IQEQ

Guide to marketing Alternative Investment Funds (AIFs) in Europe

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Introduction

Europe is the second largest pool of capital in the world after the U.S., with almost EUR120 billion raised in 2021. Many non-EU managers come to Europe once they have reached a certain size in their domestic markets.

There are 27 EU member states and three non-member states that are within the European Economic Area (EEA). Switzerland and the UK are important centres for asset management but are neither an EU member state nor within the EEA.

However, EU regulators are increasing their scrutiny of the marketing and distribution of alternative investment funds (AIFs). In particular, they have focused their attention on reverse solicitation rules, which have long been the go-to strategy for U.S. managers in particular.

For non-EU alternative investment fund managers (AIFMs) of private equity, real estate, debt and credit, hedge, and other AIFs, selecting how you market to EU professional investors is an important decision.

In this guide, we will explain the benefits and drawbacks of each of the three options U.S. and non-EU managers have to raise capital in Europe, including when and how to use each of them.

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What are the options for marketing AIFs?

U.S. and non-EU managers wishing to raise capital in Europe from professional and institutional investors currently have three options:

- Reverse solicitation
- National Private Placement Regimes (NPPRs)
- Alternative Investment Fund Manager (AIFM) marketing passport

Reverse solicitation

Reverse solicitation occurs when the client initiates contact with an investment fund or manager without any prior promotion or advertising from the fund.

The benefits of reverse solicitation include:

- Potential investors may reach out for AIFs investment on an unsolicited basis without further formalities
- Does not require either NPPR or EU marketing passport registrations

The drawbacks of reverse solicitation include:

- Reliance on reverse solicitation carries the risk of regulatory sanctions if a particular investor contact is queried by a regulator and cannot sufficiently demonstrate a genuine reverse enquiry
- European regulators may scrutinise the initial contact from investors from their jurisdiction, and any prior contact or dealings, particularly if there are several or many such investors. This could potentially result in sanctions
- A disgruntled investor may seek to rely on mis-marketing as a basis for a claim against the manager for restitution
- There may not be a clear understanding of the investment fund or manager's business practices, with no access to important information regarding past performance or regulatory history
- Reverse solicitation cannot constitute a distribution strategy

National Private Placement Regimes

NPPRs provide a way for AIFMs to promote AIFs that cannot be marketed under AIFMD's domestic or passporting provisions, mainly for non-EU AIFs and non-EU AIFMs.

The benefits of NPPRs include:

- NPPRs provide a way for AIFMs to promote AIFs that would otherwise not be available to clients, providing access to new investment opportunities
- NPPRs allow fund managers to consider a wider range of investment options, including non-EU AIFs and non-EU AIFMs, facilitating greater diversity and therefore alignment within portfolios

The drawbacks of NPPRs include:

- Only available in European countries which have such regimes, so a NPPR may not be available in each country the manager wishes to market to. Furthermore, NPPR is often limited to a certain number and types of investors
- NPPR requirements will differ among countries so local advice is needed in each country both at the start and on an ongoing basis to monitor any changes to requirements or any withdrawal of a NPPR in a target jurisdiction
- Periodic Annex IV reports are required in each country where the manager has made an NPPR registration

AIFM marketing passport

The AIFM marketing passport is a method of distributing AIF across Europe, facilitated by a streamlined process for fast market access.

How the AIFM marketing passport works:

U.S. and non-EU managers need to create an EU AIF and appoint an EU AIFM since the passport applies only to EU AIFs managed by EU AIFMs. Managers will typically establish their AIF in either Luxembourg or Ireland, although other jurisdictions such as France or the Netherlands are possible.

The benefits of the AIFM marketing passport include:

- Unlike the NPPR system, the marketing passport is enshrined in the AIFM directive and you can therefore be confident that it will continue to apply in all EEA countries (EU plus Iceland, Norway and Liechtenstein)
- Managers can either establish their own AIFM or can appoint a third-party AIFM. An appointed third-party AIFM, such as IQ-EQ, can assist in the set-up of the AIF and can manage the notifications required for marketing the AIF to professional investors (as further defined by MiFID II Directive) on a pan-European basis with relevant applications to the regulators
- There is also a similar pan-European pre-marketing system for EU AIFs pre-marketed by an EU AIFM. This can be used where the AIF has not yet been established and the manager wants to speak to professional investors to gauge their interest in the strategy. A similar notification process by the EU AIFM applies to pre-marketing. IQ-EQ can assist U.S. and non-EU managers wishing to pre-market their proposed EU AIFs in Europe through the appropriate registrations
- Apart from the advantage of being able to market and pre-market on a pan-European basis, this approach also has wider investor acceptability due to the requirement (or preference) of some professional investors for an EU onshore investment vehicle

The main drawback of the AIFM marketing passport:

- The European AIF will likely jointly invest in the same assets alongside your U.S. or other global funds. However, it is not possible to treat the EU AIF as a feeder fund, since if it invests 85% or more of its AuM into any non-EU fund then it loses the ability to use the EU marketing passport

There are a number of approaches which global asset managers can use to manage this issue, including:

- The partial feeder approach
  (limit the fed amount to under 85%)
- The reverse feeder approach
  (the non-EU fund feeds into the EU fund)
- The parallel fund* approach
  (each fund holds its own assets)

* In the case of the parallel fund, there are some choices in terms of whether the parallel funds acquire shares in each target project company in some proportion or whether they jointly invest in an 'aggregator' vehicle.

Own AIFM versus third party AIFM, such as IQ-EQ

If the decision is made to use the EU marketing passport, then an EU AIFM will be required. As noted above, one option is to appoint a third party such as IQ-EQ. The other option is to establish your own AIFM in Europe. The following are some considerations to take into account when setting up an AIFM.

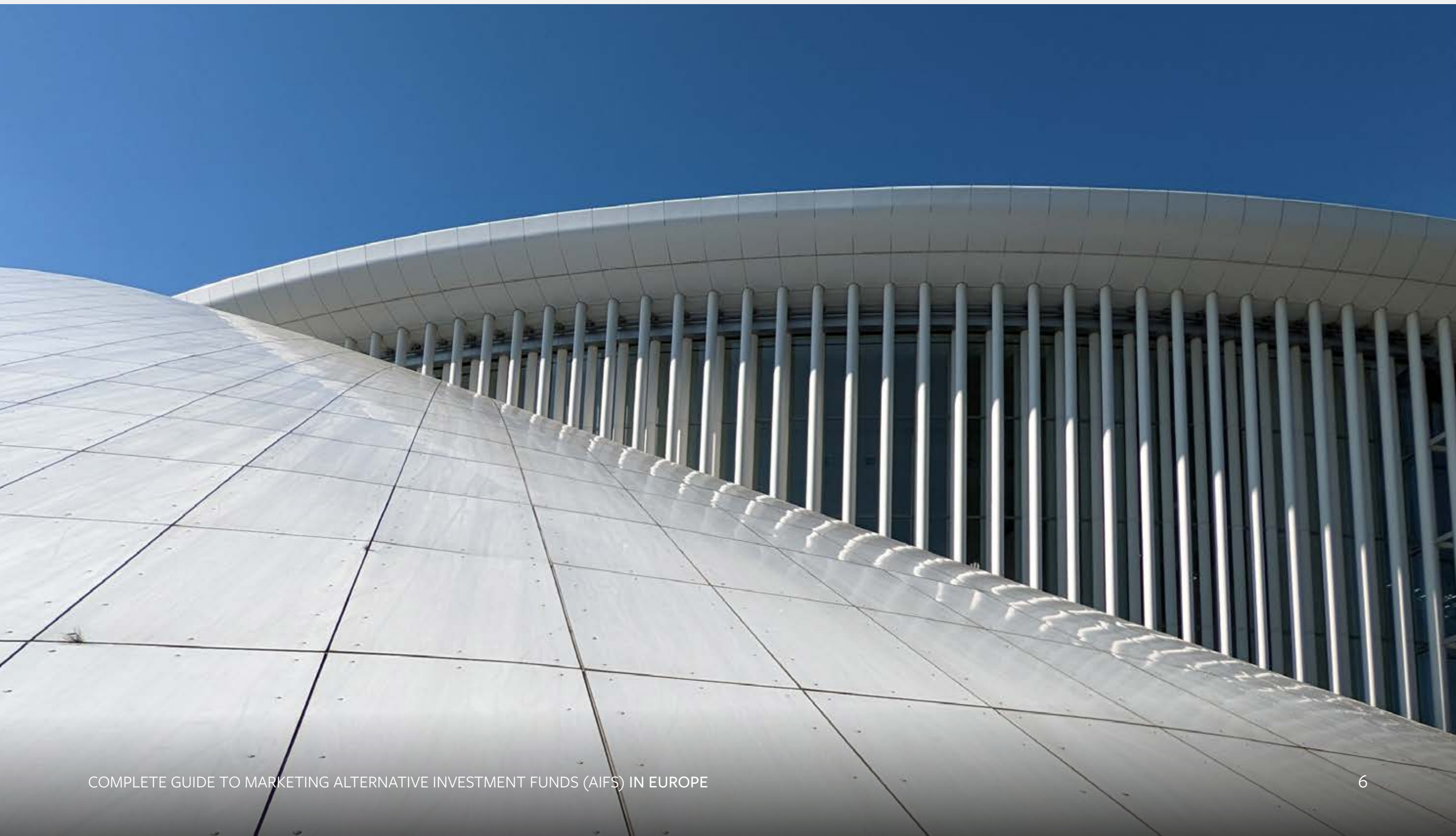
Factors to consider

There are a number of factors to take into account with setting up an AIFM directly. These include:

	Luxembourg	**Ireland**	**France**	**Netherlands**
Capital requirements	AIFMs are subject to regulatory capital requirements*.	AIFMs are subject to regulatory capital requirements.	AIFMs are subject to regulatory capital requirements.	AIFMs are subject to regulatory capital requirements.
Fees and filing by external adviser	CSSF instruction file amount to EUR 15,000, support of external adviser to ensure filing with the CSSF average amount around EUR 100,000.	Regulator fees for service providers, including AIFMs, vary widely and are calculated based on the activity undertaken and the risk rating assigned to the entity by the CBI.** Fees for external advisers also vary and are calculated on a case-by-case basis.	Except for the costs of constituting a management company, the approval of the management company is free of charge.	AFM instruction file amount to EUR 10,500, support by AFM on application review (EUR 200 p/hour with a maximum of EUR 100,000) and recommendation to use external adviser to support with AFM filing averages amount around EUR 50,000.
Senior management	Minimum staffing requirements set by CSSF. Estimated cost of staffing at least c. EUR 350,000 pa. Note: this is the minimum, as the CSSF requires significantly higher headcount from some AIFMs (with high AuM).	Minimum staffing requirements set by the CBI. Estimated cost of staffing at least c. EUR 350,000 pa. Note: this is the minimum CBI requirement. Significantly higher headcount may be required from some AIFMs if they have higher AuM, for example.	The portfolio management company must have at its disposal a full-time professional staff whose expertise is relevant to the activities: at least two financial directors and one person in charge of internal control and compliance.	Minimum staffing requirements set by the AFM. Estimated costs for assessment of persons involved in the management of the company will be EUR 700 for each person.
Board costs	CSSF approval required prior to the appointment of directors, minimum three members. Costs to support the board should be considered; approx. EUR 20,000 for Director and Officers Insurance and a Company Secretary. An overall budget of circa EUR 100,000 pa should be allocated.	CBI approval required prior to the appointment of directors, minimum three members. Independent non-executive – directors fees listed as EUR 25,000 - EUR 30,000. Additional costs to support the board could include c. EUR 20,000 for Directors & Officers Insurance and a Company Secretary. An overall budget of circa EUR 100,000 pa should be allocated.	Board members are required only for a limited number of French fund structures that have a legal personality. Costs are approximatively EUR 4,000 to EUR 6,000 per annum per mandate.	AFM approval required prior to the appointment of directors, minimum two members. Costs to support the board should be considered; approx. EUR 20,000 for Director and Officers Insurance. An overall budget of circa EUR 75,000 - EUR 100,000 should be allocated (includes corporate governance, bookkeeping, financial and regulatory reporting).

	Luxembourg	Ireland	France	Netherlands
Office support costs	Insurance costs, utilities, and rental fees.	Insurance costs, utilities, and rental fees.	1) Annual contribution to the AMF equal to the amount of net AuM at 31 Dec of the previous year, multiplied by 0.008%, with a minimum of EUR 1,500 2) All investment firms must join a professional association of their choice (with required annual fee) 3) Insurance costs, utilities, and rental fees.	Substance requirements apply. Minimal local office presence required, which can be budgeted at EUR 75,000 - EUR 125,000 pa. including insurance, office equipment and utilities, and rental charges for a small office (up to 5 people).
Length to set up your AIFM	Estimated 6-12 months from the time of a complete submission to the CSSF. Timing depends on CSSF responsiveness, but recently response times have tended longer. Material issues that arise during the application process and individual response times can create delays.	Estimated 6-9 months from the time of a complete submission to the CBI. Timing depends on CBI responsiveness, but recent response times have tended longer. Material issues that arise during the application process and individual response times can create delays.	Estimated 9-12 months from the submission of a complete application.	Estimated 13 weeks to 9 months from the time of a complete submission to the AFM. Timing depends on AFM responsiveness. Material issues that arise during the application process and individual response times can create delays.

* Minimum regulatory capital required is the greater of; EUR 125,000 plus the greater plus 0.02% of AuM over EUR 250,000 and one quarter of fixed annual overheads. Maximum capital requirement is EUR 10,000,000. ** Further information can be found on the CBI's website: Industry Funding Levy for Fees | Central Bank of Ireland.



Potential for future changes affecting your own AIFM

Given the current regulatory environment, any future changes to the AIFMD regulatory framework are only likely to increase regulatory oversight and responsibilities. For this reason, as well as those above, many U.S. and other large global asset managers raising capital in Europe choose to employ a third-party AIFM of substance such as IQ-EQ. In this scenario, the time factor of setting up an AIFM is avoided and the costs above and responsibility for managing future changes are borne by IQ-EQ.

How do European institutional investors perceive the use of a third-party AIFM?

In our experience, institutional investors regard an EU third-party AIFM positively. The U.S. and non-EU asset manager (whose strategy they wish to invest but who may be less established in Europe) is supported by an EU-regulated entity of substance. This entity is able to manage the regulatory and compliance aspects of the fund while delegating portfolio management to the asset manager, and is already plugged in (from an operational and regulatory due diligence point of view) with relevant EU stakeholders to ensure straight management of the fund.

Resources, commitment, and misdirection

Finally, and perhaps most importantly, by appointing a third-party AIFM such as IQ-EQ, you avoid the need to manage a regulated entity within your group with the time commitment and management focus that would require. Instead, our clients are able to focus on their core asset management and investor relations functions and leave the rest with us.

In addition to the above, the asset manager will need to consider the following options for how to implement their marketing and distribution strategy.

Distribution and Marketing Agent

A distributor or a marketing agent must be employed by the fund to carry out the sales and marketing activity in the EU. Such placement or marketing agent must be authorised under an EU regulatory regime within the target jurisdiction (such as a bank or a MiFID II regulated firm). The distributor or marketing agent may use the support of different financial intermediaries, such as business introducers.

Own Employees

If you intend to use your own sales force to market or pre-market in Europe, you need to ensure that the relevant authorisation has been granted to the entity in charge of the marketing activity (such as a MiFID II). Depending on the fact pattern, there are a number of approaches which asset managers take in this situation such as tied agency, ‘chaperoning’, or secondment.

IQ-EQ marketing support services

As part of its global collective portfolio management authorisation, IQ-EQ may ensure fund marketing under its own responsibility. As such, the team can help you to design and set up the marketing strategy of the fund, ensuring the relevant operational activity with the support of the sponsor of the fund or different financial intermediaries.

The best jurisdictions for an AIFM

Luxembourg

Luxembourg is a global hub for international fund distribution and home to Europe's premier investment fund centre, which is the second biggest in the world. It is the European leader in international securities listings with the first and only exchange platform (LGX) dedicated to sustainable green and social securities. LuxSE is the international market leader in the listing of Dim Sum Bonds and was the first Islamic fund centre in Europe. Luxembourg is a founding member of the European Union and one of the three official seats of the European institutions. It is also home to our Group Headquarters.

France

France is a very well-known and established market in the worldwide fund industry, with more than 700 asset managers (including 400 management companies) dedicated to the private class. Key international players with AuM higher than EUR 30,000,000,000 such as Ardian, Tikehau and Eurazeo are growing very fast and have an international exposure. Other players with less than EUR 10,000,000,000 AuM such as Andera Partners, LBO France, etc. have structured multi-strategy teams to invest their private equity, private debt, real estate and infra funds.

Most of the market (70% of 400 management companies) is composed of entrepreneurial firms with less than EUR5 Bn AuM focusing on specific strategies (health, tech, buy out, growth, etc.). One specificity on the French market: the sovereign fund "BPI France". BPI is acting as a sponsor to support entrepreneurial funds (i.e., 200 investments structured as fund of funds) but also to finance private companies directly through different strategies (venture, etc.). "Lac 1" is the BPI large cap funds with a total commitment of EUR 4,000,000,000.

Ireland

Companies seeking to gain or maintain access to EU markets are increasingly basing themselves in Ireland due to its competitive, pro-business environment. Ireland has the fastest growing economy in the Eurozone and benefits from sustainably managed finances and an 'A' grade rating from all major credit rating agencies. The country is home to over 8,000 Irish domiciled funds with net assets of EUR4.1 trillion, as of 2021. It is a recognised centre of excellence and benefits from an open and transparent tax regime which is fully compliant with OECD guidelines and EU law. Ireland serves as a gateway to Europe with full market access to its 500 million consumers and its highly educated, English-speaking workforce provides an abundance of professionals with excellent technical, language and customer service skills.

Netherlands

The Netherlands has always been a centre for financial innovation, with the world's first publicly traded company, the first stock exchange, and the first European option exchange. Now it is home to the Euronext Stock Exchange, a pan-European exchange spanning the Netherlands, Portugal, Belgium, France, Ireland and the UK. Amsterdam is considered one of the leading finance centres in Europe, and a financial centre which includes banking, asset management - and in recent years - increased development with fintech enterprises.

United Kingdom

UK AIFMs no longer have access to the AIF marketing passport but remain attractive to managers who want to market to UK and Swiss investors only or use NPPR to access EU investors. The UK also has a significant listed AIFs sector especially property funds known as Real Estate Investment Trusts (REITS).

UK delegation options

The UK is the largest European centre for alternative asset management including hedge, private equity, venture capital, private debt, real estate and ESG funds, second only to the US globally. If U.S. or Asian managers want individuals based in the UK (especially London as a global financial centre) to manage and advise the funds, then an EU AIFM can delegate portfolio management or investment advice to a UK firm directly authorised by the FCA. Alternatively, delegation can be an IQ-EQ host MiFID firm if the fund invests liquid securities or the UK sub advisor can become an appointed representative of an IQ-EQ Principal Firm and the individuals become Approved Persons of the firm if the fund invests in illiquid investments only such as private equity or real estate.

Jurisdictions to set up a National Private Placement Regime (NPPR)

The AIFMD 'passport' allows EU investment funds to be distributed across the EU. However, the EU investment fund market is still predominantly a national market; in fact, only 3% of EU alternative investment funds (AIFs) are registered for sale in more than three Member States.

Jersey and Guernsey provide a valuable alternative in the domicile selection for private funds, available only to qualified, sophisticated investors. Jersey and Guernsey AIFs can be marketed to EU member states via the National Private Placement Regime. The NPPR is a tried and tested route and, most significantly, it is quicker and less expensive than the onshore full AIFMD model.

Consideration should also be given to the number of targeted investor domiciles. If only a handful of investor domiciles will be targeted, NPPR can be a suitable route to market. The latest European Commission statistics show that 97% of passportable funds raised money from three or fewer jurisdictions. NPPR works thanks to bilateral agreements between Jersey's and Guernsey's financial regulator and those in each EU Member State. Both jurisdictions have these in place with the majority of EU countries.

Benefits of using Jersey and Guernsey fund vehicles for NPPR:

- Light-touch yet robust regulation that meets international standards
- Easy access to EU investors through NPPRs if marketing into the European Economic Area (EEA) is desired
- One to three-day regulatory turnaround for speed and ease of establishment and regulation
- Works for open or closed-ended funds and any type of investment vehicle
- Can be established using any of the common forms of investment vehicle, such as a limited partnership, company, protected cell company or a Unit Trust constituted under the laws of Jersey or Guernsey

How can IQ-EQ assist?

We are an investor services provider that assists global asset managers in establishing and operating UCITS, AIF and NPPR structures across Europe. As part of IQ-EQ, our scale and global reach ensure our clients remain compliant with all legislation and jurisdictional regulations across diverse sectors and asset classes. We offer clients market leading technology which we can tailor to meet your specific needs. Whether you prefer a hosted or standalone fund solution, we can help you bring your fund to the European market as quickly and successfully as possible.

Meet the team

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