AIFMD: Extension of Passport.
ESMA issues advice and opinion to European Parliament, Council and Commission.

The European Securities and Markets Authority (“ESMA”) has today issued its hotly awaited advice and opinion as required by Article 67 of the Alternative Investment Fund Managers Directive (“AIFMD”) on the functioning and extension of the marketing and management passports. The advice considers the application of the passport to six non-EU countries: Guernsey, Hong Kong, Jersey, Switzerland, Singapore and the United States. The opinion sets out ESMA’s analysis of the functioning of the passport for EU Alternative Investment Fund Managers (“AIFMs”), and national private placement regimes in the EU.

Summary

In its advice, ESMA concludes that are no significant obstacles to extending the passport to both Guernsey and Jersey, and also to Switzerland following certain (in progress) amendments to relevant Swiss legislation. However ESMA advises delaying the decision with regards to the U.S., Hong Kong and Singapore due to concerns related to competition, regulatory issues and a lack of sufficient evidence to properly assess the relevant criteria. In light of this, ESMA suggests that the European Parliament, Council and the Commission consider whether to wait until it has delivered positive advice on a sufficient number of non-EU countries before triggering the legislative procedures to extend the passport.

The key takeaway from the ESMA advice therefore is that the widespread introduction of the passport still looks some way off. The advice is good news for those private equity, real estate and infrastructure managers who have traditionally based some operations in the Channel Islands and wish to use the passport when it is introduced, though the global hedge fund industry, most of which is established or managed from the U.S. or Cayman Islands, may need to wait a little longer to discover its EU marketing fate.

In its opinion, ESMA notes that the delay in the implementation of AIFMD together with the delay in transposition in some Member States, make a definitive assessment difficult, and therefore sees merit in the preparation of another opinion on the functioning of the passport after a longer period of implementation in all Member States.

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ESMA’s Advice

The countries covered by the ESMA advice were selected based on a number of factors including the amount of activity already being carried out by entities from these countries under the national private placement regimes, EU national authorities’ knowledge and experience of dealing with their counterparts and the efforts by stakeholders from these countries to engage with ESMA’s process.

The advice is positive for Guernsey and Jersey, as 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 both of those countries.

The advice with respect to Switzerland is also positive, with ESMA noting “that there will be no significant obstacles impeding the potential application of the AIFMD passport to Switzerland, upon the enactment of the amendments to [the Swiss Federal Act on Stock Exchanges and Securities Trading]." The changes to that act are noted as being “at a relatively advanced stage”, with the amended act adopted by the Swiss Parliament in June, and due to enter into force on 1 January 2016. The amendments are described as relating to cooperation and information sharing.

However ESMA recommends delaying the decision on the potential application of the AIFMD passport to the United States, Hong Kong and Singapore.

In particular for the United States, ESMA’s concern is that there are conditions which might lead to a distortion of competition, and so recommends that the European Parliament, the Council and the Commission delay their decision on the application of the passport to the U.S. until such time as those conditions are addressed. ESMA also notes that, in relation to investor protection, 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”.

For Hong Kong, ESMA advises that detailed information on the Hong Kong regulatory framework remains incomplete, and 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. 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 and whether EU AIFMs and EU Alternative Investment Funds (“AIFs”) are treated in the same way as managers and collective investment schemes of Hong Kong in terms of regulatory engagement.

“[For Guernsey and Jersey]…there are no significant obstacles regarding investor protection, competition, market disruption and the monitoring of systemic risk impeding the application of the AIFMD passport.”

“ESMA advises the European Parliament, the Council and the Commission to delay their decision on the application of the passport [for the U.S., Hong Kong and Singapore].”
Finally, for Singapore ESMA advises delaying the decision on the potential application of the AIFMD passport to Singapore, noting in particular that “information regarding the cooperation between National Competent Authorities and the Monetary Authority of Singapore is scarce and difficult to assess”, and further that detailed information on the Singapore regulatory framework remains incomplete. ESMA requires more time 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.

Further Assessments by ESMA

ESMA aims to finalise the assessments of Hong Kong, Singapore and the United States as soon as practicable, and to assess further groups of non-EU countries until it has provided advice on all the non-EU countries that it considers should be included in the extension of the passport.

ESMA lists the following countries as having been identified as the domicile of non-EU AIFMs that market AIFs in the Member States and/or domiciles of non-EU AIFs marketed in the Member States examined, in addition to the six countries it has today reported on: Australia, Bahamas, Bermuda, Brazil, British Virgin islands, Canada, Cayman Islands, Curacao, Isle of Man, Japan, Mexico, Mauritius, South Africa, South Korea, Thailand and US Virgin Islands.

ESMA also gathered intelligence with respect to Malaysia, Egypt, Chile, Peru, India, China and Taiwan, however notes there are currently no supervisory cooperation arrangements in place for the purposes of the AIFMD with those countries, and will therefore continue its efforts to agree a Memorandum of Understanding with the authorities concerned, and will monitor the level of activity by entities from those countries in the EU in order to determine whether a particular jurisdiction should be assessed in detail.

Commission Delegated Act

The Commission is required by Article 67(6) AIFMD to adopt a delegated act within three months after having received “positive advice” from ESMA and taking into account criteria set out in AIFMD, such as those relating to the internal market, investor protection and the effective monitoring of systemic risk. In the delegate act, the Commission must specify the date when the passport rules become applicable in all Member States.

In ESMA’s view, the advice it has delivered today cannot be considered ‘positive’ in the sense of Article 67(4) AIFMD, and therefore suggests that the European Parliament, the Council and the Commission to which the advice is submitted 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 to extend the passport, taking into account such factors as the potential impact on the market that a decision to extend the passport might have.
ESMA’s Opinion

Following its review ESMA concludes that it would see merit in the preparation of another opinion on the functioning of the passport after a longer period, particularly as the delay in the implementation of the AIFMD together with the delay in transposition in some Member States make a definitive assessment difficult.

In relation to the functioning of the passport for EU AIFMs, even at this early stage ESMA has identified several issues in relation to its use, including:

> divergent approaches with respect to marketing rules, fees charged by the National Competent Authorities and the definition of what constitutes a “professional investor”; and

> varying interpretations of what activities constitute “marketing” and “material changes” under the AIFMD passport.

With that in mind, ESMA sees merit in harmonising in the definition of these terms.

Nevertheless, ESMA is of the view that based on available evidence, neither the AIFMD EU passport nor the national private placement regimes have raised major issues in terms of the functioning and implementation of the AIFMD framework.

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