to establish the fund, such as limited partnership laws; ii) tax laws applicable to investors and/or fund vehicles; iii) tax reporting or filing obligations e.g. FATCA and the Common Reporting Standard; iv) laws concerning permissible investments by investors e.g. CRD IV, Solvency II, the Volcker rule and ERISA v) laws concerning the preparation, audit and publication of accounts e.g. the EU Accounting Directive; vi) laws concerning the prevention of financial crime including the identification of investors and sanctions laws vii) in some cases, local product regulation (although this is the exception not the rule).

265. In their view, this respondent indicated that it would be beyond the scope of ESMA's review to seek to understand the various laws which affect the competitive landscape relevant to the extension of the passport. For reasons given elsewhere, they believed that ESMA should focus instead on removing barriers to entry and competitive distortions created by the AIFMD and described in the preceding sections of this response.

266. <u>Another respondent</u> indicated that obviously the eventual extension of the passport to non-EU AIFMs would increase competition. But this respondent was of the view that this competition might not be a fair competition: i) Because the sets of rules might not be the same in the relevant third countries and in the EU, and might therefore be less demanding and costly to comply with; ii) Because the enforcement of the sets of rules might be less stringent in third countries than in the EU iii) Because reciprocal market access would not be granted.

267. This respondent therefore welcomed ESMA's suggested approach to conduct their assessments for each individual non-EU country and to issue advice to the Commission on a country-by-country basis. In order to create a level playing field in terms of market access, they would encourage ESMA and the Commission to see the current exercise as a significant opportunity to create further market access for EU

AIFMs into non-EU countries that are not yet accessible from a European perspective.

268. This respondent indicated that regarding specifically the regulation of AIFMs and AIFs, the regulations may be weaker in some third countries on some points:

a. For instance in the US, this respondent indicated that investment advisers (acting in a way similar to asset management companies) may self-custody the assets they manage – and this possibility is still offered after the Madoff case. This respondent indicated that This flexibility generates lower costs for local players (and also a lower protection for investors) as compared to the mandatory use of an external depositary;

2. this respondent indicated that a second example relates to the segregation of fund assets: many third countries do not require a segregation of fund assets as compared to the rest of clients' assets;

3. this respondent indicated that a third example relates to the monitoring function ensured by the AIF depositary, which is not required from the custodian in most of third countries;

4. this respondent indicated that a fourth example might relate to remuneration: if remuneration rules are more flexible for asset managers in third countries than in the EU, it will give a competitive advantage to non-EU players;

5. this respondent indicated that regarding specifically pure domiciliation centres, some of them out of the EU may offer more flexible rules as compared to EU rules, in particular as they don't have local investors or markets to protect.

6. this respondent indicated that beyond the area of financial regulation as such, an advantage might be given to third countries which are less stringent than the EU regarding banking secrecy, taxation or anti-money laundering (FATF) rules: if the level of requirements or the less stringent enforcement of rules in third countries is lower than in the EU, it will generate lower compliance costs and therefore will give a competitive advantage for the players and products based in these third countries as compared to those based in the EU.

269. This respondent indicated that to sum it up, it will be crucial that regarding the assessment of third countries, ESMA takes into account not only financial regulation as such but more widely all the pieces of third country legislation – and their actual enforcement – before concluding on delivering or not an EU passport to such third countries.

270. This respondent concluded by saying that very often, the main deterrent for establishing or marketing EU funds in third countries is the requirement to comply with the whole set of local rules: in the vast majority of third countries, mutual recognition does not apply and therefore a European player would have to comply with the local rules (including local tax rules, such as FATCA) in addition to its own home rules – making the cost to entry too high, and thus deterring it to enter the market. This respondent added that as a result, only the biggest EU players have the financial means to buy local firms or to launch local subsidiaries, managing local funds sold to local investors.

271. This respondent was of the view that some countries are open, such as Singapore or Chile. But even in the most open countries, while it is usually possible to sell foreign funds, it is usually very difficult to manage local funds from abroad – the equivalent of the EU 'Management Company Passport'.

272. Another respondent indicated that their members are of the opinion that the extension of the passport to non-EU AIFMs will certainly have substantial implications on the competitive landscape of (alternative) investment funds within Europe. This respondent indicated that an unrestrictive opening of the EU single market could put EU-AIFMs at a competitive disadvantage, particularly in cases of comparatively light(er) regulatory regimes or much larger internal markets that could create important economies of scale that cannot be achieved by smaller players in the EU.

273. In order to avoid such a situation, this respondent believed that an extension of the AIFMD passport should be subject to an assessment of the regulatory, supervisory and enforcement framework in the third country in question which should aim for equivalence of outcome in terms of regulatory environment. Many of their members see this as a significant possibility to create further market access for EU AIFMs into non-EU countries that are not yet broadly accessible from a European perspective and therefore would encourage ESMA and the Commission to make use of this opportunity. Under such circumstances they were of the view that an extension will benefit European professional investors' choice while encouraging enhanced competition and market efficiency. They therefore welcome and support ESMA's suggested approach (paragraph 7) to conduct their assessments for each individual non-EU country and to issue advice to the Commission on a country-by-country basis.

274. In this context, this respondent indicated that it is also important to ensure that the national private placement regimes do not automatically cease to exist once the AIFM passport is put into force in relation to certain third countries. They believed that the evaluation procedure foreseen in Article 68 AIFMD should allow for sufficient flexibility to terminate the existing private placement regimes only in case these are being replaced by the workable passport rules for a specific non-EU jurisdiction and after an appropriate transitional period. In other instances, this respondent was of the view that the national frameworks for private placement should be allowed to remain in place for an indefinite time

B. **Investor protection and the monitoring of systemic risk**

Overall summary of the feedback

275. In addition to the comments made by the respondents in the previous part dedicated to the impact on competition and market disruption of the potential extension of the AIFMD passport to non-EU countries, the respondents further outlined the following points:

Enforcement of the AIFMD requirements for non-EU countries

276. Several respondents were of the view that that it is more difficult for local EU Regulators to enforce and oversee entities outside of their jurisdiction. No respondent has been able to demonstrate past examples of such an extension cooperation that will be required under the requirements of the AIFMD passport for non-EU countries.

277. However, other respondents were of the view that the regulatory frameworks of some non-EU countries were as stringent as the AIFMD one, even if framed in a different way. These respondents were of the view that it was not that important that the exact AIFMD requirements are enforced in these non-EU countries.

Increase of Investors' choices

278. Several respondents pointed out that the impact on investor protection of the potential extension of the passport to non-EU countries should include its impact on investor' choices. Indeed those respondents were of the view that EU investment institutions are experiencing limited investor choice and access to high quality investment options as non-AIFMs severely limit their efforts to raise capital in Europe and concentrate their efforts elsewhere. These respondents mentioned that this is not only the case for the strongest performing and established asset managers who have the greatest choice as to whether and where to raise capital, but also for younger, high performing managers. In that context the consequence would be a limitation on the EU investment institutions' ability to diversify their investment portfolios by accessing emerging market investment opportunities and obtain their target returns. This, in turn, would impact both risk and return expectations over the near, medium and long terms with the final result limiting not only returns to, for example, occupational pension holders.

279. However, other respondents indicated that for the same reasons the regulatory framework of non-EU countries should be very strictly assessed in relation to its comparability with the AIFMD regulatory framework.

Reporting

280. Some respondents indicated that one positive benefit, for both regulators and non-EU AIFs making use of the passport would be the need only to report to the Member State of Reference. This would result in considerably less duplicate reporting for AIFMs, and fewer reports being received by regulators, which would increase the efficiency of the general regulatory framework.

Depositaries

281. Some respondents mentioned that requiring the depositary to be located outside the EU is a higher risk approach. These respondents do not regard this as an optimal outcome from an investor protection perspective, as it is not immediately apparent that all non-EU jurisdictions would have the appropriate legal and regulatory framework or developed depositary business with the specialised expertise, infrastructure, resources and capacity to carry out depositary duties to AIFMD standards. The appointment of a depositary located outside the EU could in some cases create an unnecessary divergence of depositary eligibility and present greater risks for investors.

Systemic risk

282. Some respondents indicated that in terms of systemic risk, allowing the passport to third countries might lead to an import of additional systemic risk in the EU if the home non-EU countries do not master properly the potential systemic risks generated by the AIFMs and the AIFs domiciled in their jurisdictions – either by having less stringent rules and/or by having less stringent enforcement of their rules than in the EU.

Detailed summary of the feedback

283. A respondent indicated that they were of the view that an extension of the AIFM passport should require the existence of a broadly equivalent regulatory environment in the relevant third country. In this context, equivalence of regulation should mean equivalence of outcomes, in particular regarding investor protection and market integrity/stability. Another aspect to be considered in terms of equivalence is the effective enforcement of the legal framework in the non-EU jurisdiction.

284. This respondent added that the current Level 1 text of AIFMD already encompasses provisions which aim at safeguarding the EU standards of investor protection in relation to the provision of services by non-EU AIFMs. This pertains in particular to Article 37 AIFMD (authorisation in the Member State of Reference) which requires general compliance with the AIFMD in para. 2 and imposes further conditions on the authorisation in para. 7. These conditions include the existence of appropriate cooperation arrangements between the involved EU and non-EU authorities which ensure at least an efficient exchange of relevant information. This respondent emphasized that such mechanisms for closer cooperation between EU and non-EU authorities are essential for warranting effective supervision and thus ensuring augmented investor protection.

285. In addition, this respondent believed that the possibility of investors to initiate proceedings before EU courts in order to obtain compensation for damages which have occurred at the fund level represents an important element of investor protection and should be duly accounted for in the passporting conditions for non-EU AIFM.

286. Another respondent indicated that they see risks related to investor protection. They first mentioned that many AIFs will finally be part of products or packages which are not only sold or which only benefit to professional clients, but to retail ones: insurance products, pension funds, and even ELTIFs. They acknowledge that risks depend on the choice that would be made jurisdiction by jurisdiction to accept products built on the regulation applicable to AIFMs. Where the regulation is fully similar to European one, except in case wrongdoings happen, they indicated they can assume the risks are very low, if any. But where there are peculiarities in the AIF-equivalent framework, this respondent was of the view that things might be different:

a. This respondent can foresee some problems where the legislation applicable to the custodian/depositary allows some practices such as "self custody", or when segregation rules give more leeway to fund promoters ; in case of problems –and of course in case of frauds - the losses might be quite significant and investor protection lowered compared to what is required for European AIFs;

b. They can also foresee direct risks of purely and simply circumventing the European regulation. In their views, a good example is related to money market funds regulation Europe is discussing today; if funds domiciled in jurisdictions considered as equivalent to EU are set up and then marketed in Europe to professional clients according to the AIFs/AIFM passport without abiding the same rules, this respondent considered it is a breach in the European regulatory framework; they indicated that this example is not theoretical, as it is what is planned by some players to circumvent the SEC regulation on MMFs. This respondent mentioned that it is not in investor protection interests to allow such practices by opening the gates to non-EU Funds, and it seems inconsistent with the aims of European regulation itself. And it would obviously lead to regulatory.

c. This respondent indicated that the same comments can be made about other provisions of the regulatory environment, such as remunerations rules: while EU asset managers are bound to limit the variable part of remunerations, it is not the same in most non-EU jurisdictions; this respondent indicated that it would create a distortion and possibly regulatory arbitrage in favour of non-EU locations for the business.

287. This same respondent also mentioned that Europe in general – and in particular the European countries where this respondent operates as regulated asset managers (France, Belgium, Netherlands, Ireland , Lux, UK, Sweden, Finland, Italy)- has put in place a very comprehensive regulatory set of rules which, by far, differ from what is

existing in most non-European countries, with perhaps the exception of the US, HK, Australia and Canada, even though in some areas –for example the depositary regime- the local framework is less protective for investors than what they know in Europe. In most countries, the level of requirements and the level of supervision is lacking behind Europe, not for everything, but for some aspects, leading to less compliance costs, allowing more leeway or more flexibility, if not taxation advantages.

288. Another respondent indicated that it is more difficult for local EU Regulators to enforce and oversee entities outside of their jurisdiction.

289. Another respondent indicated that it was their belief that, in order to provide that the extension of the passport does not lead to a decreased level of investor protection, the assessment on the extension of the passport should consider the existence of a regulatory and enforcement environment between the EU and the third country in question, with the aim to provide equivalence of outcome in terms of investors protection, which both EU and non-EU AIFMs should safeguard. They indicated that attention should be also driven to the already established set of provisions in AIFM Directive, where safeguards are foreseen for the extension of the AIFMD passport in art. 37(2), (4) and (7), establishing a general obligation of compliance with the directive, the conditions for determination of the Member State of reference and further conditions for authorization, to ensure that a comparable level of investor protections is met.

290. This respondent further mentioned that it should also be noted that co-operation arrangements between EU Member States and the authorities of third countries are important tools that can contribute to ensure an increased level of investor protection, encouraging smoother collaboration between regulators in exercising their supervisory duties, in the ultimate interests of investors

291. Finally, this respondent indicated that with regard to the scope of the analysis, the reference for the collection should be limited to EU AIFMs and not extended to UCITS management companies, as they do not form part of the mandate for the advice under AIFMD and might entail different experiences compared to AIFs.

292. Another respondent indicated their views on the impact of the potential extension of the passport to non-EU AIFMs on investors' choices. This respondent indicated that their members have observed that EU investment institutions are experiencing limited investor choice and access to high quality investment options in emerging markets as non-AIFMs severely limit their efforts to raise capital in Europe and concentrate their efforts elsewhere. This respondent mentioned that this is not only the case for the strongest performing and established asset managers ('GPs') who have the greatest choice as to whether and where to raise capital, but also for younger, high performing GPs offering high quality investments in emerging markets. The consequence this respondent indicated is a limitation on the EU investment institutions' ability to diversify their investment portfolios by accessing emerging market investment opportunities and obtain their target returns. This, in turn, impacts both risk and return

expectations over the near, medium and long terms with the final result limiting not only returns to, for example, occupational pension holders, but also the ability of EU development finance institutions to deploy development funds consistent with their mandates. This respondent further mentioned that taxpayer-funded development finance institutions are expected to focus funds on socially beneficial investments that are profitable and therefore, scalable and sustainable to address poverty eradication and economic development in emerging markets. Foregone development opportunity is not recoverable and, once private capital exits, new collaborative opportunities take time and resources to pursue.

293. The Members of this respondent have also questioned why there is no distinction between "*professional qualified investors*" (whose capital fuels the private capital industry) and "*retail investors*" (whose capital does not). Retail investors do not typically invest in capital funds. These members see this as one example of how the AIFMD does not take into account the difference between private capital investing funded by "*professional qualified investors*" and other forms of investing funded by retail investors

294. <u>Another respondent</u> indicated that the risks of market disruption within the EU internal market and to investor protection would be limited, if any. This respondent was of the opinion that an extension of the passport will encourage a levelling-up of investor protection standards applying to both EU and non-EU AIFM. In their experience, the majority of AIFs that could potentially seek an EU passport for marketing to EU professional investors are already highly regulated in their home jurisdiction for distribution to retail investors (e.g. US 1940 Act mutual funds). Therefore this respondent was of the view that it should not be necessary to adopt any strict line-by-line equivalency of EU investor protection rules for the non-EU AIFM professional investor passport when a similar outcome has already been achieved for retail investors in the home jurisdiction. This respondent added that other non-EU jurisdictions, such as Switzerland and Jersey, are already implementing AIFMD-compatible regimes in order to enable future use of an extended AIFMD marketing passport.

295. This same respondent mentioned that a further element of improved investor protection is the increasingly closer cooperation between Member State and third country regulators since the implementation of AIFMD – for example, cooperation arrangements have been completed between regulators as a condition to the operation of Articles 36 and 42 AIFMD and also under Article 20 where investment management is delegated to a third country. This respondent indicated that this interaction between regulators should enable better supervision and improved ability for customer redress where the non-EU AIFM passport is used.

296. This respondent also mentioned that another benefit of an extended passport for both regulators and non-EU AIFMs, would be the need for non-EU AIFMs to provide regulatory reporting only to a single Member State of Reference. This respondent was of the opinion that this would result in less duplicate reporting for non-EU AIFMs

which currently market (and report) into multiple Member States under Article 42 AIFMD, and less duplicate reporting being received and processed by national regulators and, ultimately, ESMA.

297. This respondent stated that in the event of an extension of the passport for non-EU AIFs, they would also welcome greater flexibility upon the location of EU depositaries within the EU than would otherwise appear possible under Article 21.5(b) AIFMD. This respondent mentioned that an amendment to Article 21.5(b) could be considered as part of the AIFMD review under Article 69. This greater flexibility would be particularly appreciated for EU AIFMs currently marketing non-EU AIFs under Article 36. For example, this respondent manages a number of non-EU AIFs via its UK AIFM which, as part of compliance with Art 36, have appointed an Irish depositary-lite provider who utilises the data from the fund's existing Irish administrator to assist with its oversight and monitoring function. If the passport is activated for these funds, it would make greater sense in their view from an operational risk and efficiency and investor protection perspective to retain and expand the existing, tried and tested Irish service providers to include a full Irish depositary rather than have to restructure the operations of the fund and appoint a depositary in either Cayman or the UK (as would appear to be required by Article 21.5(b)), where such service providers for these types of funds are currently limited in numbers

298. Another respondent indicated that they believed the risks associated with the extension of the AIFMD passport to non-EU countries would be minimal due to the fact that such non-EU AIFMs would have to comply with AIFMD requirements in order to obtain a passport, thus minimising risks in relation to market disruption, investor protection and the monitoring of systemic risk. In addition, this respondent was of the view that these risks are especially low as regards the provision of a passport in respect of a non-EEA AIF that is managed by an EEA AIF (i.e. funds currently covered by Article 36), as the relevant AIFM will (by definition) be based in the EEA thereby removing the relevant NCA's reliance on a non-EU NCA.

299. Another respondent indicated that the risks of an eventual extension of the passport to non-EU AIFMs in relation to market disruptions and investor protection would very much depend on the quality of regulation in the relevant non-EEA jurisdiction and the facility for co-ordination between EEA and non-EEA regulators. If the private placement regime is phased out alongside the extension of the passporting regime, this respondent thinks this would have a negative impact on competition, on investor choice and on the internal movement of capital

300. Another respondent indicated that as a general assessment, because any experience related to the AIFMD passport is based on a timeframe of a maximum of only one and a half years, there is no need to hurry up for an extension of the passport regime. Moreover, this respondent indicated that the fact that the AIFMD is a manager and not a product directive makes it difficult to capture cross-border situations in which non-EU countries are involved. The latter have their own laws, and managers from those countries usually do not want to comply with an additional set of rules as long

as there are alternative solutions. This respondent added that this is particularly true for smaller players focusing on specific sectors as opposed to global players with a big distribution network.

301. All in all, this respondent was of the view that autumn 2015 is not a realistic date for an extension of the AIFMD passport to third countries. They think a decision by the European Commission on an extension of the passport should be deferred by at least three years until 2018, i.e. the point in time where National Private Placement Regimes are meant to disappear. A possible decision in favour of an extension at that stage should be followed by a transition period of one year for the abolishment of National Private Placement Regimes the benefit of existing AIFs and their managers, which will have to get familiar with the requirements set by the AIFMD.

302. Another respondent indicated that the availability of a Passport would benefit EU investors insofar as it results in a broader and better array of investment options. That said, they indicated that should an extended Passport regime be disproportionately structured or unevenly applied, and should national private placement regimes be eliminated entirely, non-EU AIFMs targeting only a small number of European investors or countries will direct their marketing efforts to jurisdictions outside Europe where the compliance burden is commensurate with the pool of potential investors or capital available. This respondent indicated that this would undermine the very benefits to market efficiency, competition and investor choice that the introduction of a marketing passport for non-EU AIFMs should create

303. In addition, this respondent indicated that their members do not anticipate that extending the Passport should pose any additional risks related to market disruptions or investor protections, as in many cases this would simply be a restoration of communication with managers that investors had identified as high quality prior to the implementation of the AIFMD. They indicate that they do, however, caution that the uneven requirements that have manifested within the implementation of the AIFMD Passport regime should not be allowed to persist if the Passport regime is extended to non-EU AIFMs. *"European investors are best served by having a wider range of potential investment opportunities, as long as those AIFMs are properly vetted and the screening process is consistent across the EU" "[There must be] a uniform application of the requirements under the AIFMD across all member states so as to prevent "forum shopping" and maintain the agreed level of requirements on AIFMs".*

304. Finally, this respondent concluded that their members strongly favour the extension of the marketing Passport to non-EU AIFMs, provided such a regime is introduced in an efficient way and is constructed to be proportionate to the role that European investors play in the funding base for non-EU AIFMs, and is consistently applied. Their members also believe that the review process should be no more and no less stringent than for EEA AIFMs, as "*making the review too stringent for non-EU AIFMs will reduce the range of investment options available to EU-based investors*," thus negating the envisioned benefits of extending the Passport regime to non-EU AIFMs in the first instance. They mentioned that many European investors believe that

AIFMs that are already subject to robust regulation in their home markets, such as registration with the SEC in the United States, should be able to easily demonstrate their credentials to the satisfaction of European authorities. They also referred to the detailed analysis presented in the submissions by EVCA and others around some of the specific impediments to be addressed and issues to be considered in the event of the extension of the Passport regime.

305. Another respondent indicated that in order to avoid any risks in relation to market disruptions and investor protection and on the basis of the AIFMD Level 1 text, they believed that the mechanisms for an extension of the AIFM passport (especially Article 37 on authorisation in the Member State of Reference) should already safeguard a level of investor protection comparable to standards applicable within the EU. This also relates, in particular, to the requirement to ensure general compliance with the AIFMD under Article 37(2) and to further conditions for authorisation under Article 37(7). This respondent indicated that the assessment of existence of same conditions between the EU and the relevant third countries should include not only the assessment of the regulation itself, but also the way the enforcement of the rules is carried out locally in practice. This respondent was of the view that in fact, if the rules or the enforcement of the rules are less stringent in some third countries, it might become ultimately a way for circumventing the EU rules as it would create an incentive for "bad" EU players to relocate themselves outside Europe before re-entering the Single Market from these third countries.

306. Another respondent indicated that the ability to passport into a Member State rather than use national private placement regimes would likely mean more AIFMs may manage or market AIFs in Member States so any failure of oversight and/or regulation relating to a non-EU AIF could have a larger impact on EU investors. However, this respondent mentioned that it should be remembered that the passport only allows access to professional investors (it remains a national competence to allow AIFs to be marketed to retail investors). Furthermore Article 37 of the AIFMD has put in place additional safeguards by the use of a Member State of Reference. This respondent added that supervisory co-operation between regulators is one of a number of regulatory requirements which need to be in place before market access is allowed (either under a passport arrangement or national private placement arrangement) meaning it is incumbent on regulators to ensure cooperation does take place.

307. This respondent added that it should also be noted that the amount of duplication in reporting would be reduced (since under Article 42(1)(a) the non-EU AIFM has to comply with Article 24 reporting obligations with respect to each Member State where an AIF is privately placed

308. Another respondent indicated that they thought the risks of extending the passport to non-EU AIFMs are likely to be low provided that the non-EU AIFMs operate in third countries with EU-equivalent regulatory environments (financial regulation, supervision, tax and anti-money laundering provisions). Jersey and Guernsey have

implemented the necessary regulations to comply fully with the AIFMD. The successful introduction of the passport would provide investors' a greater global choice of AIFMs and AIFs and could lead to a decreased concentration of systemic risk within.

309. Another respondent indicated that there would be minimal, if any, risks in relation to investor protection with the extension of the AIFMD passport: this respondent was of the view that the extension of the passport regime would serve only to level the AIFMD trade wall, that is, to ensure that a non-EU AIFM would at least be equally inconvenienced throughout the EU rather than subject to a patchwork of overtly discriminatory practices. This respondent added that in their experience, the EU AIFM regime is the strictest in the world and appears to be hostile to non EU firms wanting to serve clients in the EU.

310. Another respondent indicated that they believe that the risks of market disruption and to investor protection are limited. They mentioned that while passports should not require a line-by-line equivalency of investor protection rules, it should be remembered that many of the AIFs that would be seeking passports are designed and supervised for distribution to retail clients in their home state (e.g. US '40 Act mutual funds) while they would only be obtaining passports for marketing to professional investors in the EU. They mentioned that professional investors do not require the investor protection standards that are appropriate for retail investors investing in UCITS, while many AIFs seeking passport have been designed to retail sale standards. They added that non-EU AIFMs making use of the passport would be required to meet improved standards for their depositary and transparency.

311. This respondent added that they understand that both Jersey and Switzerland are developing AIFMD-compatible regimes, specifically to enable them to make use of AIFMD passports into the EU.

312. This respondent added that another positive factor is that, since the introduction of the AIFMD, member state and third country regulators have been in much closer dialogue, discussing supervisory standards, customer redress etc. They also indicated that one positive benefit, for both regulators and non-EU AIFs making use of the passport would be the need only to report to the Member State of Reference. This would result in considerably less duplicate reporting for AIFMs, and fewer reports being received by regulators.

313. This respondent also took this opportunity to raise a concern with regard to the location of the depositary once the third-country passport regime is extended. This respondent indicated that article 21(5) offers, among others, the possibility for a non-EU AIF depositary to be located in a third-country (non-EU) jurisdiction. Under these circumstances they mentioned that there may be concerns about the level of investor protection to the extent that the appointed depositary in the third-country is not capable of fulfilling all the obligations prescribed under the directive. This respondent would therefore encourage ESMA to consider ways of ensuring that depositaries

located outside the EU are capable of performing their duties to EU standards when recognising that depositary regulation in third country jurisdictions is of "same effect" as EU rules.

314. Another respondent indicated that in their view, the principal investor protection risk is that if non-EU AIFMs could obtain a passport without being subject to quite the same degree of regulatory scrutiny (in principle and in practice) as applies to EU AIFMs, then investor protection within the EU would be diluted and undermined. This respondent noted that Article 37 of AIFMD (addressing the potential authorisation process for non-EU AIFMs) includes various procedural safeguards designed to apply and maintain equivalent standards, in particular through relying on the concept of the Member State of Reference. However, they mentioned that the geographical disconnect between a non-EU AIFM and its Member State of reference, as well as the unavoidable reliance on the local regulator of the non-EU AIFM to assist with supervision and enforcement, creates the potential for standards of regulatory oversight (and accordingly standards of investor protection) to dip below those which apply to EU AIFMs authorised and supervised from within their home Member State. They mentioned that as investor protection is one of the core principles of AIFMD, no steps should be taken towards a third country passport without certainty that the same standards of oversight and AIFMD compliance are applied to AIFMs in the relevant third countries.

315. This respondent added that in their view, the principal market disruption risk concerns how the concept of the Member State of Reference ("MSoR") will operate in practice following the implementation of a third country passport, including but not limited to the impact on the depositary market. They indicated that Article 21.5 currently contemplates that a non-EU AIF, upon securing a marketing passport, would be required to appoint a depositary located in its home jurisdiction, in the home Member State of the AIFM, or in the MSoR. They believed that the requirement regarding depositary location in the context of the third country passport creates the potential for unnecessary market disruption, risk, uncertainty and confusion for investors.

316. They mentioned that a range of concerns arise in relation to the application of the depositary location requirement in the context of the third country passport:

a. They mentioned that the Member State of Reference is potentially subject to change and uncertainty. The process of determining the MSoR is complex, particularly where distribution is envisaged in several Member States, as no single deciding factor on the MSoR is provided. Instead regulators must come to a mutual agreement and in the absence of such agreement, ESMA will arbitrate the decision. The MSoR can also change subject to distribution and management activities in the EU. Consequently, in their view the MSoR concept does not provide a reliable basis for the selection and appointment of a depositary, as changing a depositary is a very significant task which must be carefully planned, executed and notified to investors. They mentioned that a change in depositary is not a project which an AIFM or its investors will want to contemplate frequently, given the costs, disruption and potential risks involved.

b. They also indicated that the home Member State of the AIFM may not have access to a recognised selection of depositaries. The provision of depositary services to EU regulatory standards is a highly specialised activity, carrying with it very significant responsibilities and liabilities. They mentioned that many AIFMs will want to maintain the appointment of depositaries with whom they have existing relationships and are comfortable with from a due diligence perspective. They were of the view that specialist AIF depositaries with the requisite capabilities are not established in all EU markets and it is entirely possible that the home Member State of the AIFM may not have access to a recognised selection of depositaries. They mentioned that the current requirement could limit the AIFM's scope to appoint an appropriate depositary specialised in its area of business. In their view this would prove disruptive to markets and run contrary to investors' interests to restrict the choice that an AIFM may have and to force them to appoint a depositary in a particular jurisdiction without a developed depositary business. It was as a result of this concern that Article 61.5 provided that an AIF may appoint a depositary outside of its home Member State until 22 July 2017, provided that the depositary is located in the EU.

c. They also mentioned that requiring the depositary to be located outside the EU is a higher risk approach. As currently drafted, in their view the only other option open to non-EU AIFs/AIFMs is to appoint a depositary in the location of the AIF. They do not regard this as an optimal outcome from an investor protection perspective, as it is not immediately apparent that all non-EU jurisdictions would have the appropriate legal and regulatory framework or developed depositary business with the specialised expertise, infrastructure, resources and capacity to carry out depositary duties to AIFMD standards. The appointment of a depositary located outside the EU could in some cases create an unnecessary divergence of depositary eligibility and present greater risks for investors.

d. They also indicated that many AIFMs already marketing in the EU will be forced to dismantle existing depositary arrangements causing significant market disruption. Under Article 36, EU AIFMs marketing non-EU AIFs in the EU will already have appointed a depositary. These AIFMs may consequently be forced to unbundle existing depositary arrangements only recently agreed, creating the unintended consequence of less choice in terms of available depositaries and additional costs in changing depositary. Furthermore, they added that some NPPRs (e.g. Germany, Denmark) require AIFs to appoint a depositary in order to be permitted to market in that jurisdiction. Absent a change in the provisions, the acquisition of a marketing passport would have the effect of requiring some

AIFs to change their depositary arrangements, potentially to a non-EU depositary in a case where they are already using an EU-based depositary. They indicated that there is no evident benefit to investors in requiring an AIFM to appoint a depositary in a non-EU jurisdiction but it is a bizarre and unintended outcome not to permit AIFMs to appoint a depositary in an EU Member State of their choice.

e. They also mentioned that the current requirements would limit the ability of the AIFM to appoint the most appropriate depositary. IN their view the location of an AIF's assets rarely bears (and does not need to bear) any correlation to the domicile of the AIF or the AIFM or the jurisdiction(s) in which the AIF may be marketed. They further indicated that there is no apparent benefit to investors, therefore, in requiring the depositary to be located in one of these jurisdictions, while it would additionally prove disruptive to markets to cause AIFs to move depositary in order to comply with the requirements of Article 21.5 as currently drafted. They proposed that any AIF being marketed to EU investors should be permitted to appoint the most suitably qualified and appropriate depositary specialised in its area of business. They indicated that any additional investor concern arising from the AIF being located outside of the EU can be offset by the additional flexibility afforded to AIFMs in their selection of an appropriate depositary.

317. Consequently, they strongly suggested that in advance of activation of the third country passport, ESMA and the Commission should seek to ensure sufficient flexibility in relation to the location of the depositary within the EU. Ultimately, they indicated that this would entail a change to the Level 1 text, in which case they propose that the words "*….or in any Member State, so long as the depositary so appointed meets the criteria in Article 21.3 of this Directive*" be added to the end of paragraph b) of Article 21.5.

318. <u>Another respondent</u> indicated that the passport should be extended to appropriately regulated non-EU AIFMs in recognised jurisdictions that have equivalence under the Anti-Money Laundering Directive (Directive 2005/60/EC), have implemented the necessary regulation to comply fully with AIFMD (in line with EEA AIFMD passport requirements under Level 1 and Level 2 AIFMD) and comply with the standards laid down in Article 26 of the OECD Model Tax Convention on Income and on Capital, as per Article 40(2)(c) of the AIFMD to ensure Investors are protected. The Passport needs to be implemented in a uniform and harmonised manner across Member States to ensure that investors have access to the best products that EU and non-EU AIFMs that meet these obligations, can offer and ensure competition is maintained.

319. <u>Another respondent indicated</u> indicated that that risks of an eventual extension of the passport to non-EU AIFMs in relation to market disruptions and investor protection would arise only where AIFMD equivalent regulation was not available. Nonetheless this respondent indicated that it would be essential for equivalence and assessment

mechanics to be workable and transparent in order to enable such an extension of a passport to non EU AIFMs. This respondent indicated that it is anticipated that in the event of eventual extension, initial workability issues concerning the operation of the passport will apply to third country AIFMs in the same way as they do currently to EU AIFMs. They encouraged the resolution of these issues in conjunction with the extension of the passport while maintaining the regime of NPPRs in order to preserve stability.

320. This respondent indicated that it is understood that there are a number of inconsistencies which exist in relation to the operation of the passport mechanism. For example (i) inconsistent imposition of passporting fees by different member states; (ii) requirements for additional appointments of eg paying agents in certain member states (iii) varying approaches of NCAs to levels of review of AIF documentation. As well as resolving these areas, this respondent indicated that additional areas that would need to be clarified or resolved in order to allow a passport mechanism to be available to AIFs and AIFMs in well-regulated and cooperative third country jurisdictions would include such aspects as (i) developing a consistent mechanism for determining the member state of reference (as referred to at Article 37 of the AIFMD); (ii) clarification of criteria for satisfaction of OECD model tax convention-compliant agreements; and (iii) implementation of appropriate transition rules for AIFs which were marketed prior to the development of the passport.

321. This respondent indicated that the additional authorisation and filing obligations that EU NCAs will become subject to if the passport is extended to third country AIFMs, and observes that such obligations may also require stream-lined processes and enhanced regulatory resources in order for effective regulation and investor participation to be achieved. In the absence of the above measures being taken this respondent mentioned that then there would be a significant risk of additional market disruptions.

322. Another respondent indicated that in terms of investor protection, if third countries are less demanding in their rules, and/or less stringent in their enforcement, than in the EU, it might generate a lower investor protection for EU investors if those EU investors make use of a non-EU AIFM and/or non-EU AIF. This respondent mentioned it might be an increased issue if the relevant EU investors are institutional investors acting on behalf of retail investors, such as pension funds which are financing the individual pensions of retirees. For instance, this respondent indicated that there is a risk that stringent rules on AIFs or AIFMs in Europe might lead to their circumvention through the setting of AIFMs and/or AIFs in third countries, which would then be imported back to the EU. this respondent indicated that one could see for instance the current concern in the US that the new rules on US Money Market Funds might be circumvented by launching Money Market Funds in other territories such as Cayman Islands in order to propose them back to US investors.

323. This respondent indicated that in terms of systemic risk, allowing the passport to third countries might lead to an import of additional systemic risk in the EU if the home third countries do not master properly the potential systemic risks generated by the AIFMs and the AIFs domiciled in their jurisdictions – either by having less stringent rules and/or by having less stringent enforcement of their rules than in the EU.

324. Another respondent indicated that they consider fundamental for ESMA to ensure that the extension of the AIFMD passport to non-EU AIFMs does not lead to market disruptions and/or a lower level of investor protection standards. They were of the opinion that an extension of the AIFMD passport should be subject to an assessment which should aim for equivalence of outcome in terms of investor protection standards for both EU and non-EU AIFMs. On the basis of the AIFMD Level 1 text, they believed that the mechanisms for an extension of the AIFM passport (especially Article 37 on authorisation in the Member State of Reference) should already safeguard a level of investor protection comparable to standards applicable within the EU. This also relates, in particular, to the requirement to ensure general compliance with the AIFMD under Article 37(2) and to further conditions for authorisation under Article 37(7).

325. However, this respondent indicated that this assessment should not only consider the regulatory framework between the EU and the relevant third country, but should also reflect on the enforcement of these rules in local practice – as an uneven enforcement could ultimately lead to lower investor protection standards for EU investors.

326. This respondent indicated that another important way of ensuring increased investor protection is closer cooperation between EU Member State and third country regulators. Co-operation arrangements are the first step in this process and further increased interaction between regulators should enable better supervision (i.e. powers of the non-EU relevant authorities in monitoring, enforcing, investigating and sanctioning their local market participants) and improved ability for customer redress where the non-EU AIFM passport is used. This respondent indicated that in the medium to long term the extension to non-EU AIFMs could also create some regulatory convergence for non-EU AIFMs to provide their regulatory reporting only to a single Member State of Reference. This respondent indicated that this could streamline duplicate reporting for non-EU AIFMs which currently report into multiple Member States under Article 42, and therefore lessen instances of duplicate reporting which should ultimately lead to enhanced supervision by national regulators and ESMA.

Annex 2. Summary of the feedback from the call for evidence in the case of the US

Overall summary of the feedback from the call for evidence

Investor protection

37. As a general assessment, one respondent indicated that Europe in general – and in particular the European countries where this respondent operates as regulated asset managers (France, Belgium, Netherlands, Ireland , Lux, UK, Sweden, Finland, Italy) - has put in place a very comprehensive regulatory set of rules which, by far, differ from what is existing in most non-European countries, with perhaps the exception of the US, HK, Australia and Canada, even though in some areas – for example the depositary regime- the local framework is less protective for investors than what they know in Europe. In most countries, the level of requirements and the level of supervision is lacking behind Europe, not for everything, but for some aspects, leading to less compliance costs, allowing more leeway or more flexibility, if not taxation advantages

38. As a general assessment, another respondent indicated that many European investors believe that AIFMs that are already subject to robust regulation in their home markets, such as registration with the SEC in the United States, should be able to easily demonstrate their credentials to the satisfaction of European authorities.

39. Another respondent indicated that appropriate cooperation agreements are in place between the US Securities and Exchange Commission (the "SEC"), the relevant regulatory authority with respect to US AIFMs, and the national competent authorities of the European Union, other than the national competent authorities of Croatia and Slovenia, in order to ensure at least an efficient exchange of information that allows the EU national competent authorities to carry out their duties in accordance with the AIFMD.

40. They also indicated that the United States is not on the list of Non-Cooperative Countries and Territories maintained by the Financial Action Task Force;

41. They supported the establishment and maintenance of an accessible national private placement regime in each European jurisdiction for US AIFMs that desire to market their AIFs in accordance with such regime and in compliance with the requirements set out in Article 42 of the AIFMD.

42. This respondent indicated that US AIFMs are already subject to an extensive US regulatory regime that has objectives equivalent to those of the AIFMD regime (including, without limitation, the objectives of investor protection and monitoring of systemic risk). As such, they are of the view that the application to US AIFMs of an

additional European regulatory overlay is not necessary. They understood though that the AIFMD prescribes a European regulatory framework that will apply where the Passporting Regime is extended to non-European AIFMs. They respectfully submitted that, when determining the specifics of implementation of a Passporting Regime for US AIFMs, due consideration and recognition should be given to the US regulatory regime that already applies to US AIFMs and the extensive oversight and scrutiny to which they are already subject.

43. This respondent also indicated that Investor protection is a hallmark of the US regulation of alternative investment fund managers and other investment advisory firms. The management of AIFMs and the marketing of interests in alternative investment funds (an "AIF") are subject to a comprehensive, substantive regulatory regime in the United States.

44. *First*, this respondent indicated that US AIFMs are already subject to an extensive US regulatory regime that has objectives equivalent the marketing of interests in AIFs is subject to the provisions of the US Securities Act of 1933, as amended (the "Securities Act").[33]

45. *Second*, this respondent indicated that US AIFMs are already subject to an extensive US regulatory regime that has objectives equivalent for sales of interests in most US AIFs, the US Investment Company Act of 1940, as amended (the "Investment Company Act"), requires that the investors be limited in number (to no more than 100 beneficial owners) or that an investor has investment assets of at least $5 million (in the case of an individual and a family company) or of at least $25 million (in all other cases).

46. *Third*, this respondent indicated that US AIFMs are already subject to an extensive US regulatory regime that has objectives equivalent additional US federal and/or state statutes and rules regulate (1) the management and activities of placement agents and certain other persons who are in the business, for compensation, of marketing securities, including interests in AIFs, to investors (*e.g.,* the US Securities Exchange Act of 1934, as amended), (2) anti-corruption and bribery concerns with respect to the activities of US persons, including US AIFMs and their affiliates (*e.g.,* the US Foreign Corrupt Practices Act), and (3) a variety of other matters.

47. *Fourth,* this respondent indicated that US AIFMs are already subject to an extensive US regulatory regime that has objectives equivalent US AIFMs are regulated under the US Investment Advisers Act of 1940, as expanded and amended by the US Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 (the "Advisers Act").[34] Even

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[33] The Securities Act contains anti-fraud provisions (and associated penalties for violation of those provisions) applicable to both public and private offers and sales of interests in AIFs. Private offers and sales of securities, including of interests in AIFs (which are typically sold in private offerings) are also typically subject to restrictions on the manner and nature of the offering and the number and sophistication of offerees.

[34] A US AIFM of private funds generally is required to register with the SEC if it has more than $150 million in assets under management. Certain venture capital fund advisers (narrowly defined) are exempt from registration, but these venture capital fund advisers are still required to make filings with the SEC, are subject to the anti-fraud provisions of the Advisers Act and are

before the Dodd-Frank Act, the marketing activities and ongoing dealings with clients of all US AIFMs were subject to the anti-fraud requirements and certain other provisions of the Advisers Act. The Dodd-Frank Act, by expanding the scope of the Advisers Act's registration requirement, layered additional requirements on top of the already extensive and longstanding regulatory regime described above. As a result, every sizeable US AIFM is subject to additional substantive regulation by, is required to register with, and is subject to examination (to ensure compliance with the foregoing) by the SEC under the Advisers Act.

48. Another respondent indicated they would like to share with ESMA a pragmatic approach which acknowledges the realities of marketing of closed-ended AIF to international professional investors. In this approach, they also took into account similar AIFMD rules introduced by third country concerned. This respondent indicated that they identified three groups of third countries as described below:

a. First group: Implementation of third country passport. This group includes countries which have implemented AIFMD in their jurisdiction. The third countries concerned are mainly Switzerland and the Channel Islands (Jersey and Guernsey) with whom they have significant trade, economic exchanges or partnership relations. Those countries made an effort to adopt the AIFMD legislation in their national legal system. They believed this is important to promote their approach. This is the reason why this respondent supported for those third countries the implementation of third country passport in accordance with AIFMD on the basis of equivalent rules

b. Second group: "*statu quo*" approach. This group includes countries which have not implemented AIFMD in their jurisdiction but have developed on another basis a strong legislation on marketing. The third countries concerned include the USA. This respondent indicated that they hope to implement the marketing passport in these jurisdictions one day but they believe that it is too early for this. All these countries have adopted a NPPR and are not ready yet to implement a legislation based on the same approach of AIFMD

49. Another respondent indicated that in recent years, significant non-EEA fund domiciles have strengthened both manager and fund related regulation with a focus around investors. For example, the Alternative Investment Funds (Jersey) Regulations 2012, AIFMD Rules 2013 in Guernsey, and Dodd-Frank in the U.S. This respondent mentioned that these regulations either incorporate the AIFM rules into the non-EEA fund regulations, or regulate the fund industry with the same effect as the AIFMD.

50. Another respondent indicated that regarding specifically the regulation of AIFMs and AIFs, the regulations may be weaker in some third countries on some points. For instance in the US, this respondent indicated that investment advisers (acting in a way similar to asset management companies) may self-custody the assets they manage –

subject to examination by the SEC. We further note that, in addition to fund managers/investment advisers, the general partners of AIFs organized as limited partnerships are also typically subject to registration with the SEC as investment advisers.

and this possibility is still offered after the Madoff case. This respondent indicated that this flexibility generates lower costs for local players (and also a lower protection for investors) as compared to the mandatory use of an external depositary.

Competition and Market disruption

327. There are among the respondents of the call for evidence diverging views in relation to the extent to which the U.S market is more or less accessible than the EU market for US funds. Some respondents indicated that the U.S Regulators impose heavier requirements for EU AIFMs or UCITS management companies in comparison to those that non-EU AIFMs have to comply with in order to do business in the EU. These respondents were of the view that it is impossible to get access to the US market without fully complying to the SEC regulations applicable to local asset managers. These respondents mentioned that the U.S requirements notably entail a periodicity and details in the reporting which are heavier than in Europe.

328. These respondents added that the scope of SEC supervision would not be limited in such a case to the activities which are linked to the US, but would cover all the activities performed by the non US asset manager.

329. They further indicated that the U.S market is closed to non-local AIFs or UCITS – except if the asset managers fully applies the US regulations and recognize they are subject to the US regulation and to the US regulator's supervision, including on-site inspections: this situation is very different from what is contemplated by the EU regulation if a passport is granted to non-EU AIFMs. These respondents were of the view that giving a passport to US AIFs or AIFMs would not oblige the US asset managers to fully apply the European legislation as this respondent indicated they are obliged to do if they want to establish or market funds in the US.

330. These respondents also mentioned that US actors have been the most active asset managers in Europe for the five last years while European fund managers have a very weak position in the U.S.

331. These respondents also emphasized that there are strong regulatory barriers for selling investment funds in the US or even for the free investment in EU investment funds by US citizens at their own initiative.

332. These respondent also mentioned operational barriers, namely Joining DTCC as a member is a long and heavy process. They indicated that the funds to be available for the offshore space also need to be NSCC (National Securities Clearing Corporation) eligible. This implies a specific IT protocol to be developed; they mentioned the entire process does not take less than 6-9 months. They also mentioned that other U.S rules apply, such as: i) "U.S. Shareholder" rules as described in the Code which de facto limit US investors to less than 10% of the foreign fund's share capital; ii) Controlled Foreign Corporation rules (CFC) which may also limit US ownership.

333.Those respondents conclude that when opening up to US AIFMs without requiring reciprocity, i.e. access to the US market, the EU puts EU AIFMs at a disadvantage: US AIFMs would access to the EU market with the help of the passport while EU AIMFs would continue to lack access to the US.

334.However other respondents were of the view that the United States currently grants EU AIFMs and UCITS management companies access to the US market under conditions that are broadly equivalent to those granted by the EU. These respondents focussed their explanations on the current situation, as opposed to the situation of the market after the passport would be granted to the U.S, and focused their explanations on the case of retail investors.

335.These respondents were of the view that the Extension of the Passporting Regime to US AIFMs is important for ensuring that European AIFMs and US AIFMs have a “level playing field” in connection with the marketing of AIFs to European professional investors.

336.Other respondents acknowledged that for investment management services (i.e. MiFID activity in EU-speak; “investment advice” in US-speak), non US managers have to register with the SEC. They mentioned that while it may be considered by some managers as a reasonable requirement and not draconian or difficult to secure (for instance, many UK managers are appointed investment advisers for mutual funds), such a registration may be seen by others as a barrier. It has been experienced that a strong barrier is the obligation for EU managers to register at US level to be allowed to receive a delegation from a US manager.

337.Other respondents indicated that due to the regulatory requirements of the AIFMD the large part of U.S managers would not be willing anyway to fall in the scope of the AIFMD directive, even if that meant not being able to take advantage of the AIFMD passport for managers.

338.Other respondents indicated that as for Tax barriers in the U.S, there was the PFIC Regime: Non-U.S. corporate funds are “passive foreign investment companies” (“PFICs”). U.S. taxable investors investing in non-US funds will prefer an investment structured as a partnership. US taxable investors investing in a PFIC are subject to a more disadvantageous tax regime than if they invest in a U.S.-domiciled fund or a non-U.S.-domiciled partnership.

339.A detailed summary of the feedback from the call for evidence on competition and market disruption related issues in the case of the US is included in Annex 1.

Monitoring of systemic risk

340.One respondent indicated that the regulatory regime for a US AIFM ensures the SEC has comprehensive, detailed and vigorous oversight of that US AIFM. This oversight extends to potential systemic risk concerns. While recognising that the AIFMD prescribes a regulatory framework that will apply in the event that the Passporting

Regime is extended to US AIFMs, this respondent is of the view that the regulatory regime already applicable to US AIFMs is robust.

341. This respondent indicated that the SEC requires that a US AIFM that is registered with the SEC and has greater than USD 150 million in assets under management attributable to AIFs file a Form PF in addition to a Form ADV. Form PF is a report that is designed to allow the SEC, the US Financial Stability Oversight Council (the "FSOC") and other financial regulators to assess any potential for systemic risks related to AIFs. This respondent indicated that the frequency and level of detail required by a Form PF depends on the US AIFM's assets under management and the types of AIFs the US AIFM manages, but a Form PF must be updated and filed at least annually.

342. This respondent indicated that in its Form PF a US AIFM must file information about each AIF it manages (this includes both US AIFs and *non-US AIFs*). Further and for the purposes of assessing the effectiveness of the cooperation agreements in place between the SEC and the various European national competent authorities, the records and reports of each such AIF (US and *non-US*) are deemed to be the records and reports of the US AIFM and are subject to examination by the SEC. The SEC requires US AIFMs to maintain certain books and records relating to its AIFs and it has the authority to examine all the books and records of those AIFs.

343. This respondent indicated that the information contained in the Form PF submitted by a US AIFM is primarily intended to provide empirical data to the FSOC based on which the FSOC may make determinations about the extent to which the activities of AIFs or US AIFMs pose systemic risks.[35] In addition, Form PF was drafted with the intention of advancing "international efforts relating to the collection of systemic risk information."[36] To this end, this respondent indicated that the SEC staff consulted with ESMA, the United Kingdom's Financial Services Authority, the International Organization of Securities Commissions and Hong Kong's Securities and Futures Commission during the development of Form PF[37] and the SEC expects that it may share information reported on Form PF with various foreign financial regulators.[38]

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[35] Reporting by Investment Advisers to Private Funds and Certain Commodity Pool Operators and Commodity Trading Advisors on Form PF, SEC Release No. IA-3308 (Oct. 31, 2011) at p. 8. The FSOC has stated that it will consider the data provided on Form PF when considering whether to designate either US AIFMs or the AIFs as nonbank systemically important financial institutions. Thus far, no US AIFMs have been designated as nonbank systemically important financial institutions. Authority To Require Supervision and Regulation of Certain Nonbank Financial Companies, 77 Fed. Reg. 21637 (Apr. 11, 2012).

[36] SEC Release No. IA-3308 at 11.

[37] Id. at 12. In adopting Form PF, the SEC explicitly noted that it had made changes to the originally proposed Form PF to further align the Form PF with the survey efforts of ESMA and the UK Financial Services Authority (now the Financial Conduct Authority).

[38] Id. at fn. 29. The Financial Stability Board and the International Organization of Securities Commissions noted Form PF as one of the data sources for consideration in the identification of non-bank non-insurer global systemically important financial institutions. Consultative Document: Assessment Methodologies for Identifying Non-Bank Non-Insurer Global Systemically Important Financial Institutions: Proposed High-Level Framework and Specific Methodologies (8 January 2014), available at http://www.financialstabilityboard.org/wp-content/uploads/r_140108.pdf.
See, also PEGCC and EVCA Comment Letter on Assessment Methodologies for Identifying Non-Bank Non-Insurer Global Systemically Important Financial Institutions at http://www.pegcc.org/issues/comment-letters/pegcc-and-evca-comment-letter-on-assessment-methodologies-for-identifying-non-bank-non-insurer-global-systemically-important-financial-institutions.

Detailed feedback on from the call for evidence in the case of the US

344. In relation to market disruption, one respondent indicated that they submit that no risk of market disruption is posed by permitting the extension of the Passporting Regime to US AIFMs. This respondent indicated that US AIFMs have long been marketing in the European Union and the nature of the US regulatory regime is rigorous (including, in particular, but not limited to, the SEC's ability to monitor systemic risk). In fact, this respondent indicated that limiting or prohibiting European professional investors' access to US AIFMs may lead to market disruption.

345. In relation to the access to the market, one respondent indicated that there is at least one country that imposes heavier requirements for EU AIFMs or UCITS management companies in comparison to those that non-EU AIFMs have to comply with in order to do business in the EU: the U.S. This respondent indicated that it is absolutely impossible to get access to the US market without fully complying to the SEC regulations applicable to local asset managers. Even though Europe has no reasons to consider their regime is less protecting for the investors, this respondent mentioned that the US requirements – to be SEC registered - entail a periodicity and details in the reporting which are heavier than in Europe. This respondent added that the same comments about reporting to CFTC when required.

346. Furthermore, this respondent added that the scope of SEC supervision would not be limited in such a case to the activities which are linked to the US, but would cover all the activities performed by the non US asset manager. This respondent mentioned that the so called Dodd Franck Act here has extended the regulatory reach of the US regulation.

347. This respondent indicated that the U.S market is closed to non-local AIFs or UCITS – except if the asset managers fully applies the US regulations and recognize they are subject to the US regulation and to the US regulator's supervision, including on-site inspections: in those situations, this respondent considered extraterritorial reach is the rule, which is a very different situation from what is contemplated by the EU regulation if a passport is granted to non EU AIFMS. Giving a passport to US AIFs or AIFMs would not oblige the US asset managers to fully apply the European legislation as this respondent indicated they are obliged to do if they want to establish or market funds in the US.

348. Another respondent indicated that most non-EU countries impose heavier requirements for foreign funds in comparison with what would be required from non-EU AIFMs to get access to the EU market. This respondent was of the view that the US market is clearly one of the most difficult market to enter and one which shows the most striking unbalance in terms of market access. They indicated that in fact, US actors have been the most active asset managers in Europe for the five last years while European fund managers have a very weak position in the US.

349. They indicated they provided hereafter all barriers and constraints that a non US actor has to face when trying to get access to the US market:

350. They indicated that for investment management services (i.e. MiFID activity in EU-speak; “investment advice” in US-speak), non US managers have to register with the SEC which entails heavy consequences in terms of organization, compliance and reporting.

351. They indicated that EU managers have to register at US level to be allowed to receive a delegation from a US manager.

352. They indicated that any foreign manager which provides investment management or investment advice (as an adviser or sub-adviser or manager or sub-manager) to a “mutual fund” (i.e. fund registered with the SEC for public distribution) must be registered with the SEC.

353. They indicated that foreign managers are required to register with the SEC unless they can rely on the “foreign private adviser” exemption from registration (i.e., having fewer than 15 US clients or US investors in funds and AUM from those clients/investors of less than $25 million, and manager cannot hold itself out to the US public as an investment manager).

354. They indicated that it is impossible for a US asset manager to delegate the management of a US mutual fund to a European asset manager if the European asset manager has not been registered at US level.

355. They indicated that as for the sale of foreign funds in the US:

a. In their views, there are regulatory barriers for selling investment funds in the US or even for the free investment in EU investment funds by US citizens at their own initiative (e.g. following the adoption of the Dodd Frank Act, EU asset managers developed disclaimers describing that their funds are not intended for US clients);

b. Section 7(d) of the Investment Company Act of 1940 prohibits the public offering of funds domiciled outside the US. Non-US funds can only be sold on a private placement basis in reliance on an exception under the Investment Company Act. A fund must comply with one of the following: (i) limit of 100 US persons in the non-US fund, or (ii) sales only made to “qualified purchasers” (generally, individuals with $5 million in investments or entities with $25 million in investments). A fund must choose to rely on either (i) or (ii) and cannot mix the two exemptions;

c. In their views, it is a lengthy and burdensome process to bring a fund and its offering documentation into compliance with SEC public offer requirements and to meet significant ongoing compliance, governance, and reporting requirements for a fund offered to the public in the United States (initial legal fees in excess of USD 200,000 and ongoing compliance, operational, and other related expenses that could well exceed USD 200,000 annually).

d. Shares of non-US funds must be sold based on an exemption from registration under the Securities Act of 1933 (on a private placement basis, generally to investors who are "accredited investors" under Regulation D (generally an individual with net assets of $1 million or income for last 2 years of at least $200,000 annually, or an entity with net assets of $5 million).

e. Funds being sold on a private placement basis must file a Form D with the SEC and state securities regulators. If the non-US fund is marketed to public pension plans subject to the US Employee Retirement Income Security Act of 1974 (ERISA), the fund must ensure that total ERISA benefit plan investment is kept below 25% of any class, or the manager to the fund may be deemed to be a fiduciary subject to ERISA. Local offering for clearing and settlement is extremely difficult for foreign entities (self-clearing license requirements). There are some market practices limitations: foreign funds must be NSCC eligible (incorporation is lengthy process) and trading of offshore funds through major platforms is less cost effective and all settlements are USD driven.

356. This respondent also mentioned operational barriers, namely Joining DTCC as a member is a long and heavy process. This respondent indicated that afterwards, the funds (to be available for the offshore space only) need to be NSCC eligible. This implies a specific IT protocol to be developed; As per their knowledge the entire process does not take less than 6-9 months. They mentioned that other US rules apply, such as: i) "U.S. Shareholder" rules as described in the Code which de facto limit US investors to less than 10% of the foreign fund's share capital; ii) Controlled Foreign Corporation rules (CFC) which may also limit US ownership.

357. They indicated that as a consequence of all this a public global survey carried out by PWC Luxembourg on domiciles used by the top 50 cross-border management groups for their cross-border sales revealed that out of more than 76,500 cross-border fund registrations existing at end 2013, only 5 non-US funds were registered for distribution in the US.

358. Another respondent indicated that under current US regulation it is virtually impossible to market EU AIFs to US clients. Thus, when opening up to US AIFMs without requiring reciprocity, i.e. access to the US market, the EU puts EU AIFMs at a disadvantage: US AIFMs would swamp the EU market with the help of the passport while EU AIMFs would continue to lack access to the US. This respondent was of the view that AIFMD is the lever to change that.

359. This same respondent indicated that in addition to marketing to clients in many EU countries, they market their Lux UCITS in up to 12 non-EU countries. Apart from so-called local requirements (e.g. in Taiwan, Hong Kong, Singapore and Peru), they indicated that the most fundamental sales restriction is the US. They cannot market any of their Lux UCITS (or AIFs) to US residents due to a) registration (and other)

requirements under the US Company Act of 1933 (given they have more than 300 investors) and b) distribution to US person thus subject to CFTC, Volker rule i.e. burdensome regulation.

360. Another respondent indicated that they believed that the United States grants EU AIFMs and UCITS management companies access to the US market under conditions that are broadly equivalent to those granted by the EU.

361. Accessing EU Investors: They indicated that U.S. domiciled asset managers can obtain access to fund investors in the EU under the UCITS Directive (the regulatory framework for funds that are authorized and appropriate for sale to retail investors) and the AIFMD (the regulatory framework for managers of all funds other than UCITS that are marketed in the EU). They mentioned that to access investors under the UCITS Directive, a non-EU management company must establish (or domicile) a UCITS fund in the EU and also locate the management company of the fund in the EU. This respondent added that non-EU funds cannot be qualified as UCITS. They added that to market an EU or non-EU fund other than a UCITS to EU investors a non-EU asset manager must rely on the framework of the AIFMD, which is focused on professional investors. Currently, they mentioned that the marketing of non-EU funds must comply with certain provisions of the AIFMD and such funds may be marketed only as permitted under the individual Member State private placement rules. They also mentioned that member States can permit distribution of AIF to retail investors and can impose additional rules on such funds.

362. Accessing U.S. Investors: This respondent indicated that similar to a U.S. manager wishing to access the EU retail market, an EU management company that wishes to access the retail market in the U.S. is practically required to register a fund under the Investment Company Act of 1940. Such a fund must be domiciled in the U.S., and the investment manager must be registered under the Investment Advisers Act of 1940. This respondent indicated that there is no requirement that the investment manager be domiciled or have a geographic presence in the U.S. They added that to sell shares of a fund domiciled outside the U.S., a manager may sell such shares privately by relying on exemptions from certain U.S. laws, such as exemptions for limited offerings to institutional investors. Exemptions from registration as an investment adviser under the Investment Advisers Act of 1940 may also be available.

363. This respondent indicated that the Investment Company Institute in 2013 released a white paper on *Market Access for Regulated Fund Managers in the United States and the European Union* which discusses these issues in much more detail. The text of the Paper is available at http://www.ici.org/pdf/27643.pdf

364. Another respondent indicated that as noted by a recent Preqin study (The full text of the Preqin report is available at: https://www.preqin.com/docs/reports/Preqin-Special-Report-Hedge-Fund-Managers-Respond-to-AIFMD-July-14.pdf), a significant majority of non-EU managers do not intend to market to EU investors under national private placement regimes or establish an EU AIFM to take advantage of the AIFMD

passport. Consistent with those survey results, they have heard anecdotally from their members that there is not significant interest from non-EU managers in becoming fully authorised AIFMs if the EU extended the AIFMD passport to non-EU managers.

365. This respondent indicated that the with respect to U.S. managers, only 12% of managers indicated that they plan to market under national private placement regimes, and only 4% plan to establish an EU AIFM to take advantage of the AIFMD passport. Based on their anecdotal experience, this respondent does not believe that there would be substantially more interest from U.S. managers in becoming fully authorised AIFMs to be able to market under the AIFMD passport if it were expanded to non-EU AIFMs. Similarly, the Preqin study found that only 9% of non-EU managers outside of Switzerland and the U.S. plan to market under national private placement regimes, and only 9% plan to establish an EU AIFM to take advantage of the AIFMD passport. The Preqin study found that 78% of U.S. managers cited compliance costs or uncertainty about the AIFMD as the reason why U.S. managers do not plan to market their funds to EU investors. The study found that 42% of non-EU managers outside of Switzerland and the U.S. cited compliance costs or uncertainty about the AIFMD as the reason that they do not plan to market to EU investors. Similarly, this respondent indicated that the a June 2014 survey by Aksia found that a majority of hedge fund managers do not plan to market to EU investors and 87% of managers responded that they have faced significant challenges regarding the AIFMD (The full text of the Aksia report is available at: http://www.aksia.com/media/2015_HF_Manager_Survey.pdf).

366. This respondent indicated that taken together, the Preqin and Aksia studies confirm what they have heard anecdotally from their members; that compliance costs and legal uncertainty under the AIFMD are providing a significant disincentive to non-EU managers to operate in or market to EU investors. This respondent added that this is particularly true because non-EU managers must make a decision on whether to undertake the legal and compliance costs of complying with the AIFMD prior to knowing whether they will receive any investor subscriptions as a result of marketing efforts that bring the manager within the scope of the AIFMD.

367. Another respondent indicated that from a practical perspective, extending the Passporting Regime to US AIFMs will mean that professional investors in the European Union will continue to have access to AIFs managed by US AIFMs. This respondent indicated that European investors should be permitted, within an appropriate regulatory framework, full flexibility in choosing between investing with European AIFMs and US AIFMs. This respondent indicated that investment with US AIFMs serves a number of important functions for many European investors, including diversification of investment opportunities and access to attractive returns.[39]

[39] This respondent indicated that annualized returns generated by US private equity funds equalled 14.3% over the last ten years, according to the Q2 2014 US Private Equity Fund Index (Cambridge Associates). These annualized returns far exceed annualized returns that investors could have obtained by investing in various public market indexes: MSCI Europe Index (US$),

368. This respondent believed that not extending the Passporting Regime to US AIFMs would raise significant and important market access issues for US AIFMs and could seriously harm the interests of European institutional investors. Extension of the Passporting Regime to US AIFMs is important for ensuring that European AIFMs and US AIFMs have a “level playing field” in connection with the marketing of AIFs to European professional investors.

369. This respondent indicated that a European AIFM may market its AIFs organized outside the US to a prospective investor in the United States, *provided* that (*a*) the interests in the non-US AIFs are not offered in a public offering in the United States and (*b*) the interests in the relevant non-US AIF will be beneficially owned by either (*i*) not more than 100 US persons or (*ii*) with respect to investors that are US persons only, exclusively by “qualified purchasers” (as defined in Section 2(a)(51) of the Investment Company Act). Access to the US investor base is important for European AIFMs, just as access to the European investor base is important for US AIFMs.

370. This respondent indicated that the European Commission and the US Government have signed multiple cooperation agreements with respect to competition matters to enable effective collaboration and comity between the European Union and the United States.[40] Extending the Passporting Regime so that they apply to US AIFMs will not distort or undermine competition within the European Union.

371. This respondent indicated that the United States has one of the world’s most advanced competition regimes, referred to as “antitrust” law, which is primarily enforced by the US Department of Justice’s Antitrust Division and the US Federal Trade Commission. The US Sherman Act of 1890 and the US Clayton Antitrust Act of 1914 prohibit cartels and monopolists that impose unreasonable restraints of trade which are harmful to consumers. Accordingly, this respondent indicated that the aims, objectives and structure of the US antitrust regime are broadly similar to articles 101 and 102 of the Treaty on the Functioning of the European Union.

372. <u>Another respondent</u> indicated that regarding specifically the regulation of AIFMs and AIFs, the regulations may be weaker in some third countries on some points:

a. For instance in the US, this respondent indicated that investment advisers (acting in a way similar to asset management companies) may self-custody the assets they manage – and this possibility is still offered after the Madoff case. This respondent indicated that this flexibility generates lower costs for local players (and also a lower

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7.54% annualized returns over the past 10 years (as of 30 June 2014) (reported by Cambridge Associates); Russell 2000 Index, 8.70% annualized returns over the past 10 years (as of 30 June 2014 (reported by Cambridge Associates); S&P 500 Index, 7.78% annualized returns over the past 10 years (as of 30 June 2014) (reported by Cambridge Associates).

[40] For example: The Agreement between the Government of the United States of America and the Commission of the European Communities regarding the application of their competition laws, 27 April 1995; The Agreement between the European Communities and the Government of the United States of America on the application of positive comity principles in the enforcement of their competition laws, 18 June 1998; and, US-EU Merger Working Group – Best Practices on Cooperation in Merger Investigations, 14 October 2011.

protection for investors) as compared to the mandatory use of an external depositary;

b. This respondent indicated that regarding the asymmetry of requirements between EU countries and non-EU countries, we could take the case of hedge funds, regarding AIFM reporting vs. US private fund reporting: in the US, the reporting required by the CFTC, i.e. Form PQR, has to be done on a quarterly basis in any case, while in the EU AIFM Directive the quarterly reporting requirement has to be done only in some specific cases. More widely, it seems that the requirements of US federal agencies (including the SEC) are more demanding for non-US asset management companies as compared to those required for non-EU firms by the AIFM Directive.

c. This respondent indicated that there are regulatory barriers for selling investment funds in the US or even for the free investment in EU investment funds by US citizens at their own initiative. Following the adoption of the Dodd Frank Act, this respondent indicated that many EU asset managers are required to register with the SEC. And the consequence of registering with the SEC is that EU asset managers have to comply with the whole set of US regulations, plus with the SEC compliance book and federal reporting obligations. To avoid such a registration, this respondent indicated that some EU asset managers decided to avoid selling their funds to US persons and developed disclaimers describing that their funds are not intended for US clients. To sum it up, this respondent indicated that either non-US firms decide to market their funds and services in the US but then they have to comply with the whole set of federal rules, or they cannot access the US market. From this perspective, this respondent indicated that in the view of our members the US regime is more cumbersome than the EU regime, which ends in practice with unfair market access.

d. This respondent indicated that Section 7(d) of the Investment Company Act prohibits the public offering to US investors of funds domiciled outside the US.

e. This respondent also indicated that foreign managers are required to register with the SEC to provide services (collective investment fund management or discretionary portfolio management) in the US[41]. And such registration has for consequence that the registered entities

[41] This respondent indicated that the definition of investment advisers set out in Section 202(a)(11) of the Investment Advisers Act of 1940 is very wide. Section 203 states that all investment advisers who make use of U.S. mails, etc. have to be registered with the US authorities, unless they can find an exception applicable to them. The rule then lists a large number of exceptions. However, there is no exception for a “mutual fund”, so an adviser or sub-adviser of a mutual fund has to be registered with the SEC. A foreign entity managing a US fund is required to register with the SEC as it is considered as performing an activity as defined in Section 202(a)(11), unless it can benefit from the “foreign private adviser”, the “private adviser” or the “venture capital” exemptions.

have to comply with the whole set of US rules - in addition to the whole set of EU rules. It is in practice a big impediment to access the US market. Moreover, even in the case of cross-border management delegation, it is impossible for a US asset manager to delegate the management of a US fund to a European asset manager if the European asset manager has not been registered at US level – while the reverse is not required by EU regulations

373. This respondent also indicated that a public global survey carried out by PWC Luxembourg provided the identity of the different domiciles used by the top 50 cross-border management groups for their cross-border sales. It appears that out of more than 76,500 cross-border fund registrations existing at end 2013, only 5 non-US funds were registered for distribution in the US[42]. Considering that the US fund market represents around 50% of the overall fund market at worldwide level, we may wonder why so few foreign funds are registered for distribution in the US.

374. Another respondent indicated that:

375. For investment management services (i.e. MiFID activity in EU-speak; "investment advice" in US-speak), non US managers have to register with the SEC. While it may be considered by some managers as a reasonable requirement and not draconian or difficult to secure (for instance, many UK managers are appointed investment advisers for mutual funds), such a registration may be seen by others as a barrier. It has been experienced that a strong barrier is the obligation for EU managers to register at US level to be allowed to receive a delegation from a US manager;

376. Any foreign manager which provides investment management or investment advice (as an adviser or sub-adviser or manager or sub-manager) to a "mutual fund" (i.e. fund registered with the SEC for public distribution) must be registered with the SEC.

377. Foreign managers are required to register with the SEC unless they can rely on the "foreign private adviser" exemption from registration (i.e., having fewer than 15 US clients or US investors in funds and AUM from those clients/investors of less than $25 million, and manager cannot hold itself out to the US public as an investment manager).

378. Foreign managers which only manage foreign funds with US investors (and no US managed accounts) may be able to rely on the "private fund adviser" or "venture capital adviser" exemptions. Such firms are called "exempt reporting advisers". They must file with and report information to the SEC but are not subject to the full registration and compliance regime for SEC-registered advisers.

[42] « Benchmark your Global Fund Distribution 2014", PWC Luxembourg, 2014

379. It is impossible for a US asset manager to delegate the management of a US mutual fund to a European asset manager if the European asset manager has not been registered at US level.

380. Several exemptions from CFTC regulation are available for SEC-registered investment advisers, but an investment manager engaging primarily in derivatives should consider CFTC requirements.

381. As for the sale of foreign funds in the US:

- There are regulatory barriers for selling investment funds in the US or even for the free investment in EU investment funds by US citizens at their own initiative (e.g. following the adoption of the Dodd Frank Act, EU asset managers developed disclaimers describing that their funds are not intended for US clients).
- Section 7(d) of the Investment Company Act of 1940 prohibits the public offering of funds domiciled outside the US. Non-US funds can only be sold on a private placement basis in reliance on an exception under the Investment Company Act. A fund must comply with one of the following: (i) limit of 100 US persons in the non-US fund, or (ii) sales only made to "qualified purchasers" (generally, individuals with $5 million in investments or entities with $25 million in investments). A fund must choose to rely on either (i) or (ii) and cannot mix the two exemptions.
- It is a lengthy and burdensome process to bring a fund and its offering documentation into compliance with SEC public offer requirements and to meet significant ongoing compliance, governance, and reporting requirements for a fund offered to the public in the United States (initial legal fees in excess of USD 200,000 and ongoing compliance, operational, and other related expenses that could well exceed USD 200,000 annually).

382. Shares of non-US funds must be sold based on an exemption from registration under the Securities Act of 1933 (on a private placement basis, generally to investors who are "accredited investors" under Regulation D (generally an individual with net assets of $1 million or income for last 2 years of at least $200,000 annually, or an entity with net assets of $5 million).

383. Funds being sold on a private placement basis must file a Form D with the SEC and state securities regulators.

384. If the non-US fund is marketed to public pension plans subject to the US Employee Retirement Income Security Act of 1974 (ERISA), the fund must ensure that total ERISA benefit plan investment is kept below 25% of any class, or the manager to the fund may be deemed to be a fiduciary subject to ERISA.

385. Local offering for clearing and settlement is extremely difficult for foreign entities (self-clearing license requirements).

386. There are some market practices limitations: foreign funds must be NSCC eligible (incorporation is lengthy process) and trading of offshore funds through major platforms is less cost effective and all settlements are USD driven;

387. With regard to operational barriers, Joining DTCC as a member is a long and heavy process.

388. Afterwards, the funds (to be available for the offshore space only) need to be NSCC eligible. This implies a specific IT protocol to be developed;

389. As per their knowledge the entire process does not take less than 6-9 months;

390. Other US rules apply, such as:

- "U.S. Shareholder" rules as described in the Code which de facto limit US investors to less than 10% of the foreign fund's share capital;
- Controlled Foreign Corporation rules (CFC) which may also limit US ownership.

391. In relation to the taxation regime of the U.S, one respondent indicated that as for Tax barriers in the U.S, there was the PFIC Regime: Non-U.S. corporate funds are "passive foreign investment companies" ("PFICs"). U.S. taxable investors investing in non-US funds will prefer an investment structured as a partnership. US taxable investors investing in a PFIC are subject to a more disadvantageous tax regime than if they invest in a U.S.-domiciled fund or a non-U.S.-domiciled partnership. A fund can take steps to assist investors to comply with certain PFIC reporting obligations.

392. Another respondent indicated that As for Tax barriers, PFIC Regime: Non-U.S. corporate funds are "passive foreign investment companies" ("PFICs"). U.S. taxable investors investing in non-US funds will prefer an investment structured as a partnership. US taxable investors investing in a PFIC are subject to a more disadvantageous tax regime than if they invest in a U.S.-domiciled fund or a non-U.S.-domiciled partnership. A fund can take steps to assist investors to comply with certain PFIC reporting obligations.

Annex 3. Summary of the feedback from the call for evidence in the case of Guernsey

Overall summary of the feedback from the call for evidence

Investor protection

393. In relation to the comparison between the Guernsey regulatory framework and the AIFMD, one respondent indicated that the Guernsey Financial services Commission is the regulatory body for the finance sector in the Bailiwick. They mention that the Commission's primary objective is to regulate and supervise financial services in the Bailiwick, with integrity and efficiency, and in so doing help to uphold the international reputation of the Bailiwick as a finance centre. The Commission is the only financial services regulator within the Bailiwick.

394. They indicated that the Commission is committed to international regulatory co-operation and is a signatory to the IOSCO MMoU and the IAIS MMoU. They added it also has numerous bilateral regulatory co-operative agreements in place; and, through ESMA, has in place MoUs covering AIFMD with 27 members of the EEA. They mentioned that Commission ensures the Bailiwick's regulatory framework and practice meets international standards and is a committed participant in discussions of international standards. It does so through membership of, or association with, the following international organizations: IOSCO, IAIS, GIICS, GIICS, OCDE (though the UK), Moneyval and works with BIS, FATF.

395. This respondent further indicated that the investment business regulatory framework in Guernsey was the following:

396. Investment business is regulated under the POI Law. The FSC Law transferred to the Commission the functions in relation to the authorisation and registration of open-ended collective investment funds and closed-ended collective investment funds, the making of rules in relation to such funds and the regulation of authorised and registered collective investment funds under the POI Law. It also transferred to the Commission the functions in relation to the licensing of persons to carry on controlled investment business under the POI Law, the making of rules in respect of such licensees and the regulation of controlled investment business under the POI Law.

397. In 2013 the Bailiwick created an AIFMD focused regime for those AIFMs and AIFs which market into the EU. There are two aspects to the Bailiwick's AIFMD focused regime, the first being The AIFMD (Marketing) Rules, 2013, which ensure that Guernsey AIFMs established in Bailiwick who wish to market into the EU meet the requirements of Articles 42 and 43 of AIFMD. These Rules also introduced notification requirements to the Commission which assist the Commission in co-

operating effectively with EU Competent Authorities. These Rules became effective on 22 July 2013.

398. The second part of the Bailiwick's AIFMD focused regime is an equivalent AIFMD opt-in regime for Guernsey AIFMs and Depositaries, which is predominantly based on the Level 1 Directive. The AIFMD Rules, 2013, governing this opt-in regime became effective from 2 January 2014. The Commission anticipates that the Bailiwick's proactive approach to AIFMD will assist ESMA with its advice on the application of the passport to third-country AIFMs and AIFs in accordance with the rules set out in Article 35 and Articles 37 to 41 of the AIFMD.

399. The legislation underpinning the Bailiwick's regulatory regime can be found at http://www.guernseylegalresources.gg/article/6325/Home.

400. This respondent further detailed the AIFM Licensing Requirements in Guernsey. It is as follows:

401. Any person carrying on the restricted activities of promotion, subscription, registration, dealing, management, administration, advising or custody in connection with controlled investment business or operating an investment exchange requires a licence from the Commission. Persons effectively conducting the business of an AIFM in or from within Guernsey must therefore be licensed under the POI Law.

402. The Commission shall not grant an application for a licence under the POI Law unless satisfied that the criteria specified in Schedule 4 to that law are fulfilled. Schedule 4 to the POI Law sets out the Minimum Criteria for Licensing and its provisions must be fulfilled in relation to the applicant for a licence and in relation to any person who is or is to be a director, controller, manager or partner of the applicant. A licensee, and any person who is or is to be a director, controller, manager or partner of the licensee, must continue to meet the Minimum Criteria for Licensing following the issue to it of a licence.

403. The Minimum Criteria for Licensing cover the following areas:

a. Fit and Proper Persons. The applicant or licensee is a fit and proper person to hold a licence and every person who is, or is to be, a director, controller, partner or manager of the applicant or licensee, is a fit and proper person to hold that position. In determining whether a person is a fit and proper person to hold a licence or a particular position the Commission has to give regard to various issues in respect of probity, competence, experience and soundness of judgement for fulfilling the responsibilities of that licence or as the case may be that position.

b. Integrity and Skill. The business of the applicant or licensee will be carried on with prudence and integrity and professional skill appropriate to the nature and scale of the activities undertaken and in accordance with the POI Law and applicable rules, regulations and other relevant enactments.

d. Business to be directed by at least two individuals. At least two individuals of appropriate standing and experience and who are sufficiently independent of each other are required to direct the business. This is referred to colloquially as “4 eyes.”

d. Composition of the Board of Directors. In the case of a company the board of directors shall include such number of executive and non-executive directors as the Commission considers appropriate having regards to the circumstances of the company and the nature and scale of its operations.

e. Business to be conducted in a prudent manner. The applicant or licensee must conduct its business in a prudent manner maintaining an appropriate capital base and insurance cover. The actual requirements regarding capital adequacy and insurance cover are set out in underlying rules made under the POI Law and which apply to all licensees under that legislation.

f. Information required by the Commission. The Commission may reasonably require any information for the purpose of assessing compliance with the Minimum Criteria for Licensing.

g. Conduct of Business and Capital Adequacy Rules. Underpinning the POI Law are rules relating to the conduct of business and capital adequacy, which apply to all licensees under the POI Law. In addition, Guernsey AIFMs and Depositaries which are conducting AIFMD related business with the EU also have the ability to opt-in to comply with The AIFMD Rules, 2013, which are predominantly based on the Level 1 Directive.

404.The respondent considered that for many years the aforementioned Minimum Criteria for Licensing has ensured that Guernsey AIFMs’ do not fulfil the attributes of a “letter box entity”; however, this respondent mentioned that this has been reinforced with the introduction of The AIFMD Rules.

405. Another respondent indicated that they thought the risks of extending the passport to non-EU AIFMs are likely to be low provided that the non-EU AIFMs operate in third countries with EU-equivalent regulatory environments (financial regulation, supervision, tax and anti-money laundering provisions). Jersey and Guernsey have implemented the necessary regulations to comply fully with the AIFMD. The successful introduction of the passport would provide investors’ a greater global choice of AIFMs and AIFs and could lead to a decreased concentration of systemic risk within.

406.This respondent added that the regimes in Jersey and Guernsey are both fully equivalent to the EU framework. Jersey and Guernsey have each implemented the necessary regulation to comply fully with AIFMD. This respondent mentioned that Jersey and Guernsey also meet the relevant AIFMD standards as regards compliance with international standards to counter money laundering and terrorist financing as required by the FATF and has committed to effective exchange of information in tax matters in compliance with the standards laid down in Article 26 of the OECD Model Tax Convention on Income and on Capital.

407. Another respondent indicated that both Jersey and Guernsey have a well-established and long-standing legal framework that underpin the fund regimes in both islands respectively and there are no such limitations in the legal framework in these countries that impede or limit an organisation from collaborating with an EU NCA. Both the Jersey and Guernsey NCAs were early signatories to the ESMA "MoUs" regarding regulatory co-operation with EU NCAs, and indeed assisted ESMA with the preparation of the model cooperation agreement that was subsequently rolled out to third country regulators worldwide. This respondent mentioned that the Jersey and Guernsey NCAs have each entered into cooperation agreements with all of the EEA member states that have opted in to AIFMD, with the exception of Spain, Italy, Slovenia and Croatia.

408. This respondent further mentioned that the Protection of Investors (Bailiwick of Guernsey) Law, 1987 (as amended provides the statutory structure for the regulation and administration of funds and fund managers in Guernsey. The AIFMD (Marketing) Rules, 2013 were brought into force by the Guernsey NCA with effect from 22 July 2013 for the express purpose of assisting the Guernsey NCA with cooperating with EU NCAs. Meanwhile in Jersey the regulation of funds and fund managers is underpinned principally by the Collective Investment Funds (Jersey) Law 1988, the Control of Borrowing (Jersey) Order 1958, the Financial Services (Jersey) Law 1998, the Alternative Investment Funds (Jersey) Regulations 2012 and the Alternative Investment Funds (Jersey) Order 2013 – this legislation provides a clear legal basis for collaboration between the Jersey NCA and a relevant NCA. In particular this expressly provides for the ability of the Jersey NCA to assist and to liaise with relevant NCAs. The respective laws detailed above provide for appropriate investor protection, regulatory oversight and disclosure. In both this respondent was of the view that Guernsey and Jersey a full review has taken place during 2012 and 2013 to ensure the laws provide for full collaboration with EU NCAs and that both Jersey and Guernsey have subsequently implemented a fully compliant AIFMD regulatory structure.

409. Another respondent indicated that the current regime in the Channel Islands is very similar to the EU. This respondent indicated that the legal and regulatory framework is Norman-French in origin but is heavily influenced by the United Kingdom (e.g. legal interpretation and principles, accounting and audit standards) and, in practice, is remarkably similar to what we see in Luxembourg, where there is commonly both manager and product based regulation and reporting (i.e. dual tiers). This respondent indicated that the framework in the Channel Islands is also increasingly being influenced directly by the EU in areas such as financial services, data protection and information exchange and co-operation. This respondent further indicated that Conduct of business rules apply to all regulated entities in the Islands, which are also subject to strict rules intended to counter money laundering and terrorist financing (based on guidance published from time to time by the Financial Action Task Force.

410. Another respondent indicated that Guernsey's fund management and administration industry is regulated by the GFSC and is widely recognised as a highly regulated jurisdiction, its main aim being the protection of investors. As one would expect with such a reputation, this respondent indicated that Guernsey has a robust infrastructure in place, with highly regulated local Depositaries, a number of which having some of the largest European and US banking parentage. This respondent further indicated that Given Guernsey's developed regulatory framework and infrastructure alike, by extending the passport to a non-EU jurisdiction such as Guernsey, they do not believe there is any risk to either market disruption or to investor protection.

411. Another respondent indicated that they would like to share with ESMA a pragmatic approach which acknowledges the realities of marketing of closed-ended AIF to international professional investors. In this approach, they also took into account similar AIFMD rules introduced by third country concerned. This respondent indicated that they identified three groups of third countries as described below:

First group: Implementation of third country passport. This group includes countries which have implemented AIFMD in their jurisdiction. The third countries concerned are mainly Switzerland and the Channel Islands (Jersey and Guernsey). Those countries made an effort to adopt the AIFMD legislation in their national legal system. They believed this is important to promote their approach. This is the reason why this respondent supported for those third countries the implementation of third country passport in accordance with AIFMD on the basis of equivalent rules.

412. Another respondent indicated that both Jersey and Guernsey have a well-established and long-standing legal framework that underpins the fund regimes in both islands respectively and there are no such limitations. This respondent indicated that both the JFSC and GFSC were early signatories to the ESMA MoUs regarding regulatory co-operation with EU NCAs, and indeed assisted ESMA with the preparation of the model cooperation agreement that was subsequently rolled out to third country regulators worldwide. This respondent indicated that the JFSC and GFSC have each entered into cooperation agreements with all of the EEA member states that have opted in to the AIFMD, with the exception of Spain, Italy, Slovenia and Croatia

413. This respondent further indicated that the Protection of Investors (Bailiwick of Guernsey) Law, 1987 (as amended) provides the statutory structure for the regulation and administration of funds and fund managers in Guernsey. The AIFMD (Marketing) Rules, 2013 were brought into force by the GFSC with effect from 22 July 2013 for the express purpose of assisting the GFSC with cooperating with EU NCAs. Meanwhile in Jersey the regulation of funds and fund managers is underpinned principally by the Collective Investment Funds (Jersey) Law 1988, the Control of Borrowing (Jersey) Order 1958, the Financial Services (Jersey) Law 1998, the Alternative Investment Funds (Jersey) Regulations 2012 and the Alternative Investment Funds (Jersey) Order 2013 – this legislation provides a clear legal basis for collaboration between the JFSC and a relevant NCA. In particular this respondent

indicated that this expressly provides for the ability of the JFSC to assist and to liaise with relevant NCAs.

414. This respondent indicated that the respective laws detailed above provide for appropriate investor protection, regulatory oversight and disclosure. In both Guernsey and Jersey a full review has taken place during 2012 and 2013 to ensure the laws provide for full collaboration with EU NCAs. This respondent indicated that both Jersey and Guernsey have subsequently implemented a fully compliant AIFMD regulatory structure.

415. Another respondent indicated that in recent years, significant non-EEA fund domiciles have strengthened both manager and fund related regulation with a focus around investors. For example, the Alternative Investment Funds (Jersey) Regulations 2012, AIFMD Rules 2013 in Guernsey, and Dodd-Frank in the U.S. This respondent mentioned that these regulations either incorporate the AIFM rules into the non-EEA fund regulations, or regulate the fund industry with the same effect as the AIFMD.

416. In relation to anti-laundering measures, another respondent indicated that Jersey and Guernsey are each treated as “equivalent” under the Anti-Money Laundering Directive (Directive 2005/60/EC). Jersey and Guernsey comply with the standards laid down in Article 26 of the OECD Model Tax Convention on Income and on Capital, as per Article 40(2)(c) of the AIFMD.

417. Another respondent indicated that:

418. In 2011, the IMF reported Guernsey as being compliant or largely compliant with 47 out of 49 of the FATF recommendations on Anti-Money Laundering (AML) and Countering the Financing of Terrorism (CFT); the highest standard of any jurisdiction so far assessed.

419. Compliance with the 49 FATF Standards based upon the most recent reviews of each jurisdiction;

420. Guernsey was one of the first places in the world to regulate trust providers;

421. Guernsey is recognised by the Securities and Exchange Commission (SEC) for providing a compliant, well regulated environment;

422. Guernsey is signed up to the International Organisation of Securities Commissions – Multilateral; Memorandum of Understanding (IOSCO) MMoU;

423. Businesses, including trust providers follow Know Your Client (KYC) and Anti Money Laundering (AML) procedures in line with international standards.

Competition and Market disruption

424. In relation to the access to the market, another respondent indicated that Jersey and Guernsey grant market access to EU AIFMs and UCITS management companies under equivalent conditions to their domestic AIFMs. This respondent indicated that EU AIFMs and UCITS management companies are subjected to the same regulatory requirements as Jersey or Guernsey AIFMs. Moreover, in practice, they added that the regulatory application process will take comfort from the domestic regulatory status of the EU AIFM or UCITS management company because the Jersey or Guernsey Financial Services Commission, as the case may be, will be able to co-operate with the respective EU competent authorities in accessing the fitness, propriety and track record of the principal persons of such companies. In respect of marketing activity, there were of the view that there are already well established regulatory regimes for the circulation in the Channel Islands of foreign fund prospectuses to Channel Island investors with no filing fees and short regulatory response timeframes.

425. Another respondent indicated that in relation to EU AIFMs and UCITS Management Companies managing AIFs established in the Bailiwick, there is no requirement for a Guernsey AIF to have a Guernsey AIFM. Consequently there is no restriction on EU AIFMs and UCITS Management Companies establishing AIFs in the Bailiwick. However, the Commission does insist that Promoters and/or Investment Managers, irrespective of their location, (including their directors, controllers and senior managers) must be fit and proper. This can be defined as being a requirement for integrity (or honesty), competence (or track record) and solvency.

426. This same respondent indicated that in relation to EU AIFMs and UCITS Management Companies managing AIFs established in the Bailiwick EU AIFMs and UCITS Management Companies marketing AIFs or UCITS in the Bailiwick:

427. General Promotional Requirements. Under the POI Law, promotion of collective investments schemes (including AIFs) is a restricted activity, which requires a licence. The POI Law defines promotion as i) advertising; ii) issuing a prospectus, application form or proposal form; and iii) circulating or making available promotional material. However, promotion of collective investments schemes (including AIFs) will not be regarded as an activity requiring a licence under the POI Law provided that the promoters have taken and can demonstrate that they have taken steps to ensure that any such promotion will be directed only to those firms supervised by the Commission. In these circumstances promotional material must make it clear that it is not for distribution to private investors, and invitations to promotional seminars must not be directed to private investors.

428. Licence Exemptions. Under Section 29(1) of the POI Law, the Investor Protection (Designated Countries And Territories) Regulations 1989 and the Investor Protection (Designated Countries And Territories) (Republic Of Ireland) Regulations 1992 ("the Regulations"), Designated Territory status has been granted to the UK, Jersey, Isle of Man and Ireland. An applicant carrying on business in relation to collective investment schemes with a main place of business in any of the above does not

require a licence under the POI Law to promote certain collective investment schemes (UCITS equivalent) in the Bailiwick, but must give prior notice to the Commission. The Regulations were drafted on the basis of reciprocity; therefore, the Commission will extend the Regulations to all Member States, should the passport be extended to Guernsey AIFMs and AIFs

429. This respondent argued that the Regulations were drafted on the basis of reciprocity; therefore, the Commission will extend the Regulations to all Member States, should the passport be extended to Guernsey AIFMs and AIFs

430. Another respondent indicated that in Guernsey EU AIFMs or UCITS management companies are not subject to heavier requirements than their non-EU competitors in order to do business in the EU. In Guernsey the NCA permits UCITs funds and equivalents to be promoted into Guernsey by distributors based in certain EU member states without the need (ordinarily required) to obtain a license from the NCA, provided such promotion is first notified to the NCA.

431. Another respondent indicated that UCITs funds and equivalents can be promoted into Guernsey by distributors based in certain EU member states without the need (ordinarily required) to obtain a license from the NCA, provided such promotion is first notified to the Guernsey NCA (the GFSC.

432. This same respondent indicated that the promotion of investment products and services in Guernsey is a restricted activity requiring a licence under the Protection of Investors (Bailiwick of Guernsey) Law, 187 (the 'POI Law'). The promotion of certain types of open-ended funds is exempted from the licensing requirements and, in addition bilateral agreements are in place with certain jurisdictions providing for mutual recognition of funds. These agreements do not confer an automatic right to promote funds into Guernsey but authorised schemes may be promoted into Guernsey where they have been registered with the GFSC and the appropriate fee paid.

433. In relation to the taxation regime in Guernsey, another respondent indicated that investment funds are not typically taxed in the Channel Islands as in the EU; especially partnership arrangements which are generally tax transparent in any event. The taxation of fund 'functionaries' depends on the extent to which they carry on an actual business in the Islands. Low rates of 'general' taxation in the Islands means that they do not typically benefit from international tax treaty access in the same way as Luxembourg or the Netherlands do (with a resulting loss of business). In reality though, these 'low' rates are little different from the 'actual' rates of taxation really applied in many Member States.

434. Another respondent indicated that:

- In December 2012, Guernsey's corporate tax regime was given a seal of approval as being fully ratified as compliant by the EU Code of Conduct Group on Business Taxation which had undertaken a review of the Island's tax regime;

- Guernsey's right to raise its own taxes is a long established constitutional principle;

- Guernsey has signed 57 Tax Information Exchange Agreements (TIEAs) to date including with 21 EU countries and 16 G20 countries;

- To date Guernsey has signed 13 Double Taxation Agreements;

- On the signing of Guernsey's 50th TIEA in November 2013, Pascal Saint-Amans, the OECD's; Head of Global Tax Policy, commented: "Guernsey has been one of the most active jurisdictions promoting transparency in practice. The number of TIEAs signed so far seriously enhances Guernsey's reputation as a responsible and transparent financial centre, as recognised by the Global Forum peer review.";

- Guernsey is a member of the OECD's 'whitelist' established in 2009 making it one of only 40 jurisdictions placed on the original list;

- Guernsey has been automatically exchanging information under the EU Savings Tax Directive for a number of years now, ahead of many of our competitors and indeed some of the countries of the EU, e.g. Luxembourg will move to automatic exchange from 1 January 2015. Austria still offers the withholding tax option instead of automatic exchange of information.

Annex 4 Summary of the feedback from the call for evidence in the case of Jersey

Overall summary of the feedback from the call for evidence

Investor protection

435. In term of cooperation with the EU NCAs, one respondent indicated that the Jersey Financial Services Commission has co-operated and will co-operate with other regulators to provide assistance in relation to on-site visits by other regulators and has undertaken joint on-site visits with other regulators. They were not aware of any enforcement action against Jersey regulated entities in respect of AIFMD.

436. This respondent also mentioned they were not aware of any limitations in the legal framework of Jersey that impede or limit them from collaborating with an EU NCA. They indicated Jersey Financial Services Commission has a wide range of powers to license, supervise and enforce the regulatory regime in Jersey. Moreover, they mentioned that Jersey Financial Services Commission is able to exercise these powers at the request of, or for the purposes of assisting, overseas regulatory authorities. They added that the Jersey Financial Services Commission's regulatory laws also provide gateways that enable the Jersey Financial Services Commission to communicate any information held to another regulatory authority to assist that authority in the exercise of its supervisory functions.

437. The specific regulatory laws in relation to Jersey AIFMs and Jersey AIFs are the Financial Services (Jersey) Law 1998, the Collective Investment Funds (Jersey) Law 1988, the Alternative Investment Funds (Jersey) Regulations 2012 and associated subordinate legislation. They finally mentioned that the Enforcement and Supervision divisions of the Jersey Financial Services Commission continue to respond, in a timely manner, to requests for assistance from overseas supervisory authorities, taking any action locally that is required as appropriate.

438. In relation to specific investor's protection policy, this respondent indicated Jersey Financial Services Commission takes an active part in investor education in Jersey and also internationally through IOSCO Committee 8. The Jersey Financial Services Commission is concerned with the inappropriate marketing of complex financial products to retail investors and inadequate disclosure of AIFs to professional investors.

439. Between 2011 and 2013 this respondent indicated that the Jersey Financial Services Commission undertook its Review of Financial Advice (similar to the UK FCA's Retail Distribution Review) and implemented changes with effect from 1 January 2014 to

require that registered persons should be remunerated by charges that are explained to the client upfront and agreed with the client, rather than by commissions set by product providers.

440. This respondent added that the Jersey Financial Services Commission is implementing a financial education strategy which is designed to improve investors' understanding of investment risks. As part of this strategy, the Jersey Financial Services Commission has launched a portal on its website which is dedicated to investor protection (www.protectyourmoney.je). In addition to maintaining this website, the Jersey Financial Services Commission's current financial education activities include participating in an initiative to develop a programme of financial education for Jersey's secondary school children.

441. The aim of the financial education strategy is to reduce the risk of investors "mis-buying" financial products or services (including investment funds) which are inappropriate for their individual circumstances and may, in some cases, be fraudulent or illegal. This strategy complements the wider supervisory and enforcement activities of the Jersey Financial Services Commission which address the mis-selling of financial products and services.

442. This respondent indicated that the Jersey Financial Services Commission has a formal complaints process in relation to complaints against regulated financial service providers. The following link provides details of the complaints process: http://www.jerseyfsc.org/pdf/Complaints_against_regulated_service_providers_July_2012.pdf . 16 formal complaints were provided to the Jersey Financial Services Commission in relation to regulated fund service providers during the two year period from 1 January 2013 to 31 December 2014. Of those 16 complaints almost half of the concerns related to fund performance, with 2 relating to inappropriate marketing and the remainder relating to administrative matters.

443. In relation to the consequences of the possible extension of the AIFMD passport to non-EU AIFMs, from a regulatory perspective, noting full application to an EEA State would be required by a non-EEA AIFM, this respondent mentioned they expect that there will be increased co-operation between regulators and harmonisation of requirements, but that there will also be areas of regulatory duplication for non-EEA AIFMs and their AIFs.

444. They added that the risks of an extension of the AIFMD passport to non-EU AIFMs would be related to where the regulatory requirements on non-EEA AIFMs and their AIFs are not equivalent to those AIFMD regulatory requirements for EEA AIFMs and their AIFs and to where the adequacy of investor protection standards for non-EEA AIFMs and their AIFs is not equivalent to those AIFMD requirements for EEA AIFMs and their AIFs. They noted that this would not be a risk in Jersey but not all third countries may have implemented the requirements of AIFMD.

445. They mentioned that it will be critical for there to be a transparent and fair assessment process of third countries. From a regulatory perspective, they indicated they expect

that there will be increased co-operation between regulators but also incidences of regulatory duplication for non-EEA AIFMs and their AIFs.

446. They noted that full application to an EEA NCA would be required by a non-EEA AIFM and that this would mean that the EEA NCA has additional authorisation obligations and filing requirements which may require stream-lined processes and enhanced regulatory resources in order for effective regulation and investor protection to be achieved. This risk should and could be mitigated by the regulatory support and co-operation of the non-EEA NCA.

447. This respondent was also concerned about the unwieldiness of the passport regime, with the complex Member State of Reference provisions and the ability of a Member State to refer to ESMA even where they have no involvement with the AIF.

448. They finally indicated they would encourage maintaining and harmonising the NPPRs in conjunction with the implementation of the passport regime to non-EEA AIFMs and non-EEA AIFs. In relation to the implementation of the passport regime, such implementation should attempt to avoid where possible the delayed/partial implementation as experienced in the implementation of the NPPRs.

449. Another respondent indicated that the current regime in the Channel Islands is very similar to the EU. This respondent indicated that the legal and regulatory framework is Norman-French in origin but is heavily influenced by the United Kingdom (e.g. legal interpretation and principles, accounting and audit standards) and, in practice, is remarkably similar to what we see in Luxembourg, where there is commonly both manager and product based regulation and reporting (i.e. dual tiers). This respondent indicated that the framework in the Channel Islands is also increasingly being influenced directly by the EU in areas such as financial services, data protection and information exchange and co-operation. This respondent further indicated that Conduct of business rules apply to all regulated entities in the Islands, which are also subject to strict rules intended to counter money laundering and terrorist financing (based on guidance published from time to time by the Financial Action Task Force.

450. Another respondent indicated that both Jersey and Guernsey have a well-established and long-standing legal framework that underpin the fund regimes in both islands respectively and there are no such limitations. This respondent indicated that both the JFSC and GFSC were early signatories to the ESMA MoUs regarding regulatory co-operation with EU NCAs, and indeed assisted ESMA with the preparation of the model cooperation agreement that was subsequently rolled out to third country regulators worldwide. This respondent indicated that the JFSC and GFSC have each entered into cooperation agreements with all of the EEA member states that have opted in to the AIFMD, with the exception of Spain, Italy, Slovenia and Croatia

451. This respondent further indicated that the Protection of Investors (Bailiwick of Guernsey) Law, 1987 (as amended) provides the statutory structure for the regulation and administration of funds and fund managers in Guernsey. The AIFMD (Marketing) Rules, 2013 were brought into force by the GFSC with effect from 22 July 2013 for

the express purpose of assisting the GFSC with cooperating with EU NCAs. Meanwhile in Jersey the regulation of funds and fund managers is underpinned principally by the Collective Investment Funds (Jersey) Law 1988, the Control of Borrowing (Jersey) Order 1958, the Financial Services (Jersey) Law 1998, the Alternative Investment Funds (Jersey) Regulations 2012 and the Alternative Investment Funds (Jersey) Order 2013 – this legislation provides a clear legal basis for collaboration between the JFSC and a relevant NCA. In particular this respondent indicated that this expressly provides for the ability of the JFSC to assist and to liaise with relevant NCAs.

452. This respondent indicated that the respective laws detailed above provide for appropriate investor protection, regulatory oversight and disclosure. In both Guernsey and Jersey a full review has taken place during 2012 and 2013 to ensure the laws provide for full collaboration with EU NCAs. This respondent indicated that both Jersey and Guernsey have subsequently implemented a fully compliant AIFMD regulatory structure.

453. <u>In relation to the comparison between the AIFMD regime and the Jersey regulatory framework for funds and managers</u>, one respondent indicated that where AIFMD is applicable to the activities of a Jersey AIFM, a Jersey AIF, or a Jersey AIF Depositary, Jersey implemented the necessary regulatory infrastructure to comply fully with AIFMD from 22 July 2013. In this regard, the Jersey regulatory requirements are in line with the AIFMD requirements for private placement to EEA investors and in the event of a passport being available, or for those Jersey AIFMs who wish to be fully compliant earlier, in line with EEA AIFMD passport requirements. The Jersey Financial Services Commission further stated that:

454. The Collective Investment Funds (Jersey) Law 1988 and the Alternative Investment Funds (Jersey) Regulations 2012 legislate in respect of all Jersey AIFs, and the Financial Services (Jersey) Law 1998 in respect of fund services business and AIF services business and the Alternative Investment Funds (Jersey) Regulations 2012 legislate in respect of all AIFMs. In July 2013, the Jersey Financial Services Commission issued Codes of Practice for AIFs and AIF Services Businesses (which replicate the requirements of AIFMD and the Level 2 Regulations) and amended the Codes of Practice for Certified Funds and the Codes of Practice for Fund Services Businesses.

455. Different sections of the Codes of Practice for AIFs and AIF Services Businesses apply depending on whether the Jersey AIFM is subject to the Private Placement Rules or opts into the full regime. Where the Jersey AIFM is subject to the Private Placement Rules, Article 42 of the Level 1 AIFM Directive provides that only the transparency requirements relating to: Annual report; Disclosure to investors; and Reporting obligations to competent authorities (Articles 22 to 24 of the Level 1 AIFM Directive) will apply and, if within scope, Articles 26 to 30 of the Level 1 AIFM Directive setting out the obligations for Directive AIFMs managing Directive AIFs which acquire control of non-listed companies and issuers will also apply. The Codes

naturally apply in full where the Jersey AIFM opts in to the full regime. The Jersey Financial Services Commission also mentioned that it should be noted, due to additional requirements imposed by EEA States, that the requirements of any EEA State in relation to the Level 1 AIFM Directive and the Level 2 AIFMD Regulation also need to be considered separately and, to the extent applicable, complied with in addition to the requirements set out in the Codes of Practice for AIFs and AIF Services Businesses.

456. In relation to the required co-operation agreements, the Jersey Financial Services Commission indicated they were able to enter into 27 out of 31 AIFMD co-operation agreements, noting that some EEA States have not signed with Jersey nor with any third country.

457. Another respondent indicated that they thought the risks of extending the passport to non-EU AIFMs are likely to be low provided that the non-EU AIFMs operate in third countries with EU-equivalent regulatory environments (financial regulation, supervision, tax and anti-money laundering provisions). Jersey and Guernsey have implemented the necessary regulations to comply fully with the AIFMD. The successful introduction of the passport would provide investors' a greater global choice of AIFMs and AIFs and could lead to a decreased concentration of systemic risk within.

458. Another respondent indicated that they understand that both Jersey and Switzerland are developing AIFMD-compatible regimes, specifically to enable them to make use of AIFMD passports into the EU.

459. Another respondent indicated that both Jersey and Guernsey have a well-established and long-standing legal framework that underpin the fund regimes in both islands respectively and there are no such limitations in the legal framework in these countries that impede or limit an organisation from collaborating with an EU NCA. Both the Jersey and Guernsey NCAs were early signatories to the ESMA "MoUs" regarding regulatory co-operation with EU NCAs, and indeed assisted ESMA with the preparation of the model cooperation agreement that was subsequently rolled out to third country regulators worldwide. This respondent mentioned that the Jersey and Guernsey NCAs have each entered into cooperation agreements with all of the EEA member states that have opted in to AIFMD, with the exception of Spain, Italy, Slovenia and Croatia.

460. This respondent further mentioned that the Protection of Investors (Bailiwick of Guernsey) Law, 1987 (as amended provides the statutory structure for the regulation and administration of funds and fund managers in Guernsey. The AIFMD (Marketing) Rules, 2013 were brought into force by the Guernsey NCA with effect from 22 July 2013 for the express purpose of assisting the Guernsey NCA with cooperating with EU NCAs. Meanwhile in Jersey the regulation of funds and fund managers is underpinned principally by the Collective Investment Funds (Jersey) Law 1988, the Control of Borrowing (Jersey) Order 1958, the Financial Services (Jersey) Law 1998,

the Alternative Investment Funds (Jersey) Regulations 2012 and the Alternative Investment Funds (Jersey) Order 2013 – this legislation provides a clear legal basis for collaboration between the Jersey NCA and a relevant NCA. In particular this expressly provides for the ability of the Jersey NCA to assist and to liaise with relevant NCAs. The respective laws detailed above provide for appropriate investor protection, regulatory oversight and disclosure. In both this respondent was of the view that Guernsey and Jersey a full review has taken place during 2012 and 2013 to ensure the laws provide for full collaboration with EU NCAs and that both Jersey and Guernsey have subsequently implemented a fully compliant AIFMD regulatory structure.

461. Another respondent (a private equity fund administrator) indicated that their largest office is in Jersey, which has already adopted an AIFMD-compliant regime (the Alternative Investment Funds (Jersey) Regulations 2012) and keenly adheres to international best practice in matters of financial regulation, supervision, tax and anti-money laundering provisions. Jersey's 'USP' for private equity funds, is the jurisdiction's stability, infrastructure and close ties with / proximity to the United Kingdom. Jersey compliments well the position of London-based managers that have both European and international customers.

462. This respondent also mentioned that Jersey has a clear regulatory regime for the circulation of prospectuses related to local and international private equity funds. In relation to international funds, there are no filing fees, delays or other discriminatory obstacles.

463. Another respondent indicated that Jersey was the first third country to offer a fully compliant opt-in AIFMD regime and has reviewed its legislation to ensure that there are no obstacles for an EU NCA to perform its supervisory duties. This respondent indicated that Jersey's legislative and regulatory framework is robust and facilitates smooth co-operation between the EU and Jersey authorities.

464. This respondent further indicated that Jersey provides specialised cross-border banking, wealth management, investment and legal services. In an increasingly global world, there is growing demand for secure and efficient multinational transactions. This is particularly important for individuals and companies who are conducting business globally.

465. This same respondent indicated that there are no limitations in the legal framework in Jersey that impede or limit from collaborating with an EU NCA. Specifically, This same respondent indicated that Jersey has had long-standing statutory regimes for the regulation of funds and fund managers underpinned by laws principally including the Collective Investment Funds (Jersey) Law 1988, the Control of Borrowing (Jersey) Order 1958 and the Financial Services (Jersey) Law 1998. Under these regimes, This same respondent indicated that AIFs have been subject to regulatory certification (including codes of practice) and AIFMs have been subject to licensing (again including codes of practice) but subject in appropriate cases to exemptions or lighter

forms of consent. This same respondent indicated that in order to ensure compatibility with the regulatory supervision requirements of the AIFMD, a regulatory review was undertaken in 2012 and 2013, resulting in additional regulatory obligations such that all types of Jersey AIFs and AIFMs involved in marketing to professional investors in the EU are regulated by the Jersey Financial Services Commission (JFSC) on a basis consistent with the AIFMD.

466. This same respondent indicated that accordingly the statutory framework in Jersey (being, in relation to AIFMs, the Financial Services (Jersey) Law 1998, and in relation to AIFs being the Collective Investment Funds (Jersey) 1988 as underpinned specifically in relation to the AIFMD by the Alternative Investment Funds (Jersey) Regulations 2012 and the Alternative Investment Funds (Jersey) Order 2013) provides a clear legal basis for collaboration between the JFSC being the relevant regulatory authority in Jersey and a relevant NCA. In particular this same respondent indicated that this expressly provides for the ability of the JFSC to assist and to liaise with relevant NCAs.

467. This same respondent indicated that the Jersey Financial Services commission (JFSC) also has a long-standing track record of investor protection within Jersey as a matter of robust regulation. This respondent indicated that by way of illustration, they understand from JFSC data that 16 formal complaints were provided to the JFSC in relation to regulated fund services providers for the two year period 1 January 2013 to 31 December 2014. Of those 16 complaints almost half of the concerns related to fund performance, with 2 relating to inappropriate marketing and the remainder relating to administrative matters.

468. This respondent further indicated that where AIFMD is applicable to activities of a Jersey AIFM, a Jersey AIF, or a Jersey AIF Depositary, Jersey has had in place regulatory infrastructure to comply fully with AIFMD since 22 July 2013. In this regard, Jersey regulatory requirements are in line with AIFMD requirements for private placement to EEA investors and in the event of a passport being available, or for those Jersey AIFMs who wish to be fully compliant earlier, in line with EEA AIFMD passport requirements. The Collective Investment Funds (Jersey) Law 1988 and the Alternative Investment Funds (Jersey) Regulations 2012 Regulations cover all Jersey AIFs, the Financial Services (Jersey) Law 1998 covers fund services business and AIF services business and the Alternative Investment Funds (Jersey) Regulations 2012 cover all AIFMs. In July 2013, the Jersey Financial Services Commission issued Codes of Practice for AIFs and AIF Services Businesses (which replicate the requirements of AIFMD and the Level 2 Regulations) and amended the Codes of Practice for Certified Funds and the Codes of Practice for Fund Services Businesses.

469. Different sections of the Codes of Practice for AIFs and AIF Services Businesses apply depending on whether the Jersey AIFM is subject to the Private Placement Rules or opts into the full regime. Where the Jersey AIFM is subject to the Private Placement Rules, Article 42 of the Level 1 AIFMD provides that only the transparency requirements relating to an Annual report, disclosure to investors and reporting

obligations to competent authorities (Articles 22 to 24 of the Level 1 AIFM Directive) will apply and, if within scope, Articles 26 to 30 of the Level 1 AIFM Directive setting out the obligations for control of non-listed companies. This respondent indicated that the Codes naturally apply in full where the Jersey AIFM opts in to the full regime. To the extent that additional requirements are imposed by EEA States then these will need to be considered in addition.

470.This respondent further indicated that in relation to the required co-operation agreements the Jersey Financial Services Commission was able to enter into 27 out of 31 AIFMD co-operation agreements, noting that some EEA States have not signed with Jersey nor with any third country;

471.This respondent further indicated that Jersey is not listed as a Non-Cooperative Country and Territory by FATF; and the multi-lateral Convention on Mutual Assistance in Tax Matters came into force in Jersey on 1 June 2014. This respondent further indicated that further information is available on Jersey Government's website, which states that "The Jersey authorities are committed to numerous double tax agreements and information exchange programs". The Jersey Government's website provides information about these international tax agreements and explains how information may be requested. It details five main headings in relation to international tax agreements, namely: Automatic exchange of information and FATCA, Double taxation agreements, EU Savings Directive, the Multilateral Convention (international tax) and Tax information exchange agreements.

472.Another respondent indicated they would note that non-EU jurisdictions such as Jersey have taken affirmative steps to align their regimes with the AIFMD.

473.Another respondent indicated that they would like to share with ESMA a pragmatic approach which acknowledges the realities of marketing of closed-ended AIF to international professional investors. In this approach, they also took into account similar AIFMD rules introduced by third country concerned. This respondent indicated that they identified three groups of third countries as described below:

First group: Implementation of third country passport. This group includes countries which have implemented AIFMD in their jurisdiction. The third countries concerned are mainly Switzerland and the Channel Islands (Jersey and Guernsey). Those countries made an effort to adopt the AIFMD legislation in their national legal system. They believed this is important to promote their approach. This is the reason why this respondent supported for those third countries the implementation of third country passport in accordance with AIFMD on the basis of equivalent rules.

474.Another respondent indicated that in recent years, significant non-EEA fund domiciles have strengthened both manager and fund related regulation with a focus around investors. For example, the Alternative Investment Funds (Jersey) Regulations 2012, AIFMD Rules 2013 in Guernsey, and Dodd-Frank in the U.S. This respondent mentioned that these regulations either incorporate the AIFM rules into the non-EEA fund regulations, or regulate the fund industry with the same effect as the AIFMD.

475. In relation to anti-money laundering measures, one respondent indicated Jersey is not listed as a Non-Cooperative Country and Territory by FATF. It also noted that:

476. By virtue of a footnote included in the list of third countries that are currently considered as having equivalent AML/CFT systems to the European Union (published under the Common Understanding between Member States on third country equivalence under the Anti-Money Laundering Directive (Directive 2005/60/EC), Jersey may be considered as "equivalent" by Member States ;

477. Measures to prevent money laundering and terrorist financing that must be taken by financial institutions and designated non-financial businesses and professions are set out in the Money Laundering (Jersey) Order 2008 (the "Money Laundering Order"). The Money Laundering Order applies to any person who is carrying on financial services business (a term that is defined in Schedule 2 of the Proceeds of Crime (Jersey) Law 1999) in or from within Jersey, and any legal person established under Jersey law carrying on financial services business (wherever in the world that activity is carried on).

478. Another respondent (an asset manager) indicated that non-EU jurisdictions, such as Jersey, are already implementing AIFMD-compatible regimes in order to enable future use of an extended AIFMD marketing passport.

479. This respondent added that the regimes in Jersey and Guernsey are both fully equivalent to the EU framework. Jersey and Guernsey have each implemented the necessary regulation to comply fully with AIFMD. This respondent mentioned that Jersey and Guernsey also meet the relevant AIFMD standards as regards compliance with international standards to counter money laundering and terrorist financing as required by the FATF and has committed to effective exchange of information in tax matters in compliance with the standards laid down in Article 26 of the OECD Model Tax Convention on Income and on Capital.

480. Another respondent indicated that Jersey and Guernsey are each treated as "equivalent" under the Anti-Money Laundering Directive (Directive 2005/60/EC). Jersey and Guernsey comply with the standards laid down in Article 26 of the OECD Model Tax Convention on Income and on Capital, as per Article 40(2)(c) of the AIFMD.

481. Another respondent indicated that Jersey's compliance with international standards to counter money laundering and terrorist financing, as required by the Financial Action Task Force (FATF):

482. This respondent indicated that as referred to in a footnote included in the list of third countries that are currently considered as having equivalent AML/CFT systems to the European Union (published under the Common Understanding between member states on third country equivalence under the Anti-Money Laundering Directive (Directive 2005/60/EC), Jersey is treated as "equivalent" by member states of the EU.

483. This respondent further indicated that measures to prevent money laundering and terrorist financing to be taken by financial institutions and designated non-financial businesses and professions are set out in the Money Laundering (Jersey) Order 2008 (the "Money Laundering Order"). The Money Laundering Order applies to any person who is carrying on financial services business (a term that is defined in Schedule 2 of the Proceeds of Crime (Jersey) Law 1999) in or from within Jersey, and any legal person established under Jersey law carrying on financial services business (wherever in the world that activity is carried on). In addition This respondent indicated that it should be noted that: i) Jersey is fully aligned with the highest standards of the 3rd Anti-Money Laundering EU Directive; ii) Jersey was rated by the IMF in 2009 as a 'top division' international finance centre; iii) Jersey is well prepared for the periodic assessment of Jersey's compliance with international standards to counter money laundering and terrorist financing, as required by the Financial Action Task Force (FATF). Previously carried out by the IMF, the work will be carried out on this third occasion by MONEYVAL, a body of the Council of Europe, in January 2015.

Competition and Market disruption

484. As a general assessment, one respondent noted from industry feedback they received, that in their view, an eventual extension of the passport to non-EU AIFMs will improve competition and will provide a wider asset management choice for EEA and non-EEA investors, which in turn could reduce systemic risk in the EEA. This will also facilitate the continued investment of capital into the EEA.

485. From a regulatory perspective, noting full application to an EEA State would be required by a non-EEA AIFM, this respondent expected that there will be increased co-operation between regulators and harmonisation of requirements, but that there will also be areas of regulatory duplication for non-EEA AIFMs and their AIFs.

486. In relation to the access to the market, this same respondent indicated that if EU AIFMs and UCITS management companies want to establish a place of business in Jersey then the same regulatory requirements will apply as they do to a Jersey AIFM, however in practice the regulatory application process will take comfort from the regulatory status of the EU AIFM and UCITS management company as the Jersey Financial Services Commission will be able to co-operate with the respective EEA regulators in respect of the fitness, propriety and track record of the principal persons of such companies.

487. This respondent added Jersey has a well-established regulatory regime for the circulation in Jersey of non-Jersey fund prospectuses to Jersey investors. There are no filing fees and the application is subject to a short regulatory response timeframe, in practice normally no more than ten working days. The process can also be fast tracked where the fund is approved by another regulator and the consent granted may also be more flexible where such funds are subject to another regulator's approval. Within the Financial Services (Jersey) Law 1998 there is a specific Overseas Distributors exemption available for non-Jersey distributors of UCITS where

such distributors are financial service providers which are appropriately supervised by their relevant supervisory authority. The Jersey Financial Services Commission finally stated that it should be noted that it is not possible to set up a UCITS in Jersey as there is no third country element to the UCITS Directive.

488. In relation to the access to the market, on respondent indicated that Jersey and Guernsey grant market access to EU AIFMs and UCITS management companies under equivalent conditions to their domestic AIFMs. This respondent indicated that EU AIFMs and UCITS management companies are subjected to the same regulatory requirements as Jersey or Guernsey AIFMs. Moreover, in practice, they added that the regulatory application process will take comfort from the domestic regulatory status of the EU AIFM or UCITS management company because the Jersey or Guernsey Financial Services Commission, as the case may be, will be able to co-operate with the respective EU competent authorities in accessing the fitness, propriety and track record of the principal persons of such companies. In respect of marketing activity, there were of the view that there are already well established regulatory regimes for the circulation in the Channel Islands of foreign fund prospectuses to Channel Island investors with no filing fees and short regulatory response timeframes.

489. Another respondent indicated that in Jersey EU AIFMs or UCITS management companies are not subject to heavier requirements than their non-EU competitors in order to do business in the EU. In Jersey there is a statutory exemption from additional regulation by the NCA for EU based distributors of UCITs funds and equivalents. In addition it has a regulatory regime for the circulation of non-Jersey fund prospectuses within Jersey, which is subject to swift NCA approval, if necessary.

490. Another respondent indicated that Jersey is an important conduit for Foreign Direct Investment to the EU – for example, the 2013 Jersey's Value to Britain research found that Jersey is a conduit for nearly £0.5 trillion (€0.64 trillion) of foreign investment into the UK, comprising 5% of the entire stock of foreign owned assets (as at 2011), vividly highlighting Jersey's role as an investment gateway to Europe (source - Capital Economics research – Jersey's Value to Britain, 2013). This respondent indicated that Jersey is recognised by investors as having a significant depth and breadth of professional expertise which has been developed for over 50 years. This respondent also indicated that Jersey has a stable political and economic environment with an established infrastructure designed to support the needs of the investment management industry. This respondent indicated that International organisations with a presence in Jersey include BNP Paribas, Deutsche Bank, JP Morgan Chase, Citibank, Standard Bank, Royal Bank of Canada, State Street, UBS, and SG Hambros.

491. This same respondent indicated that there are no impediments to the application of the passport to the marketing of Jersey AIFs by EU AIFMs in EU member states and the management and/or marketing of AIFs by Jersey AIFMs and that Jersey is a well-

established jurisdiction for the formation of alternative investment funds and for the delivery of funds services, having provided such services for a number of decades.

492. In relation to Jersey taxation regime, one respondent indicated that:

493. Article 40(2)(c) of the Alternative Investment Fund Managers Directive refers to both bilateral and multilateral tax agreements for the effective exchange of information in tax matters and requires that all such agreements should fully comply with the standards laid down in Article 26 of the OECD Model Tax Convention on Income and on Capital;

494. The Tax Information Exchange Agreements entered into by Jersey with EU Member States are all in accord with the OECD Model Tax Convention on Exchange of Information on Tax Matters and this is consistent with Article 26 of the OECD Model Tax Convention on Income and on Capital;

495. This has been confirmed by the Global Forum on Transparency and Exchange of Information for Tax Purposes when assessing Jersey. The OECD/Council of Europe Convention on Mutual Administrative Assistance in Tax Matters provides for exchange of information on request in accord with the OECD Model Tax Convention on Exchange of Information on Tax Matters and the OECD Model Tax Convention on Income and on Capital.

496. The multi-lateral Convention on Mutual Assistance in Tax Matters came into force in Jersey on 1 June 2014; and

497. Further information is available on Jersey Government's website, which states that "The Jersey authorities are committed to numerous double tax agreements and information exchange programs". The following link: https://www.gov.je/TaxesMoney/InternationalTaxAgreements/Pages/default.aspx to the Jersey Government's website provides information about these international tax agreements and explains how information may be requested. The link details five main headings in relation to international tax agreements, those being: Automatic exchange of information and FATCA, Double taxation agreements, EU Savings Directive, the Multilateral Convention (international tax) and Tax information exchange agreements.

498. Another respondent indicated they have direct experience of marketing EU managed AIFs and/or UCITS into Jersey. This respondent indicated that their experience demonstrates that such third country does not impose excessively heavy requirements or restrictions on European asset managers and this respondent considered such country as already granting market access under broadly equivalent conditions.

499. Another respondent indicated that investment funds are not typically taxed in the Channel Islands as in the EU; especially partnership arrangements which are generally tax transparent in any event. The taxation of fund 'functionaries' depends

on the extent to which they carry on an actual business in the Islands. Low rates of 'general' taxation in the Islands means that they do not typically benefit from international tax treaty access in the same way as Luxembourg or the Netherlands do (with a resulting loss of business). In reality though, these 'low' rates are little different from the 'actual' rates of taxation really applied in many Member States. A simplified VAT regime (Goods and Services Tax (GST)) applies in Jersey.

500. Another respondent indicated that Jersey offers tax neutrality to investors which means they can pool investments from all over the world including the EU to finance projects globally efficiently and cost-effectively. This respondent indicated that Jersey's robust legal framework and sound judiciary offer protection to investors who might be uncomfortable investing directly into riskier countries. This respondent indicated that through their strong links with London, Jersey has deep access to capital markets for investment in infrastructure, telecommunications networks, machinery, buildings, homes and other physical capital to foster jobs and growth.

501. This same respondent indicated that_Article 40(2)(c) of the AIFMD refers to both bilateral and multilateral tax agreements for the effective exchange of information in tax matters and requires that all such agreements should fully comply with the standards laid down in Article 26 of the OECD Model Tax Convention on Income and on Capital. This respondent indicated that the Tax Information Exchange Agreements entered into by Jersey with EU member states are all in accordance with the OECD Model Tax Convention on Exchange of Information on Tax Matters and this is consistent with Article 26 of the OECD Model Tax Convention on Income and on Capital. This respondent indicated that this has been confirmed by the Global Forum on Transparency and Exchange of Information for Tax Purposes when assessing Jersey. This respondent indicated that in addition Jersey has been subject to the multilateral convention since 1 June 2014. The OECD/Council of Europe Convention on Mutual Administrative Assistance in Tax Matters provides for exchange of information on request in accord with the OECD Model Tax Convention on Exchange of Information on Tax Matters and OECD Model Tax Convention on Income and on Capital. This respondent indicated that it is clear from the Global Forum assessments that the multilateral agreement and the bilateral agreements are to be treated as having equal merit. More generally this respondent indicated that in respect of tax matters:

- Jersey has signed up to 36 Tax Information Exchange Agreements (TIEAs), with 8 under negotiation;
- Jersey has signed up to 8 Double Taxation Agreements with 14 under negotiation;
- Jersey was one of the first international finance centres to be placed on the Organisation for Economic Co-operation and Development's (OECD) "white list" as having implemented internationally agreed tax standards in 2009;

- The results of Jersey's 2011 OECD Peer Review found that 'Jersey's practices to date have demonstrated a responsive and cooperative approach';

- Jersey was one of the 51 'early adopters' in the signing of the Multilateral Competent Authority Agreement as a further step in the implementation of a new single global standard for automatic exchange of taxpayer information;

- Jersey sits on the Organisation for Economic Co-operation and Development's (OECD) Global Forum Working Group on automatic exchange of information as Vice Chair alongside Italy, the Netherlands, Colombia and India;

- Jersey supports the St Petersburg G20 Summit Leaders Declaration which covered tax avoidance by multinational companies, tax information exchange and the need to work with developing countries;

- Jersey is a supporter of the G8 Action Plan in enhancing the transparency of the ownership and control of legal persons and legal arrangements;

- Jersey is committed to automatic exchange of information under the EU Savings Directive which took effect on 1 January 2015;

- Jersey is not a member of the EU but is in customs union with the member states. Jersey pursues a "good neighbour" policy and has supported the EU by voluntarily entering into agreements on the taxation of savings income and the application of the Code of Conduct on Business Taxation;

- Jersey has signed intergovernmental agreements for improving international tax compliance with the USA for FATCA and with the UK for equivalent legislation;

- Jersey is a member of the Global Forum on Transparency and Exchange of Information for Tax Purposes;

- Jersey has been rated by the Global Forum as largely compliant, a rating that matches that of Germany, the UK and USA; and

- Jersey has joined the Multilateral Convention on Mutual Assistance in Tax Matters

Annex 5 Summary of the feedback from the call for evidence in the case of Hong Kong

Overall summary of the feedback from the call for evidence

Investor protection

502. In relation to the comparison between the AIFMD regime and the Hong Kong regulatory framework for funds and managers, one respondent indicated that Hong Kong's regulatory regime is of international standards. As noted from the IOSCO Objectives and Principles of Securities Regulation Detailed Assessment Report prepared by IMF in the context of the Financial Sector Assessment Program (FSAP) for Hong Kong that was published in July 2014, this respondent mentioned that Hong Kong has developed a sound framework for the regulation of securities markets, which exhibits a high level of implementation of the IOSCO principles. In particular, Hong Kong has been graded "fully implemented" on all IOSCO Principles for CIS (collective investment scheme) in the FSAP report. The full FSAP report is available at the IMF website: https://www.imf.org/external/pubs/cat/longres.aspx?sk=41750.0.

503. This respondent believed that, while some of the specific requirements in Hong Kong may not be identical with those under the EU framework, Hong Kong SFC-authorized funds offer substantially equivalent investor protection and are subject to comparable rules and regulations as UCITS funds that would lead to similar regulatory outcomes. The SFC has also entered into memoranda of understanding concerning consultation, cooperation and the exchange of information related to the supervision of AIFMD entities (AIFMD MoU) with competent authorities of 28 European Union or European Economic Area countries respectively. The AIFMD MoU provide a framework for mutual assistance in the supervision and oversight of managers of alternative investment funds that operate on a cross-border basis, and for exchange of information for supervisory and enforcement purposes in a manner consistent with and permitted by all applicable laws and requirements.

504. As a consequence, this respondent was of the view that the AIFMD passport arrangement should be extended to Hong Kong AIFs and funds managed by Hong Kong AIFMs so that they may be marketed to European non-public investors as currently EU AIFs and other funds managed by EU AIFMs may be marketed to non-public investors in Hong Kong through SFC licensed/registered intermediaries. This respondent also indicated that as UCITS funds which comply with the streamlined procedures may seek SFC authorization for public offering in Hong Kong, by way of reciprocity, this respondent would also like to seek similar treatment for marketing and distribution of Hong Kong domiciled SFC-authorized funds to public investors in Europe.

505. As a general assessment, one respondent indicated that Europe in general – and in particular the European countries where this respondent operates as regulated asset managers (France, Belgium, Netherlands, Ireland , Lux, UK, Sweden, Finland, Italy)- has put in place a very comprehensive regulatory set of rules which, by far, differ from what is existing in most non-European countries, with perhaps the exception of the US, HK, Australia and Canada, even though in some areas – for example the depositary regime- the local framework is less protective for investors than what they know in Europe. In most countries, the level of requirements and the level of supervision is lacking behind Europe, not for everything, but for some aspects, leading to less compliance costs, allowing more leeway or more flexibility, if not taxation advantages.

506. As a general statement, another respondent indicated that they are aware of some potential issues in Hong Kong in relation to specific limitations in the legal framework in your country that impede or limit your organisation from collaborating with an EU NCA, but there is a pending consultation on regulatory changes to change the laws there to ensure the SFC is able to comply with the required cooperation arrangements.

Competition and Market disruption

507. In relation to the access to the market, one respondent indicated that Hong Kong is a favourable location for conducting asset management business in the Asian region. This respondent indicated that this industry in Hong Kong encompasses all types of fund management business activities including portfolio management, sales and marketing and fund administration and advisory. The number of licensed professionals with expertise in the asset management industry's core functions continues to increase resulting in a variety of investment funds made available to retail and professional investors in Hong Kong.

508. This same respondent indicated that a fund manager providing portfolio management services in Hong Kong is required to be licensed for Type 9 regulated activity (on asset management). On distributing and selling of CIS in Hong Kong, where marketing of the CIS to potential investors is involved, a licence for Type 1 regulated activity (on dealing in securities) is required as CIS are regarded as securities. If an EU management company does not provide any asset management services in Hong Kong, it is not required to be licensed or registered with the Hong Kong Securities and Futures Commission (SFC), although it must distribute its fund products through SFC licensed/registered intermediaries.

509. This respondent further mentioned that CIS that are offered to the public in Hong Kong are required to obtain prior authorization from the SFC, even if the CIS has been authorized by a foreign regulator, unless an exemption applies. The SFC, in general, adopts an open architecture towards admitting and authorizing overseas funds that wish to offer their products to the retail public in Hong Kong, bearing in mind investors' interests. The guiding principle is that the legal and regulatory

framework for these funds and the enforcement of investors' rights in a particular overseas jurisdiction should provide a level of investor protection comparable to that offered in Hong Kong.

510. This respondent indicated that the SFC has already authorized UCITS funds for public offering in Hong Kong for many years. Applications for authorization of UCITS funds domiciled in a number of European jurisdictions have been processed under streamlined procedures by the SFC since the commencement of its operations in 1989. UCITS funds which comply with the streamlined procedures may seek SFC authorization for public offering in Hong Kong. Currently, about 1,300 UCITS funds domiciled in Luxembourg, Ireland and the UK are authorised by the SFC for public offering in HK, representing 65% of the total public funds in Hong Kong in number.

511. This respondent also indicated that AIFs and/or UCITS that are offered to professional investors or a private placement basis in Hong Kong need not obtain prior authorization from the SFC, although these fund products must be distributed through SFC licensed/registered intermediaries subject to applicable laws and regulations.

512. Another respondent indicated that Hong Kong, in relation to funds, not to asset managers, would be in the situation where the non-EU country grants market access to EU AIFMs and UCITS management companies under broadly equivalent conditions.

513. Another respondent indicated they have direct experience of marketing EU managed AIFs and/or UCITS into Hong Kong. This respondent indicated that their experience demonstrates that such third country does not impose excessively heavy requirements or restrictions on European asset managers and this respondent considered such country as already granting market access under broadly equivalent conditions.

514. Another respondent indicated that The Hong Kong market has been for long an important market for them. They indicated it is one of the most accessible among non-EU countries.

515. Another respondent indicated that in addition to marketing to clients in many EU countries, they market their Lux UCITS in up to 12 non-EU countries. There are some so-called local requirements including in Hong Kong.

516. Another respondent indicated that i) Entities seeking to perform investment management and distribution activities in HK will need to be licenced by the SFC and need an appointed Hong Kong representative ii) Only Luxembourg, Irish, French, German and UK funds can seek registration in HK. The Securities and Futures Commission, SFC, designated certain jurisdictions as "acceptable inspection regimes" ("AIRs"). If the investment manager is not located and authorised in an AIR, the SFC are highly unlikely to license the entity iii) The use of derivatives for investment purposes can lead to difficulties when trying to register a fund for

distribution in HK iv) The authorisation process to distribute a new UCITS in Hong Kong can take up to 9 months v) The SFC accepts the UCITS III restrictions but will typically impose far greater disclosure obligations in relation to funds than European regulators vi) Post-authorisation: compliance with ongoing regulatory requirements can be challenging, particularly when seeking to coordinate changes (and the timetable) amongst the home regulator and SFC.

Annex 6 Summary of the feedback from the call for evidence in the case of Switzerland

Overall summary of the feedback from the call for evidence

Investor protection

517. In relation to the comparison between the AIFMD regime and the Switzerland regulatory framework for funds and managers, one respondent indicated that Switzerland has implemented the AIFMD standards in its system of regulation. Therefore, Switzerland grants market access to EU AIFMs (as well as to UCITS management companies). Hence, this respondent was of the view that Switzerland is ready for EU market access. Despite the lack of an explicit equivalence requirement, Switzerland has already implemented all AIFMD standards in its regulation to ensure that it meets the market access condition.

518. This same respondent mentioned that to a large extent, there is equivalence between the Swiss regulatory regime and the EU regulatory regime. They indicated the following:

Revision of the Collective Investment Schemes Act

519. On 1 March 2013, most of the provisions of the revised Collective Investment Schemes Act (CISA) and of the consequently amended Collective Investments Schemes Ordinance (CISO) entered into force. One of the main objectives of the revision was to close gaps in Swiss regulation resulting from the continued development of international standards, in line with the EU's Alternative Investment Fund Managers Directive (AIFMD).

520. General authorization requirement for asset managers of collective investment schemes: Modelled on the AIFMD, the scope of the CISA was extended to cover all asset managers of collective investment schemes, i.e. in particular, it now also covers "persons who manage *foreign collective investment schemes* in or from Switzerland" (Art. 2 para. 1 let. c CISA). The authorization requirements have been increased in some cases, and brought in line with the requirements under the AIFMD.

521. De minimis exceptions. As is the case with the AIFMD, the CISA also has a de minimis rule. Art. 2 para. 2 let. h CISA sets out rules exempting asset managers of collective investment schemes from the requirement to obtain authorization pursuant to Art. 13 para. 2 let. f CISA, provided certain conditions are met. First and foremost, the investors in the collective investment scheme have to be qualified investors. Article 1b CISO also sets out principles for the calculation of the relevant thresholds. Unlike the AIFMD, the CISA does not provide for an exemption to the authorization requirement for cases in which the thresholds are occasionally exceeded. Hence the CISA is stricter than European regulation in this respect

522. Authorization requirements: The partial revision of the CISA added some more detailed provisions on the capital requirements of an asset manager and on the appropriate organizational structure. The new Art. 12a CISO contains some significant provisions on organizational structure. As in the AIFMD, the asset manager must ensure it has proper and appropriate risk management, an internal control system and a compliance system covering its entire business activities.

523. Custodian banks: The partial revision of the CISA led to more specific and stricter requirements regarding the custodian banks of Swiss collective investment schemes. The new and amended provisions are aimed at improving investor protection and adopting international standards (in particular AIFMD), and also continue to allow Swiss custodian banks to perform the safekeeping of fund assets for foreign collective investment schemes if delegated to them.

524. The CISA previously contained only general provisions regulating the organization and activity of custodian banks, and more specific detail has been added as part of the partial revision of Swiss collective investment schemes legislation. In particular, detailed provisions have been adopted which require the custodian banks (like all CISA licensees) to ensure that it has an appropriate risk management, an internal control system and a compliance system, with the corresponding separation of functions from the operating units (Art. 12a and Art 102a et seq. CISA, Art. 77 et seq. CISO-FINMA). Furthermore, new detailed provisions with regard to the duties of the custodian bank in general and to the delegation of safekeeping have been implemented in the CISO in order to align the respective rules with the AIFMD (Art. 104 and 105a CISO). For example, specific duties regarding the timely settlement of transactions, the safekeeping of assets held in custody and the ownership verification and record keeping have been implemented (Art. 104 para 1 CISO). Moreover, it has been specified, in Art. 105a CISO, that a custodian bank must, when it delegates the safekeeping of assets to a third-party custodian, i.a., verify and monitor whether the latter possesses an appropriate organisational structure and the specific qualifications required and whether it is subject to external audits.

525. In addition, the liability of custodian banks of Swiss collective investment schemes was increased in order to largely approximate the liability of a custodian bank to the standard as set forth by the AIFMD. According to Art. 145 para. 3 CISA, if a custodian bank assigns the fulfillment of a task to a third party, it is liable for the losses caused by that third party unless it proves that it applied the degree of due diligence required in the given circumstances with regard to selection, instruction and monitoring (reversal of the burden of proof). Furthermore, the safekeeping of financial instruments may, in general, be transferred only to regulated third-party custodians and collective securities depositories (Art. 73 para. 2^{bis} CISA).

526. When adopting the liability regime as set forth in Art. 145 para 3 CISA, the legislator took, i.a., into consideration that, in 2010, Switzerland enacted a new Intermediated Securities Act (FISA) which regulates the custody of certificated and uncertificated assets by custodians and ensures the protection of property rights of investors (Art. 1

FISA). This act strenghtens the position of investors (such as collective investment schemes) vis-à-vis their custodians (e.g. Art. 17 FISA states that, if a custodian bank is subject to cumpulsory liquidation, the investors' securities are excluded *ex officio* from the custodian's estate).

527. Although the Swiss regulatory liability regime for the losses of financial instruments by the custodian bank of Swiss collective investment schemes has not been completely aligned to the regime set forth by the AIFMD, the above described recent adaptations to the Swiss legislation have the same effect, because, in practice, the liability of the custodian bank may be contractually increased between the fund, the depositary, and the sub-depositary.

528. Remuneration policy. This respondent mentioned that the ESMA Guidelines state that when delegating portfolio management or risk management activities according to Article 20 of the AIFMD, the AIFM must ensure that: i)the entities to which portfolio management or risk management activities have been delegated are subject to regulatory requirements on remuneration that are equally as effective as those applicable under these Guidelines; or ii) appropriate contractual arrangements are put in place with entities to which portfolio management or risk management activities have been delegated in order to ensure that there is no circumvention of the remuneration rules set out in the present Guidelines. These contractual arrangements should cover any and all payments made to the delegates' identified staff as compensation for the performance of portfolio or risk management activities on behalf of the AIFM.

529. Where asset management is outsourced to Switzerland, these provisions already apply today. Swiss AIFMs will have to comply with the AIFMD once the AIFMD passport is available for third countries. However, Switzerland already has rules in place today that provide equivalence (cf. SFAMA Code of Conduct, margin no. 43 which refers to FINMA Circular 2010/1 Minimum standards for remuneration schemes of financial institutions.

530. In addition, this same respondent indicated that FINMA, which is responsible for the prudential and conduct oversight of banks, insurance companies, exchanges, securities dealers, *collective investment schemes*, distributors and insurance intermediaries in Switzerland, is in a position to ensure that it can perform its supervisory functions. This respondent mentioned that according to ESMA, Switzerland has "effective on-going supervision and enforcement". Moreover, This respondent mentioned that according to ESMA assessment and evaluation regarding the regulatory equivalence under EMIR "The Swiss financial supervisory regime is robust with a track record of effective supervision of financial markets including during the recent financial crisis" [43].

[43] " Final report / Technical advice on third country regulatory equivalence under EMIR – Switzerland ", ESMA, September 2013

531.Another respondent indicated that they understand that both Jersey and Switzerland are developing AIFMD-compatible regimes, specifically to enable them to make use of AIFMD passports into the EU.

532.Another respondent noted that non-EU jurisdictions such as Switzerland, Jersey and the Cayman Islands have taken (or plan to take) affirmative steps to align their regimes with the AIFMD.

533.In relation to anti-money laundering measures, one respondent indicated that Switzerland attaches great importance to the integrity of its financial centre. This respondent mentioned Switzerland is engaged in developing standards aimed at fighting money laundering and terrorist financing at the international level and applies them consistently at the national level. Switzerland actively supports the fight against money laundering at a multilateral level. It is particularly involved in the Financial Action Task Force against Money Laundering and Terrorist Financing (FATF). By swiftly implementing the revised FATF recommendations (Financial Action Task Force), Switzerland is underscoring that it attaches high priority to its international obligation.

534.This same respondent added that the Federal Council adopted the dispatch on the new Federal Act for Implementing the Revised FATF Recommendations in December 2013. The aim was to combat money laundering and terrorist financing even more efficiently. The Swiss Parliament approved the bill with minor changes in December 2014. The revised legislation will come into force in 2015. Therefore the revised FATF Recommendations have now been transposed into national law.

535.Another respondent indicated that non-EU jurisdictions, such as Switzerland, are already implementing AIFMD-compatible regimes in order to enable future use of an extended AIFMD marketing passport.

536.Another respondent indicated that the Swiss legislation on Collective Investment Schemes (CIS) currently in force is in line with the EU CIS regulation. In the past years, this respondent indicated that the Swiss CIS regulation has equally followed the various UCITS directives and their implementing acts, as well as the AIFM directive.

537.This respondent added that in 2002, an expert commission was mandated to draft a new act in order to adapt Swiss legislation on Investment Funds to the fast-changing EU legislation. The new Collective Investment Schemes Act (CISA) entered into force on 1 January 2007. It was designed as a framework act with two implementing ordinances and contained the following main changes:(i) introduction of SICAVs and of two forms of closed-ended CIS, SICAFs and limited partnerships for CIS; (ii) introduction of the requirement for asset managers of Swiss CIS to obtain authorisation; and (iii) introduction of two categories of investors with different needs of protection, the investor and the qualified investor.

538. This respondent mentioned that the most recent revision of the CISA was initiated in 2012 by the Swiss Federal Council to adapt the Swiss CIS provisions to the AIFMD (Directive 2011/61/EU) and Directive 2009/65/EU (UCITS IV Directive). The amended CISA (and the associated ordinance) came into force on 1 March 2013.

539. This respondent mentioned that this legislative development in the Swiss fund industry has led to an adaptation of the Swiss CIS legislation to the respective EU legislation. The Swiss CIS legislation formally consists of only one act, the CISA, which governs products (i.e. securities funds, the Swiss equivalent of UCITS, and other funds for traditional and alternative investments, etc.), as well as the management and distribution of CIS and the safekeeping of CIS assets, but it does, in its regulatory outcome, correspond to the AIFMD. This conformity is highlighted by several CISA references to the respective EU legislation (e.g. Art. 53 CISA states that securities funds are open-ended collective investment schemes which invest their assets in securities *and comply with the laws of the European Communities*; Art. 152 CISA requires that the Federal Council and FINMA *observe the key requirements of the law of the European Union when issuing subordinate legislation*).

540. This same respondent further indicated that:

(i) In contrast to the respective EU legislation, Swiss CIS legislation consists, of only one act, the CISA, which governs products, as well as CIS management and distribution and the safekeeping of CIS assets.

(ii) With the latest revision of 2012, the Swiss CIS legislation was again aligned with the revised EU legislation, in particular with the newly introduced AIFMD (Directive 2011/61/EU) and the Directive 2009/65/EU (UCITS IV Directive).

(iii) Whereas the respective EU legislation primarily aims at providing an internal market within the European Union, the Swiss CIS legislation consists of a national act which primarily applies to persons domiciled in Switzerland. Hence, the Swiss CIS legislation contains very few cross-border provisions (Art. 119 et seq. CISA).

(iv) Even though Swiss CIS legislation does not feature any express provisions regarding passporting, Switzerland is very open and attractive as a distribution location for foreign CIS. This has been confirmed by the statistical numbers on market share of foreign (and in particular EU-domiciled) CIS in Switzerland.

(v) As the Call for Evidence relates to the AIFMD passport and third country AIFMs, the following comparison focuses on the CISA provisions covering asset managers of CIS and the respective provisions for AIFMs under the AIFMD. However, tax issues, and tax-related topics are therefore not addressed in this response.

c) Scope of the Swiss and the EU legislative framework and respective exemptions

Under Article 2 para. 1 AIFMD, the *AIFMD* applies, subject to exemptions, to:

(a) EU AIFMs which manage one or more AIFs irrespective of whether such AIFs are EU AIFs or non-EU AIFs;

(b) non-EU AIFMs which manage one or more EU AIFs; and

(c) non-EU AIFMs which market one or more AIFs in the European Union irrespective of whether such AIFs are EU AIFs or non-EU AIFs.

This provision applies irrespective of whether the AIF belongs to the open-ended or closed-ended type, it is constituted under the law of contract, trust law or statute, or has any other legal form, irrespective of the legal structure of the AIFM (Art. 2 para. 2 AIFMD).

The amended CISA of 2012 (Art. 2 para. 1 CISA) follows the AIFMD and applies, irrespective of their legal status, to:

a. Swiss CIS and persons who are responsible for the management and distribution of such schemes, and the safekeeping of assets held in them;

b. foreign CIS distributed in Switzerland;

c. persons who manage foreign CIS in or from Switzerland;

d. persons who distribute foreign CIS in Switzerland;

e. persons who distribute, from Switzerland, foreign CIS which are not exclusively reserved for qualified investors as defined in Article 10, or subject to equivalent foreign law;

f. persons who represent foreign CIS in Switzerland.

The term AIFM is defined in Article 4 para. 1 let. b AIFMD as “legal persons whose regular business is managing one or more AIFs”. Annex I to the AIFMD describes the investment management functions an AIFM shall at least perform when managing an AIF (i.e. portfolio management and risk management), as well as other functions an AIFM may additionally perform in the course of the collective management of an AIF (i.e. administration, marketing and activities related to the assets of AIFs).

The amended CISA of 2012 introduced the same distinction for asset managers. Under Article 18a CISA, asset managers of CIS ensure the proper conduct of portfolio and risk management for one or more CIS. They may in the course of such duties additionally perform administrative activities, as well as certain ancillary services (for a detailed wording of Art. 18a para 3 CISA see question 28, section 2 above).

Article 2 para. 2 CISA contains exemptions for asset managers from the CISA which are in line with the exemptions listed in Article 2 para. 3 AIFMD.

Article 3 AIFMD further sets out specific exemptions for small AIFMs and AIFMs acting within a group. For these AIFMs, the AIFMD requires member states to ensure that such AIFMs are subject to registration with the competent authorities of their home member state.

Based on the AIFMD, the amended CISA of 2012 introduced similar de minimis and group exemptions (Art. 2 para. 2 let. h CISA). Asset managers of CIS whose investors are qualified investors and who meet certain requirements are exempt from the requirement to obtain authorisation as an asset manager (for a detailed wording of Art. 2 para. 2 let. h CISA see question 28, section 2 above). In contrast to the AIFMD, such exempted asset managers are required to register with the competent authorities. However, Article 2 para. 2^{bis} CISA states that the Federal Council may introduce a registration requirement in order to be able to collect economically significant data irrespective of whether such asset managers subject themselves to the CISA.

As regards the de minimis thresholds, the CISA does– unlike the AIFMD – not provide for an exemption to the authorisation requirement for cases in which these thresholds are occasionally exceeded. The CISA provides for stricter rules in this respect than the AIFMD.

The above comparison shows that the scope of the Swiss framework and the respective exemptions are very similar to the related provisions under the EU regime.

1. Authorisation of AIFMs and asset managers of CIS

Authorisation of AIFMs as set out in Chapter II of the AIFMD deals with the conditions for taking up activities as an AIFM, applying for authorisation, the conditions for granting authorisation, initial capital and own fund, changes in the scope of the authorisation, and withdrawal of authorisation (Arts. 6 – 11 AIFMD).

As mentioned above, the CISA does not exclusively cover asset managers of CIS but also other parties responsible for the management of a CIS, the safekeeping of the assets held in a CIS and the distribution of a CIS to non-qualified investors (Art. 13 para. 1 CISA). The scope of the covered institutions under the CISA is therefore wider than the scope of the AIFMD. The conditions for granting authorisation to asset managers (Art. 14 para. 1 CISA) apply to all CISA-regulated institutions (including asset managers) and are generally in line with the respective AIFMD provisions for AIFMs. Under Article 14 para. 1 CISA, authorisation is granted if:

a. the persons responsible for management and the business operations have a good reputation, guarantee proper management, and possess the requisite specialist qualifications;

b. the significant equity holders have a good reputation and do not exert their influence to the detriment of prudent and sound business practice;

c. compliance with the duties under the CISA is assured by internal regulations and an appropriate organisational structure;

d. sufficient financial guarantees are available;

e. the additional authorisation conditions listed in the relevant provisions of the CISA are met.

The additional authorisation requirements for asset managers of CIS relating to the organisation, duties, delegation of tasks and changes are listed in Article 18 – 18c CISA and were mainly introduced in the revised CISA of 2012 for the purpose of its alignment with the AIFMD.

Depending on the activity and the legal form, asset managers of CIS must have a minimum capital of at least 200,000 or 500,000 Swiss francs, paid up in cash, or collateral which equates to the minimum capital specified in Article 19 CISO. In addition to the minimum capital and in accordance with the AIFMD, asset managers must have appropriate own funds (Art. 21 et seq. CISO).

Any change in the circumstances based on which authorisation or approval was granted must be authorised or approved by FINMA prior to the continuation of the respective activity (Art. 16 CISA). FINMA must also be notified in advance of any changes in CIS asset managers (art. 18c CISA).

Regarding the withdrawal of an authorisation as an asset manager, the specific provisions on supervision set out in the CIS legislation, i.e. Articles 132 – 144 CISA, apply. In particular, Article 133 para. 1 CISA states that in the event of infringements of the contractual or regulatory provisions or of the provisions of the articles of association, the supervisory instruments defined in Articles 30 – 37 of the Financial Market Supervision Act of 22 June 2007 (FINMASA) apply accordingly. Under Article 37 para. 1 FINMASA, FINMA shall revoke the licence of a supervised person or entity, or withdraw its recognition or cancel its registration if it no longer fulfils the requirements for the activity it performs, or seriously violates the supervisory provisions. The Swiss provisions on the withdrawal of authorisation therefore largely correspond to the respective provisions under the AIFMD (Art. 11 AIFMD).

2. <u>Operating conditions for AIFMs and asset managers of CIS</u>

The operating conditions for AIFMs are set out in Chapter III of the AIFMD. The general principles of Article 12 AIFMD are reflected in Article 20 CISA, which deals with the code of conduct, duty of loyalty in particular, due diligence and the duty to provide information.

The remuneration provision in Article 13 AIFMD is not explicitly addressed in the CISA, but forms part of the duty of loyalty (Art. 20 para. 1 a. CISA). Further, the “Code of Conduct” of the Swiss Funds & Asset Management Association (SFAMA) of 7 October 2014 contains provisions on remuneration. This Code of Conduct is accepted by FINMA as a minimum standard (Art. 20 para. 2 CISA and Art. 7 para. 3 FINMASA).

The conflicts of interest provision in Article 14 AIFMD is reflected in the newly introduced Article 32b CISO, and the provisions on risk management (Art. 15 AIFMD) have been incorporated into Article 12a CISO. As in the AIFMD, asset managers must ensure proper and appropriate risk management, an internal control system and a compliance system covering its entire business activities. Risk management must be organised in a way that all material risks can be adequately identified, assessed, controlled and monitored (Art. 12a para. 2 CISO). Asset managers must separate risk management, the internal control system and compliance functionally and hierarchically from the operating units, in particular from the investment decisions (portfolio management) function (Art. 12a para. 3 CISO). Article 68 para. 3 let. c CISO-FINMA further requires asset managers to implement internal guidelines setting out the processes and systems for the assessment and management of all material risks of the authorised institution and the collective investment schemes, and in particular their market, liquidity and counterparty risk.

Liquidity management (Art. 16 AIFMD) is addressed in the CISA as part of the due diligence (Art. 20 para. 1 b. CISA) and the risk management (art. 12*a* CISO) requirements. Asset managers of CIS have to implement organisational measures necessary for proper management (Art. 68 para. 3 let. c CISO-FINMA).

The requirement for a proper and independent valuation of the AIF assets (Art. 19 AIFMD) is addressed in Article 88 CISA, which states that investments listed on a stock exchange or another regulated market open to the public shall be valued at the prices paid on the main market. Other investments for which no current price is available must be valued at the price which would probably be obtained in a diligent sale at the time of valuation. The CISO-FINMA further states that investments must be valued at market value and displayed in the financial statement of the fund according to their method of valuation (Art. 84 CISO-FINMA). The valuation of the investments must be strictly separated from portfolio management, and be carried out by sufficiently qualified specialists (Art. 72 CISO-FINMA). The SFAMA “Guidelines on the valuation of the assets of CIS” of 20 June 2008 accepted by FINMA as a minimum standard contain further provisions on valuation.

The CISA provisions on the delegation of asset management functions correspond to the respective AIFMD provisions (Art. 20 AIFMD). Asset managers of CIS may delegate specific tasks, provided it is in the interest of efficient management, the persons appointed are properly qualified to execute the delegated task, and the persons to whom the task was delegated receive the instruction, monitoring and control required for the implementation of the assigned task (Art. 18b CISA). They may only delegate investment decisions to asset managers of CIS who are subject to recognised supervision. The letterbox entity provisions under Article 82 of the Commission-delegated regulation, (EU) No. 231/2013 to the AIFMD, are reflected accordingly in Article 66 para. 3 CISO-FINMA. Any change in circumstances underlying the authorisation or approval requires FINMA’s consent prior to continuation of the activity (Art. 16 CISA). Further, any change in asset managers of CIS requires authorisation from FINMA.

541. This respondent was of the view that, by revising the CISA and the associated ordinances in 2012, Switzerland has fully implemented the AIFMD standards into Swiss CIS regulation. They believed that Switzerland has therefore established the basis for fulfilling the requirements for the extension of the EU passport to the AIFMs and AIFs of third countries, thus allowing EU market access for alternative investment funds to professional investors in the EU.

542. This respondent would welcome the extension of the EU passport to third countries and is convinced that such market access will have a positive impact on the funds

market and investor choice in the EU, as well as in Switzerland. With the conclusion of cooperation arrangements between FINMA and EU national competent authorities based on applicable ESMA guidelines, a strong and well-functioning basis for supervisory cooperation has already been established which can then be further enhanced. Links to Swiss legislation on Collective Investment Schemes:

Federal Act on Collective Investment Schemes (Collective Investment Schemes Act, CISA) of 23 June 2006
Ordinance on Collective Investment Schemes (Collective Investment Schemes Ordinance, CISO) of 22 November 2006
Ordonnance de l'Autorité fédérale de surveillance des marchés financiers sur les placements col-lectifs de capitaux (Ordonnance de la FINMA sur les placements collectifs, OPC-FINMA) du 27 août 2014
Federal Act on the Swiss Financial Market Supervisory Authority (Financial Market Supervision Act, FINMASA) of 22 June 2007

543. Another respondent indicated that would like to share with ESMA a pragmatic approach which acknowledges the realities of marketing of closed-ended AIF to international professional investors. In this approach, they also took into account similar AIFMD rules introduced by third country concerned. This respondent indicated that they identified three groups of third countries as described below:

544. First group: Implementation of third country passport. This group includes countries which have implemented AIFMD in their jurisdiction. The third countries concerned are mainly Switzerland and the Channel Islands (Jersey and Guernsey). Those countries made an effort to adopt the AIFMD legislation in their national legal system. They believed this is important to promote their approach. This is the reason why this respondent supported for those third countries the implementation of third country passport in accordance with AIFMD on the basis of equivalent rules.

545. Another respondent indicated that its analysis of the AIFMD compatibility of Swiss regulation was the following:

546. Relevant regulations in Switzerland. These are the following:

- Collective Investment Schemes Act of 23 June 2006 (as amended on 1 January 2014) (“CISA”).

- Collective Investment Schemes Ordinance of 22 November 2006 (as amended on 1 January 2014) (“CISO”).

- The completely revised Collective Investment Schemes Ordinance of FINMA of 14 October 2014 (“CISO-FINMA”).

- FINMA Circular 2013/9 Distribution of collective investment schemes (28 August 2013).

- FINMA Circular 2010/1 Minimum standards for remuneration schemes of financial institutions (21 October 2009, as amended on 1 June 2012).

- SFAMA Guidelines on Duties Regarding the Charging and Use of Fees and Costs (22 May 2014).

- Code of Conduct of the Swiss Funds & Asset Management Association ("Code of Conduct") of 7 October 2014.

547. Comparison of legal regimes:

General authorization requirement for asset managers of collective investment schemes

548. Modelled after the AIFMD, the scope of the CISA was extended to cover all asset managers of collective investment schemes, i.e. in particular, it now also covers "persons who manage foreign collective investment schemes in or from Switzerland" (Art. 2 para. 1 let. c CISA). Correspondingly, it is now no longer only asset managers of Swiss collective investment schemes that are subject to an authorization requirement, but instead all "asset managers of collective investment schemes" (Art. 13 para. 2 let. f CISA).

549. The authorization requirements have been increased in some cases, and brought in line with the requirements under the AIFMD. Article 18a para. 1 CISA sets out the core duties of an asset manager under the CISA. The asset manager must ensure proper portfolio and risk management for one or more collective investment schemes. This definition corresponds to that in the AIFMD.

550. The fund management company may delegate investment decisions as well as specific tasks, provided this is in the interest of efficient management. Moreover it shall appoint only those persons who are properly qualified to execute the task, and ensure they receive their instruction, monitoring and control required for the implementation of the assigned tasks.

551. It may only delegate investment decisions to asset managers of collective investment schemes who are subject to a recognized supervision. Where foreign law requires an agreement on cooperation and the exchange of information with foreign supervisory authorities, it may only delegate investment decisions to asset managers abroad where such an agreement exists between FINMA and the relevant foreign supervisory authorities for the investment decisions concerned.

552. An asset manager may additionally perform administrative activities and certain ancillary services (e.g. fund business for foreign collective investment schemes, under the condition that an agreement on cooperation and the exchange of information exists between FINMA and the relevant foreign supervisory authority in the country in which the foreign collective investment scheme is domiciled; discretionary management of individual portfolios, investment advice, the distribution

of collective investment schemes, and the representation of foreign collective investment schemes).

2. *De minimis exemptions*

553. As is the case with the AIFMD, the CISA also has a de minimis rule. Art. 2 para. 2 let. h CISA sets out rules exempting asset managers of collective investment schemes from the requirement to obtain authorization pursuant to Art. 13 para. 2 let. f CISA, provided certain prerequisites are met. First and foremost, the investors in the collective investment scheme have to be qualified investors. One of the following requirements must then also be met:

- the assets under management, including the assets acquired through the use of leveraged finance, amount in total to no more than CHF 100 million;

- the assets under management of the collective investment schemes consist of non-leveraged collective investment schemes for which investors are not permitted to exercise redemption rights for a period of five years after their first investment is made in each of these collective investment schemes, and amount to no more than CHF 500 million; or

- the investors are exclusively group companies of the group of companies to which the asset manager belongs.

554. Article 1b CISO also sets out principles for the calculation of these thresholds. This extended view, which corresponds to the AIFMD, is aimed at preventing the splitting of assets under management across different group companies to remain below the threshold and thus circumvent the authorization requirement. The value of the total assets under management must be calculated on at least a quarterly basis, under due consideration of any leverage effect. If there is no market price for the assets under management, their value is determined on the basis of the capital commitments or nominal value of the collective investment vehicles concerned.

555. FINMA determines the details for calculating the assets and the leverage effect. Since the value of the collective investment assets under management may fluctuate, the possibility of the value of the assets rising and exceeding the threshold cannot be ruled out. In such an event, Art. 1b para. 3 CISO states that the asset manager must notify FINMA to this effect within 10 days, and must submit an application to FINMA for approval pursuant to Article 14 et seqq. CISA within 90 days.

556. Unlike the AIFMD, the CISA does not provide for an exemption to the authorization requirement for cases in which the thresholds are occasionally exceeded. Hence the CISA is stricter than the European regulation in this respect.

3. *Authorization requirements*

557.The partial revision of the CISA added some more detailed provisions on the capital requirements of an asset manager and on the appropriate organizational structure. The new Art. 12a CISO contains some significant provisions on organizational structure. As in the AIFMD, the asset manager must ensure it has proper and appropriate risk management, an internal control system and a compliance system covering its entire business activities.

558.Risk management must be organized so that all material risks can be adequately identified, assessed, controlled and monitored (Art. 12a para. 2 CISO). The asset manager must also separate risk management, the internal control system and compliance in functional and hierarchical terms from the operating units, in particular from the investment decisions (portfolio management) function (Art. 12a para. 3 CISO). The completely revised CISO-FINMA will address these issues in more detail.

559.The Collective Investment Schemes Ordinance also contains detailed provisions (Art. 19 et seqq. CISO) regarding the “sufficient financial guarantees” required in accordance with Art. 14 para. 1 let. d CISA of an asset manager of collective investment schemes organized under Swiss law. i.e. the minimum capital required. As before, the minimum capital required is CHF 200,000. However, if a Swiss asset manager manages foreign funds, the minimum capital required is CHF 500,000. Furthermore, own funds amounting to at least one quarter of the fixed costs must be held. This amount increases by 0.02% of the amount by which the value of the portfolio exceeds the amount of CHF 250 million, up to a maximum of CHF 20 million (Art. 21 para. 1 c CISO).

560.The CISA imposes stricter requirements than the AIFMD in terms of minimum capital and capital adequacy of asset managers.

4. *Delegation:* Concerning the AIFMD delegation rules, in particular the “letter box entity” rules, the swiss rules on delegation and substance which were contained in the FINMA Circular 2008/37 have been abrogated with the entry into force of the CISO-FINMA as of 1 January 2015. New rules are set up in Art. 66 CISO-FINMA and we expect that FINMA will precise the principles of Art. 66 in due time. Unlike the ESMA Guidelines on Key Concepts of the AIFMD, with the exception of Art. 7 para. 1 CISA, Switzerland does not have any explicit provisions exempting family offices from collective investment schemes legislation

5. Cooperation agreements: The need to conclude cooperation agreements with the competent supervisory authorities in EU member states was recognized at an early stage and set down in the CISA. On 16 July 2013, FINMA and ESMA signed cooperation agreements on behalf of all 27 EU national competent authorities for securities markets regulation.

Custodian banks

561. The partial revision of the CISA led to more specific and stricter requirements regarding the custodian banks of Swiss collective investment schemes. The new and amended provisions are aimed at improving investor protection and adopting international standards (in particular AIFMD), and also continue to allow Swiss custodian banks to perform the safekeeping of fund assets for foreign collective investment schemes if delegated to them.

562. The CISA previously contained only general provisions regulating the organization and activity of custodian banks, and more specific detail has been added as part of the partial revision of Swiss collective investment schemes legislation. In particular, detailed provisions have been adopted which require the custodian banks (like all CISA licensees) to ensure that it has an appropriate risk management, an internal control system and a compliance system, with the corresponding separation of functions from the operating units (Art. 12a and Art 102a et seq. CISA, Art. 77 et seq. CISO-FINMA). Furthermore, new detailed provisions with regard to the duties of the custodian bank in general and to the delegation of safekeeping have been implemented in the CISO in order to align the respective rules with the AIFMD (Art. 104 and 105a CISO). For example, specific duties regarding the timely settlement of transactions, the safekeeping of assets held in custody and the ownership verification and record keeping have been implemented (Art. 104 para 1 CISO). Moreover, it has been specified, in Art. 105a CISO, that a custodian bank must, when it delegates the safekeeping of assets to a third-party custodian, i.a., verify and monitor whether the latter possesses an appropriate organisational structure and the specific qualifications required and whether it is subject to external audits.

563. In addition, the liability of custodian banks of Swiss collective investment schemes was increased in order to largely approximate the liability of a custodian bank to the standard as set forth by the AIFMD. According to Art. 145 para. 3 CISA, if a custodian bank assigns the fulfillment of a task to a third party, it is liable for the losses caused by that third party unless it proves that it applied the degree of due diligence required in the given circumstances with regard to selection, instruction and monitoring (reversal of the burden of proof). Furthermore, the safekeeping of financial instruments may, in general, be transferred only to regulated third-party custodians and collective securities depositories (Art. 73 para. 2bis CISA).

564. When adopting the liability regime as set forth in Art. 145 para 3 CISA, the legislator took, i.a., into consideration that, in 2010, Switzerland enacted a new Intermediated Securities Act (FISA) which regulates the custody of certificated and uncertificated assets by custodians and ensures the protection of property rights of investors (Art. 1 FISA). This act strengthens the position of investors (such as collective investment schemes) vis-à-vis their custodians (e.g. Art. 17 FISA states that, if a custodian bank is subject to compulsory liquidation, the investors‘ securities are excluded *ex officio* from the custodian's estate).

565. Although the Swiss regulatory liability regime for the losses of financial instruments by the custodian bank of Swiss collective investment schemes has not been completely

aligned to the regime set forth by the AIFMD, the above described recent adaptations to the Swiss legislation have the same effect, because in practice, the liability of the custodian bank may be contractually increased between the fund, the depositary, and the sub-depositary.

Remuneration policy

566. On 11 February 2013, ESMA published its *Final Report Guidelines on sound remuneration policies under the AIFMD*. According to Annex 2 of the AIFMD, the remuneration policy for AIFMs must be consistent with sound and effective risk management, and must promote this. Furthermore, it may not encourage risk-taking which is inconsistent with the risk profiles, contractual conditions or instruments of incorporation of the AIFs managed. The remuneration policy must also be in line with the business strategy, objectives, values and interests of the AIFM and the AIFs it manages or the investors in such AIFs, and must include measures to avoid conflicts of interest (these must be specified in detail according to the ESMA Guidelines).

567. Where asset management is outsourced to Switzerland, these provisions already apply today. The ESMA Guidelines state that when delegating portfolio management or risk management activities according to Article 20 of the AIFMD, the AIFM must ensure that:

- the entities to which portfolio management or risk management activities have been delegated are subject to regulatory requirements on remuneration that are equally as effective as those applicable under these Guidelines; or

- appropriate contractual arrangements are put in place with entities to which portfolio management or risk management activities have been delegated in order to ensure that there is no circumvention of the remuneration rules set out in the present Guidelines. These contractual arrangements should cover any and all payments made to the delegates' identified staff as compensation for the performance of portfolio or risk management activities on behalf of the AIFM.

568. Swiss AIFMs will have to comply with the AIFMD once the AIFMD passport is available for third countries. However, Switzerland already has comparable rules in place today (cf. SFAMA Code of Conduct, margin no. 43 which refers to FINMA Circular 2010/1 Minimum standards for remuneration schemes of financial institutions which should comply with CRD IV).

Corporate social responsibility

569. Corporate social responsibility comprises rules governing remuneration, conflicts of interest, asset stripping and transparency: unlike the CISA, the AIFMD features very detailed rules in these respects.

Risk management

570. The principles of risk management feature in the revised CISO-FINMA. Precise rules are expected to be covered by a FINMA circular or a FINMA approved self-regulation initiative in the near term.

Reporting

571. According to the AIFMD, AIFMs must draw up reports on the AIFs and submit these to the competent authorities. In total, AIFMs must provide fresh data on a regular basis on 130 individual points at the manager level and for each individual fund. This corresponds to a large amount of data that must be gathered from various sources at different intervals and in different formats. All of this information has to be checked and validated at different times. In Switzerland the Swiss Financial Market Supervisory Authority (FINMA) does not directly control the fund activities. The supervision is ensured by audit firms which are controlled by the Federal Audit Oversight Authority (FAOA). With the total revision of CISO FINMA as of 14 October 2014, the scope of the supervision shall be extended.

572. This respondent underlined that it is important to stress that the AIFMD does not require any equivalence of third country regulation. Despite this lack of an explicit equivalence requirement, this respondent mentioned that Switzerland has already implemented all AIFMD standards in its regulation to ensure that it meets the market access conditions.

573. This respondent also wanted to like to highlight that Switzerland has concluded cooperation agreements with the EU member states in July 2013. Furthermore, FINMA has been an ordinary member of IOSCO since 1996 and actively participates in the meetings of the IOSCO Board and the European Regional Committee, as well as various committees and task forces relevant to Switzerland.

574. This respondent added that certain Swiss institutions have constructed their marketing strategies on the premise of the possible extension of the passport to third countries. The obstacles encountered by a majority of our members with the national private placement regimes - these regimes are not scalable, entails high legal uncertainty and costs (regarding legal/regulatory advice by external consultants / lawyers in or to understand the different local rules applying) – strengthen the importance of the AIFMD passport for Switzerland.

Competition and Market disruption

575. <u>In relation to the access to the market in Switzerland, as a general assessment, one respondent</u> indicated that EU market access is of fundamental importance to Swiss banks and the Swiss asset management industry. From that perspective, this respondent fully endorsed, in principle, the extension of the passport to the AIFMs and AIFs of third countries. Moreover, they were confident that the extension of the passport for third countries will be positive for the European Union, as more providers will deepen the fund market. Competition will increase to the benefit of investors, certainly in terms of the breadth of products offered and most probably also in terms

of fees. Without passporting the complexity of the heterogeneous local regulations in the different EU Member States will effectively hamper EU-wide distribution of EU AIFs to EU clients to the detriment of the latter.

576. Another respondent indicated they have direct experience of marketing EU managed AIFs and/or UCITS into Switzerland. This respondent indicated that their experience demonstrates that such third country does not impose excessively heavy requirements or restrictions on European asset managers and this respondent considered such country as already granting market access under broadly equivalent conditions.

577. Another respondent indicated that from what they heard from their members, Switzerland grants market access under broadly equivalent conditions for UCITS and AIFs (but it is worth noting that the terminology used for investors is different (qualified investors and further sub-categories).

578. Another respondent indicated that Switzerland primarily is, and always has been, a location for the distribution of investment funds. Recent figures exemplify this: as of 31 November 2014, 6555 UCITS and 138 European AIFs were approved by FINMA for public distribution in Switzerland. Moreover, Switzerland is also an important place for the production of investment funds. As of 31 November 2014, 1505 Swiss investment funds were approved by FINMA (The local Authority).

579. This same respondent indicated that depending on the intended activity to be exercised by EU AIFMs or UCITS management companies in Switzerland, different CISA (Collective Investment Schemes Act) provisions apply and different authorisations (for institutions) and approvals (for products) have to be obtained. The following scenarios can be distinguished:

1. Management of one or more Swiss CIS (non-EU AIFs)

   Swiss CIS may be launched as an open-ended CIS in the form of a contractual fund (Arts. 8 and 25 et seq. CISA) or an investment company with variable capital (SICAVs; Arts. 8 and 36 et seq. CISA), or they may be launched as closed-ended CIS in the form of a limited partnership for CIS (art. 9 and 98 et seq. CISA), or an investment company with fixed capital (SICAFs; Art. 9 and 110 et seq. CISA). The CISA provides for three types of open-ended CIS: (i) securities funds (Swiss equivalent of UCITS, Art. 53 et seq. CISA), (ii) real estate funds (Art. 58 et seq. CISA) and (iii) other funds for traditional and alternative investments (Art. 68 et seq. CISA). From an EU perspective, all types of open and closed-ended CIS qualify as non-EU AIFs according to the AIFMD.

   Any party responsible for the management of one or more Swiss CIS must obtain authorisation from FINMA, e.g. authorisation as a fund management company to manage one or more Swiss contractual funds (Arts. 13 para. 2 let. a and 28 et seq. CISA), or authorisation as a CIS asset manager (Arts. 13 para. 2let. f and 18 et seq. CISA).

Under Swiss law, a fund management company must be a company limited by shares with its registered seat and main administrative office in Switzerland. It must provide for a share capital of at least 1 million Swiss francs, paid up in cash. Further, an appropriate ratio is required between the equity of a fund management company and the total CIS assets of a CIS it manages (Arts. 28 and 32 CISA; Arts. 43 and 48 Collective Investment Schemes Ordinance, CISO).

The main purpose of a fund management company is the conduct of fund business for Swiss CIS which includes the distribution (marketing) of CIS (Art. 29 para. 1 CISA). Authorisation as a fund management company is the most comprehensive form of authorisation under the CISA. Therefore, any party authorised as a fund management company is exempted from the requirement to obtain authorisation for CIS asset managers, distributors and representatives of foreign CIS (Art. 8 para. 1bis CISO).

In addition, the fund management company may provide the following ancillary services (Art. 29 CISA):

a. discretionary management of individual portfolios;

b. investment advisory services;

c. safekeeping and technical administration of CIS.

Further, it may conduct fund business for foreign CIS, provided an agreement exists on cooperation and exchange of information between FINMA and the competent foreign supervisory authorities, and foreign law requires such an agreement.

A fund management company may delegate investment decisions (portfolio and risk management), as well as certain specific tasks to CIS asset managers which are subject to recognised supervision (Art. 31 para. 3 CISA), e.g. to asset managers of CIS according to Article 13 para. 2 let. f CISA or to EU AIFMs and UCITS management companies in line with FINMA established practice. The fund management company remains liable for the actions of its agents as if they were its own actions (Art. 31 CISA).

EU AIFMs and UCITS management companies not intending to conduct fund business for Swiss CIS, but to focus their activities on investment decisions (portfolio and risk management) in or from Switzerland, need to obtain FINMA authorisation as an asset manager of CIS (Arts. 13 para. 2 let. f and 18 et seq. CISA; for detailed asset management authorisation requirements, see Section 2 below).

To sum up, EU AIFMs and UCITS management companies intending to manage Swiss CIS (non-EU AIFs) in Switzerland need FINMA authorisation, be it an authorisation as a fund management company where one or more Swiss contractual funds are managed, or as an asset manager of CIS.

2. <u>Management of one or more UCITS and EU AIFs</u>

EU AIFMs and UCITS management companies intending to manage UCITS or EU AIFs in or from Switzerland need to obtain FINMA authorisation to act as an asset manager of CIS (Arts. 13 para. 2 let. f and 18 et seq. CISA).

Under the CISA regime of 2006, only asset managers of Swiss CIS were obliged to obtain FINMA authorisation, whereas asset managers of foreign CIS did not come under the CISA's scope. To align with international standards and in particular with the AIFMD, the amended CISA of 2012 introduced similar authorisation requirements for asset managers of Swiss and of foreign CIS.

Under Article 18 para. 1 CISA, asset managers of (Swiss or foreign) CIS with their registered office in Switzerland may be:

a. legal entities in the form of companies limited by shares, partnership limited by shares or limited liability companies;

b. general and limited partnerships;

c. Swiss branches of a foreign asset manager of CIS, provided:

    1. the asset manager, including the branch, is subject to appropriate supervisory control at its registered office,

    2. the asset manager is adequately organised and has commensurate financial resources and qualified personnel to operate a branch in Switzerland, and

    3. an agreement on cooperation and exchange of information exists between FINMA and the responsible foreign supervisory authorities.

Article 29 lets. a-f CISO specify the conditions for obtaining authorisation as an asset manager of CIS under foreign laws as set out in Article 18 para. 1 let. c CISA.

Depending on the activity and legal form, asset managers of CIS must have a minimum capital of at least 200,000 or 500,000 Swiss francs, paid up in cash, or collateral which equates to the minimum capital mentioned (Art. 19 CISO). In addition to the minimum capital and in accordance with the AIFMD, asset managers must have appropriate own funds (Art. 21 et seq. CISO).

In line with the AIFMD, the CISA stipulates that asset managers of CIS ensure the proper conduct of portfolio and risk management for one or more CIS (Art. 18a para. 1 CISA) and may perform additional administrative activities.

It may further provide the following ancillary services, including (Art. 18a para. 3 CISA):

a. fund business for foreign CIS, provided an agreement on cooperation and exchange of information exists between FINMA and the competent foreign supervisory authorities the fund business, and foreign law requires such an agreement;

b. discretionary management of individual portfolios;

c. investment advisory services;

d. CIS distribution;

e. representation of foreign CIS.

Asset managers are exempted from the requirement to obtain authorisation as a distributor, but not as a representative of foreign CIS (art. 8 para. 2 CISO).

Similar to the fund management company, the asset manager of CIS may delegate specific tasks to asset managers of CIS who are subject to recognised supervision, provided this is in the interest of efficient management, the persons appointed are properly qualified to execute the delegated task, and the persons to whom the task was delegated receive the instruction, monitoring and control required for the implementation of the assigned task (Art. 18 para. 1 let. b CISA). They may only delegate investment decisions to asset managers of CIS who are subject to recognised supervision. In line with FINMA practice, EU AIFMs and UCITS management companies are considered asset managers of CIS for which recognised supervision is given.

Following the AIFMD, Article 2 para. 2 let. h CISA further provides for the following exemptions from authorisation as an asset manager:

1. Asset managers of (Swiss or foreign) CIS whose investors are qualified investors[44] and that meet one of the following requirements:

    a. the assets under management, including the assets acquired through the use of leveraged finance, amount in total to no more than CHF 100 million.

    b. the assets under management of the CIS consist of non-leveraged CIS where investors are not permitted to exercise redemption rights for a period of five years after their first investment is made in each of these CIS, and amount to no more than CHF 500 million.

    c. the investors are exclusively group companies of the group to which the asset manager belongs.

    Asset managers of CIS that meet the requirements under section 1 above may subject themselves to the CISA if this is required by the country in which the CIS is established or distributed.

2. FINMA may exempt asset managers of CIS in the case of single investor funds where the fund management company has delegated the investment decisions to the single investor (Art. 7 para. 4 CISA).

[44] Regulated financial intermediaries such as banks, securities traders, fund management companies and asset managers of collective investment schemes, as well as central banks; regulated insurance institutions; public entities and retirement benefits institutions with professional treasury operations; companies with professional treasury operations; high-net-worth individuals if they declare in writing that they wish to be deemed qualified investors (Art. 10 para. 3 et seq. CISA).

3. FINMA may, in individual and justified cases (and regardless of the amount of business handled by a specific asset manager) fully or partially exempt asset managers from certain CISA provisions, provided, among others, the CISA's protective purpose is not impaired (Art. 18 para. 3 CISA).

To sum up, EU AIFMs and UCITS management companies that intend to manage UCITS and EU AIFs in or from Switzerland need to obtain FINMA authorisation as asset managers of CIS.

3. <u>Marketing of one or more UCITS and EU AIFs to regulated financial intermediaries and insurance institutions</u>

Any marketing / distribution of CIS directed exclusively at (i) regulated financial intermediaries such as banks, securities traders, fund management companies and asset managers of CIS and central banks; or (ii) regulated insurance institutions does not require respective authorisation under the CISA. UCITS or EU AIFs can therefore be marketed to regulated financial intermediaries or insurance institutions in Switzerland without authorisation for CIS distribution under CISA.

4. <u>Marketing of one or more UCITS and EU AIFs to qualified investors</u>

Based on the AIFMD, the amended CISA of 2012 introduced more stringent rules on the distribution of foreign CIS to qualified investors.[45] While no changes were introduced on the product level (i.e. no foreign product approval is required for foreign CIS to be distributed in Switzerland to qualified investors), the revised CISA requires the appointment of a representative and a paying agent for such products to be distributed in Switzerland (Art. 120 para. 4 CISA). The financial intermediary that markets the UCITS or EU AIFs to qualified investors in Switzerland must be admitted for CIS distribution in its country of domicile and has to conclude a written distribution agreement governed by Swiss law with a CIS representative (Art. 30a CISO).

5. <u>Marketing of one or more UCITS and EU AIFs to retail investors</u>

From a Swiss law perspective, UCITS and EU AIFs qualify as foreign CIS. EU AIFMs and UCITS management companies intending to market UCITS or EU AIFs in Switzerland to retail investors must therefore comply with the following requirements:

a. FINMA approval is required for foreign products for each UCITS / EU AIF (Arts. 119 – 122 CISA). Approval is granted where:

   1. the CIS, fund management company or company, asset manager of the CIS and depository are subject to supervision intended to protect investors;

[45] Regulated financial intermediaries such as banks, securities traders, fund management companies and asset managers of collective investment schemes, as well as central banks; regulated insurance institutions; public entities and retirement benefits institutions with professional treasury operations; companies with professional treasury operations; high-net-worth individuals if they declare in writing that they wish to be deemed qualified investors (Art. 10 para. 3 et seq. CISA).

2. in terms of organization, investor rights and investment policy, the fund management company or company and the depository are subject to regulations equivalent to the CISA provisions;

3. the designation of the CIS does not provide grounds for confusion or deception;

4. a representative and a paying agent are appointed for the distribution of units in Switzerland;

5. an agreement on cooperation and exchange of information exists between FINMA and the competent foreign supervisory authorities with regard to distribution.

b. The fund management company or company must appoint a FINMA authorised representative that represents the CIS towards investors and FINMA (Arts. 13 para. 2 let. h and 123 para. 1 CISA). The representative may distribute the CIS itself or appoint distributors. Representatives of foreign CIS are exempted from the requirement to obtain the requisite authorisation (Art. 8 para. 3 CISO).

c. Any party responsible for the distribution of CIS to non-qualified investors must also obtain FINMA authorisation as distributor of CIS (Arts. 13 para. 2 let. g and 19 CISA). As mentioned above, fund management companies, asset managers of CIS and representatives of foreign CIS are exempted from the requirement to obtain authorisation to act as distributors (Art. 8 CISO).

Links to Swiss legislation on Collective Investment Schemes:

Federal Act on Collective Investment Schemes (Collective Investment Schemes Act, CISA) of 23 June 2006
Ordinance on Collective Investment Schemes (Collective Investment Schemes Ordinance, CISO) of 22 November 2006
Ordonnance de l'Autorité fédérale de surveillance des marchés financiers sur les placements col-lectifs de capitaux (Ordonnance de la FINMA sur les placements collectifs, OPC-FINMA) du 27 août 2014
Federal Act on the Swiss Financial Market Supervisory Authority (Financial Market Supervision Act, FINMASA) of 22 June 2007

580. Another respondent indicated that some third countries agreed mutual recognition agreements that allow French funds to be sold with no further restrictions (registration of French funds and/or managers, impose transparency requirement, require the use of local distributors, set quotas, put in place tax regimes unfavorable to foreign funds or even fully prohibit the access to their market). For instance, the Swiss and French regulators reached an agreement in 2000 that introduced the principle of mutual recognition for investment funds, in particular for funds aimed at retail investors. However, last year, the Swiss legislation restricted the marketing of foreign funds in Switzerland. It is at this stage too early to assess the consequences of this legislative change.

581. In relation to the taxation regime of Switzerland, one respondent indicated that in Switzerland double taxation agreements (DTAs) prevent double taxation and thus also remove obstacles to cross-border economic transactions. DTAs also govern administrative assistance in tax matters, which enables countries to exchange information for tax purposes. Switzerland has been applying the OECD standard in full since 2009. Since 2012, the standard also allows group requests. This respondent added that Switzerland has also signed tax information exchange agreements (TIEAs). Unlike DTAs, which primarily govern the avoidance of double taxation, TIEAs deal solely with the exchange of information.

582. Overall, this respondent indicated that Switzerland has signed 49 DTAs in accordance with the international standard, of which 41 are in force, and 7 TIEAs, of which 3 are in force[46].

583. This respondent indicated that moreover, on 19 November 2014, the "Federal Council approved a declaration on Switzerland joining the multilateral agreement on the automatic exchange of information in tax matters. This international agreement, which was developed within the framework of the OECD, forms a basis for the future introduction of the cross-border automatic exchange of information. The question regarding the countries with which Switzerland should introduce this exchange of data is not affected by the signing of the multilateral agreement; it will be presented to Parliament separately at a later stage.

Monitoring of systemic risk

584. One respondent indicated that as regards the monitoring of systemic risk, Switzerland entered into cooperation agreements with the EU member states in July 2013 and that FINMA has been an ordinary member of IOSCO since 1996 and actively participates in the meetings of the IOSCO Board and the European Regional Committee, as well as various committees and task forces relevant to Switzerland.

[46] https://www.sif.admin.ch/sif/en/home/themen/internationale-steuerpolitik/doppelbesteuerung-und-amtshilfe.html

Annex 7 Summary of the feedback from the call for evidence in the case of Singapore

Overall summary of the feedback from the call for evidence

Investor protection

585. One respondent indicated they would like to share with ESMA a pragmatic approach which acknowledges the realities of marketing of closed-ended AIF to international professional investors. In this approach, they also took into account similar AIFMD rules introduced by third country concerned. This respondent indicated that they identified three groups of third countries as described below:

586. First group: Implementation of third country passport. This group includes countries which have implemented AIFMD in their jurisdiction. The third countries concerned are mainly Switzerland and the Channel Islands (Jersey and Guernsey) with whom they have significant trade, economic exchanges or partnership relations. Those countries made an effort to adopt the AIFMD legislation in their national legal system. They believed this is important to promote their approach. This is the reason why this respondent supported for those third countries the implementation of third country passport in accordance with AIFMD on the basis of equivalent rules.

587. Second group: "*statu quo*" approach. This group includes countries which have not implemented AIFMD in their jurisdiction but have developed on another basis a strong legislation on marketing. The third countries concerned are mainly USA, Canada and Singapore. This respondent indicated that they hope to implement the marketing passport in these jurisdictions one day but they believe that it is too early for this. All these countries have adopted a NPPR and are not ready yet to implement a legislation based on the same approach of AIFMD.

Competition and Market disruption

588. One respondent indicated the Hong Kong market has been for long an important market for them. They indicated that it is one of the most accessible as well as the Singaporean market and, to a lower degree, the Korean market.

589. Another respondent indicated that in addition to marketing to clients in many EU countries, they market their Lux UCITS in up to 12 non-EU countries. There are some so-called local requirements including in Singapore.

590. Another respondent indicated that in term of market access some countries are open, such as Singapore or Chile. But even in the most open countries, while it is usually possible to sell foreign funds, it is usually very difficult to manage local funds from abroad – the equivalent of the EU 'Management Company Passport'.

591. Another respondent indicated that some asset managers understand that there are no visible barriers for funds and service:

- Singapore Information memorandum is required to be prepared and lodged with the Monetary Authority of Singapore, MAS;
- For all UCITS products these need to include all marketing materials intended to be used to sell the product;
- Singapore allows foreign funds to register for sale in Singapore. An authorized or recognized CIS (Collective Investment Schemes) can be freely marketed to Singapore retail investors, subject only to prospectus filing requirements;
- Local and foreign retail funds can be freely marketed to Singapore retail investors, subject only to prospectus filing requirements and authorization or recognition requirements for open-ended funds;
- Registered fund management companies with MAS are subject to registration requirements which include serving not more than 30 qualified investors and managing assets the aggregate of which does not exceed S$250million;

Annex 8 Detailed information showing a breakdown by non-EU country of the number of non-EU AIFs and non-EU AIFMs active in Member States in accordance with Articles 36 and 42 of the AIFMD

Feedback from the NCAs (Q3:1 July - 31 September; Q4:1 October – 31 December 2014; Q5: 1 January 2015 – 31 March 2015)

1.1. UK

Non-EEA AIF Jurisdiction marketed under Article 36		
	Q3	**Q4**
Bahamas	1	1
Bermuda	8	9
Cayman Islands	261	275
Guernsey	22	25
Jersey	7	8
US	19	19
British Virgin Islands	25	25

Non-EEA AIFM and AIF marketed under Article 42				
	AIFM Q3	AIF Q3	AIFM Q4	AIF Q4
Australia	13	14	12	13
Bahamas	13	1	0	1
Bermuda	0	24	16	28
Brazil	2	0	2	0
Canada	3	3	3	3
Cayman Islands	29	553	33	587
Guernsey	51	140	57	121
Hong Kong	13	2	15	2
IoM	2	0	2	0
Japan	13	14	16	18
Jersey	21	34	27	47
Mauritius	5	6	6	9
Republic of Korea	1	0	1	0
Mexico	40	4	4	4
Singapore	8	6	11	7

South Africa	1	0	1	0
Switzerland	8	1	9	1
Thailand	1	1	2	2
United States	254	225	269	236
British Virgin Islands	3	45	3	42
US Virgin Islands	1	0	1	0

1.2. Ireland

Non-EU AIFs marketed under Article 36			
	Q3	**Q4**	**Q5**
Cayman Islands	9	15	0
British Virgin Islands	1	0	0
United States	1	0	0
Guernsey	1	0	2

Non-EU AIFMs marketing AIFs under Article 42			
	Q3	**Q4**	**Q5**
United States	47	13	18
Bermuda	17	0	2
Guernsey	5	11	2
Cayman Islands	4	2	1
Jersey	1	0	3
Australia	1	0	0
Switzerland	1	1	1
British Virgin Islands	0	0	2
Hong Kong	0	0	1

AIFs marketed by non-EU AIFMs under Article 42			
	Q3	**Q4**	**Q5**
Cayman Islands	130	18	23
United States	33	18	21
Bermuda	24	1	5
Ireland	10	0	0
Guernsey	9	7	11
Jersey	8	0	2
Luxembourg	7	0	2
British Virgin Islands	1	0	0
United Kingdom	1	0	1
Australia	1	0	0

Singapore	0	1	0
Hong Kong	0	0	8
Isle of Man	0	0	2
Mauritius	0	0	1

1.3. Sweden

Non-EU AIFs marketed by EU AIFMs under Article 36			
	Q3	**Q4**	**Q5**
Cayman Islands	17	37	14
U.S.	0	3	0
Guernsey	0	1	4
Bermuda	0	0	1

Non-EU AIFMs market AIFs under Article 42(1)			
	Q3	**Q4**	**Q5**
U.S.	25	44	16
Cayman Islands	5	2	7
Guernsey	3	4	1
Switzerland	1	0	0
Isle of Man	1	0	0
Bermuda	1	0	0
Australia	0	1	0
Jersey	0	0	2
Brazil	0	0	1
Hong Kong	0	0	1
Canada	0	0	1
Mauritius	0	0	1

AIFs marketed by non-EU AIFMs under Article 42(1)			
	Q3	**Q4**	**Q5**
U.S	5	32	13
Cayman Islands	47	84	30
Guernsey	7	3	2
Bermuda	1	1	1
Ireland	1	2	0
Luxembourg	1	1	0
British Virgin Islands	0	5	0
Australia	0	1	0
The UK	0	1	0
Jersey	0	0	1
Canada	0	0	1

1.4. The Netherlands

Non-EU AIFs marketed in the Netherlands under Article 36		

	Q3	Q4	Q5
Cayman Islands	45	17	3
USA	5	0	0
Bermuda	1	2	2
British Virgin Islands	0	16	17
Guernsey	0	4	4
Curacao	0	5	5

1.5. Luxembourg

Non-EU AIFMs marketing under Article 42			
	Q3	**Q4**	**Q5**
Guernsey	12	0	5
Jersey	6	0	2
Cayman Islands	7	3	4
Mauritius	1	0	2
Mexico	1	0	0
U.S	41	9	17
Australia	0	0	1
Canada	0	0	1
Hong Kong	0	0	1

AIFs marketed under Article 42			
	Q3	**Q4**	**Q5**
Bahamas	1	2	1
United Kingdom	2	0	0
Guernsey	20	0	7
Ireland	3	0	0
Jersey	6	0	3
Cayman Islands	80	10	20
Luxembourg	2	0	0
Mauritius	1	0	2
Mexico	1	0	0
U.S	70	4	12
Virgin Islands	5	0	0
Australia	0	0	1

1.6. Finland

Non-EU AIFs marketed in Finland under Article 36		
	Q4	**Q5**
Cayman Islands	23	2
Bermuda	1	0
British Virgin Islands	1	0
Guernsey	0	4

Non-EU AIFMs marketing under Article 42		
	Q4	**Q5**
Guernsey	3	0
U.S	20	12
Jersey	0	2
Brazil	0	1
Cayman Islands	0	2

Non-EU AIFs marketed under Article 42		
	Q4	**Q5**
Guernsey	1	0
Cayman Islands	21	23
U.S	17	7
Jersey	0	3
UK	0	1

1.7 Denmark

Non-EU AIFs marketed in Denmark under Article 36	Q4
U.S	1

Non-EU AIFMs marketing under Article 42	
	Q4
Guernsey	1
U.S	11
Cayman Islands	2
Hong Kong	1
Australia	1

AIFs marketed under Article 42	
	Q4
Guernsey	1
Cayman Islands	8
U.S	13
The UK	3
Hong Kong	1

1.8 Belgium

Non-EU AIFs marketed in Belgium under Article 36	Q4	Q5
Cayman Islands	15	23
Guernsey	0	7

Non-EU AIFMs marketing under Article 42		
	Q4	**Q5**
Guernsey	5	2
U.S	24	2
Cayman Islands	5	1
Jersey	5	2
Singapore	1	0
Switzerland	1	0

AIFs marketed under Article 42		
	Q4	**Q5**
Guernsey	6	8
Cayman Islands	71	69
U.S	10	12
The UK	2	2
Bermuda	1	1
Ireland	4	3
Singapore	1	1
Jersey	0	7
Luxembourg	0	2