

October 20, 2010

## EU Council of Ministers Reaches Agreement on AIFM Directive

### Summary

On October 19, the European Union Council of Ministers announced that agreement had been reached at its ECOFIN meeting on a compromise text of the proposed Alternative Investment Fund Managers Directive (AIFMD).

The Council text must be approved by the European Parliament before it becomes effective and will then go to the individual member states for implementation and to the European Securities and Markets Authority (ESMA) for detailed rules to be prepared on several key aspects of the AIFMD.

The Council stated that there is a large degree of agreement between it and the Parliament and accordingly that it hopes to be able to conclude negotiations with the Parliament in time for a final text of the AIFMD to be before the Parliament for approval on November 10. If that happens, the AIFMD text will come into force in early 2011 and will be required to be implemented by EU member states by early 2013.

Michel Barnier, the European Commissioner for Internal Markets and Services, issued a separate statement on October 19 in which he confirmed that the agreement reached at the ECOFIN meeting included a passport for funds managed by non-EU managers.

### Belgian Compromise Proposal – October 15, 2010

The ECOFIN agreement appears to have been based on the compromise proposal released on October 15 by the Belgian presidency of the EU Council (the Proposal). In an attempt to reach agreement over the most contentious issue of the passport for non-EU funds and managers, the Proposal set out a dual system allowing non-EU managers to apply for a passport from 2015, while EU managers will be able to obtain a passport from the initial implementation date of the AIFMD in 2013. The existing private placement regime will remain in place throughout this transition period, but may be withdrawn in 2018 if the passport for non-EU managers is successful—see below.

In order to obtain a passport, non-EU managers will need to meet a number of requirements, including appointing an EU legal representative to be a point of contact within the EU for regulators and others. There will also need to be co-operation agreements in place between the competent regulatory authorities of the manager's home jurisdiction and the 'host' member state(s) in which the manager is carrying out marketing activity. The manager's home state must not be on the list of Non-Cooperative Countries and Territories (NCCTs) maintained by the Financial Action Task Force (FATF) in connection with anti-money laundering and terrorist financing, and the manager's home state must have signed a tax treaty with the 'host' member state(s) which complies with the OECD Model Tax Convention.

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For EU managers to manage and/or market non-EU funds, and for non-EU managers to market non-EU funds within the EU, the funds themselves are also subject to requirements under the Proposal, which are similar to those for non-EU managers in relation to NCCTs, co-operation agreements and tax treaties.

Subject to the restrictions on the domicile of non-EU funds described above, an EU manager will be able to apply for a passport to market a non-EU fund in the same way as it makes such an application for an EU fund.

The Proposal retains other provisions that have raised concerns within the alternative investment fund industry, in particular with respect to depositaries and their liability. Under the Proposal, funds (whether EU or non-EU) which are managed by EU managers must have depositaries—and among other requirements, the depositary must be liable to the fund, or the investors, for the loss of any financial instruments which it holds for the fund. The liability remains, even where a depositary has delegated responsibility for custody to a third party—the depositary will be able to contract out of this liability, but only if the contract meets certain specific requirements. Various other AIFMD proposed provisions with respect to depositaries have been amended to meet industry concerns.

## Implementation

The Proposal makes special provision for the implementation of the passport for non-EU managers. Two years after member states have implemented the AIFMD, ESMA will produce a report on the functioning of the European passport and the private placement regimes which exist in individual member states. This report will include advice to the European Commission as to whether to implement the passport for non-EU managers. If the advice is positive, then the Commission must produce implementing measures specifying when the passport provisions will come into force. The passport would, in this scenario, be available to non-EU managers by approximately 2015. The existing private placement regime of individual member states will remain in place throughout this period but may be withdrawn if and when the passport for non-EU managers is granted. The Proposal also requires ESMA to review the passport regime three years after its implementation by the Commission (approximately 2018). At that stage, ESMA must advise the Commission on whether or not to remove the national private placement regimes.

## Conclusion

It remains to be seen whether the European Parliament will accept the compromise proposal. It is also not clear what provisions remain to be negotiated: for example whether to allow small managers to be exempt from the regime. What is clear is that reaching agreement on the previously controversial and divisive issue of passports for non-EU managers represents a significant landmark in progress towards adoption of the AIFMD.

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