



SHARTSIS FRIESE LLP

One Maritime Plaza ♦ Eighteenth Floor
San Francisco, California 94111-3598

April 11, 2013

VIA E-MAIL

To Our Investment Adviser Clients and Other Friends

**Re: European Union Alternative Investment Fund Managers Directive
("AIFMD")**

The AIFMD is a European Union ("EU") directive that attempts to harmonize regulations concerning investment managers ("**Advisers**") to alternative investment funds ("**Funds**")¹ across the EU.² Generally, the AIFMD regulates the marketing (see section 2.a for definition) and management of Funds in the EU. The AIFMD directive was adopted on July 22, 2011, and will become effective on July 22, 2013. The European Commission has promulgated implementing regulations for the AIFMD, which will become effective on July 22, 2013, and which were adopted without the need for Member State implementation to avoid any potential discrepancies in national rules (the "**Level 2 Measures**"). Nonetheless, each EU Member State is required to ensure that its national laws comply with the requirements of the AIFMD and has until July 22, 2013, to effect necessary changes. Despite this deadline, some Member States have not updated their national laws to reflect the AIFMD, and may not do so in time. This letter provides a brief overview of some material considerations for non-EU Advisers preparing for the coming regulations.

1. Key Implementing Dates. There are three key implementing dates for the AIFMD: July 22, 2013; September 2015; and September 2018.

a. July 22, 2013. For EU-domiciled Advisers or Funds, the AIFMD regulations apply beginning on July 22, 2013. While EU-domiciled Advisers and Funds must comply with the AIFMD's increased disclosure requirements and regulatory oversight, such Advisers and Funds will be permitted to market throughout the EU without the need to comply with each Member State's private placement regime (the "**Passport Regime**"). See the "Re-domiciling Fund" section below regarding whether to consider re-domiciling a Fund to take advantage of the Passport Regime.

¹ The AIFMD defines the Adviser as the legal entity with ultimate responsibility for portfolio and risk management of a Fund. There can be only one Adviser for each Fund. There may be situations under which the Fund itself may be deemed the Adviser.

² It is expected that the AIFMD will be implemented in the broader European Economic Area, which includes Iceland, Liechtenstein and Norway.

Non-EU Advisers and Funds marketing in the EU from July 22, 2013, through September 2015, will be subject to some of the AIFMD reporting requirements, but will not be able to take advantage of the Passport Regime. To understand the compliance requirements, such Advisers and Funds will need to analyze the private placement rules in each Member State where marketing will occur on a Member-State-by-Member-State basis.

b. September 2015. The Passport Regime will be available to Non-EU Advisers and Funds starting in September 2015. From September 2015 through September 2018, non-EU Advisers and Funds may elect to follow either the private placement regimes of the Member States or the Passport Regime. Non-EU Advisers or Funds that desire to use the Passport Regime must designate an applicable Member State of reference for compliance and reporting purposes.³ When the Non-EU Advisers and Funds are in compliance with the applicable regulations in the Member State of reference, they may then take advantage of the Passport Regime.

c. September 2018. After September 2018, it is expected that the national private placement regimes will be terminated and Advisers marketing in the EU will be required to rely on the Passport Regime.

2. Key Exemptions.

a. Reverse Solicitations Not Subject to AIFMD. The AIFMD will not apply if a non-EU Adviser does not “market” a non-EU Fund in the EU. Marketing is defined broadly and covers any direct or indirect offering or placement, at the initiative or on behalf of an Adviser, of a Fund’s interests with investors domiciled or with an office in the EU.

The AIFMD marketing rules provide an exception for “reverse solicitations.” If an EU-domiciled investor on its own initiative approaches a non-EU Adviser concerning investments in such Adviser’s non-EU Funds, placement of interests to such investor should not be subject to the AIFMD. Advisers should approach the reverse solicitation exception with caution, as the AIFMD does not contain detailed guidance for Advisers regarding compliance with the exception. Advisers that intend to rely on the exception should carefully document any interactions with EU investors and should consider the following:

- 1) Generalized statements on websites, at conferences or trade shows, or to the media made outside of the EU that do not target EU investors should not be considered marketing. As a result, Advisers should be able to rely on the exception even if EU investors inquire into a Fund as the result of such generalized statements.
- 2) An Adviser should be able to inform existing EU investors in current Funds that the Adviser will not provide information about future Funds unless such investors affirmatively request such information. If existing EU investors solicit

³ An Adviser marketing in many Member States has discretion to select its Member State of reference, taking into account its activities in Europe, reporting language, marketing campaign and other factors. In all other cases, an Adviser must select its Member State of reference based on guidelines provided in AIFMD Article 37.

information as a result, the Adviser should be able to provide the information and still qualify for the exemption.

3) EU regulators may be more likely to deem “marketing” to include any meeting or correspondence that occurs in the EU regarding a Fund. As a result, responding to inquiries or solicitations for information (including in the situation described above regarding current EU investors), providing offering documents, conducting meetings with EU investors, and other similar activities should take place outside of the EU. For example, Fund documents could be provided to EU investors at meetings held in New York rather than through electronic mail into the EU.

An Adviser that complies with the reverse solicitation exception must also review the private placement regime of each potential investor’s Member State to ensure that such Member State will not regulate the sale or placement of any interests in a reverse solicitation transaction. While it is currently not expected that any Member State will regulate reverse solicitations, this may change as Member States enact final private placement laws in response to the AIFMD. We can assist you in consulting local Member State counsel regarding the current reverse solicitation exception and the effect of any new private placement regulations.

b. Smaller Fund Limited Exemption. If an Adviser cannot rely on the reverse solicitation exemption, another limited exemption from certain AIFMD requirements (although not the entire directive) may be available to smaller Advisers. An Adviser with assets under management that do not exceed either (i) €100m (including assets acquired through leverage), or (ii) €500m (subject to the Adviser not being leveraged and investors having no redemption rights in the first five years of a Fund), do not need to comply with some of the more onerous reporting regulations. Nonetheless, an Adviser taking advantage of this limited exemption remains subject to many of the reporting requirements discussed below.

3. Active Fund Raising in the EU. A non-EU Adviser that cannot rely on the reverse solicitation exception may still market in the EU (at least until September 2018) subject to the private placement regimes of Member States and compliance with the AIFMD reporting requirements described below. To be able to market:

1) The Adviser must comply with the private placement regime in each Member State where marketing will occur.

2) Cooperation Agreements must be in place between the appropriate regulatory authority of the Adviser and the Fund and the regulators in each Member State where marketing will occur. Currently, the Securities and Exchange Commission and the Cayman Islands Monetary Authority are negotiating and finalizing these agreements with each Member State. It is unclear whether such agreements will be finalized in time to allow Cayman-regulated Funds and SEC-regulated Advisers to market in all Member States starting July 22, 2013.

3) The Adviser must comply with specified AIFMD reporting requirements, including providing: (i) certain pre-investment disclosures to potential investors (Article 23); (ii) annual reports to investors and Member State regulators that include, among other things, information concerning material changes from prior reports, activities during the most recent financial year, and remuneration of the Adviser's employees and officers (including carried interest or performance fees or allocations) (Article 22 of AIFMD and Articles 103 to 107 of the Level 2 Measures); (iii) reports to Member State regulators regarding trading instruments, trading market participation and diversification (Article 24 of AIFMD and Article 110 of the Level 2 Measures); (iv) periodic disclosures regarding side-pocket arrangements, new arrangements for managing liquidity and current risk profile and management systems; (v) regular disclosures of changes to maximum leverage levels; and (vi) disclosures regarding private equity investments if investing primarily in non-listed companies registered in the EU.

a. Information Requirements. To comply with the information requirements applicable to Advisers marketing in the EU, an Adviser that does not qualify for exemptions and intends to market within the EU should consider the following:

- 1) While many of the pre-investment disclosures required by the AIFMD may already appear in the Adviser's offering documents, the Adviser should review these documents to ensure compliance.
- 2) The Adviser should consider how to comply with the remuneration reporting requirements, including how to comply with the requirement to report separately remuneration paid to each senior manager and each employee who has a material effect on the applicable Fund's risk profile.
- 3) The Adviser should consider how to implement controls and reporting processes to ensure that periodic and annual reporting information is documented and presented in a manner that complies with the various requirements of the AIFMD discussed in section 3 above.
- 4) The Adviser should review internal policies and procedures to ensure that material changes to the pre-investment information provided to investors pursuant to Article 23 is noted and appropriate consideration is given to any reporting obligations.

b. Private Placement Regimes. As noted above, in response to the AIFMD, a number of European jurisdictions are revising their private placement regimes. Some jurisdictions (including Germany) have proposed prohibiting any marketing activities under their private placement regimes following the implementation of the AIFMD, which may result in non-EU Advisers not being able to market Funds in such jurisdictions.

To comply with applicable private placement regimes, an Adviser should identify the Member States where its marketing activities will occur. The Adviser may then need to consult local counsel regarding the applicable Member States' private placement regimes to determine the steps necessary to comply. This letter does not address the specifics of

Member States' private placement regimes because they vary greatly and many of the regimes are currently in flux.

4. Re-Domiciling Fund. An Adviser that expects to market broadly across the EU may consider re-domiciling its Funds into a Member State to exploit the Passport Regime. Some EU jurisdictions have created legal frameworks to facilitate Funds re-domiciling from locations such as the Cayman Islands. The benefits of being able to exploit the Passport Regime may be offset, however, by increased costs associated with domiciling in the EU and complying with the full range of AIFMD regulations, which include, among other things, regulations concerning capital requirements, establishing remuneration policies that are consistent with effective risk management and do not encourage undue risk taking, establishing organizational policies and procedures to indentify, monitor and prevent conflicts of interests, establishing separate risk management systems, implementing required liquidity and leverage management systems, engaging valuation experts, and complying with new regulations concerning prime brokers.

* * * * *

This letter only generally summarizes the AIFMD, is not intended as specific or complete advice, and is subject to change as the regulations evolve. We do not provide legal advice regarding EU matters, but can assist you in engaging local counsel. For further assistance, please contact Doug Hammer, John Broadhurst, Geoff Haynes, Chris Rupright, Carolyn Reiser, Neil Koren, Jim Frolik, Christina Hamilton, Joan Grant, Ellyn Roberts, Anthony Caldwell or David Suozzi.

SHARTSIS FRIESE LLP