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Legal Briefings

PRE-MARKETING AND REVERSE SOLICITATION IN THE EU – THE IMPACT ON EU FUND MANAGERS AND OFFSHORE FUND MANAGERS

October 2022

1. Background

The Alternative Investment Fund Managers Directive[1] ("**AIFMD**"), which came into effect on 21 July 2011[2], as a policy response to the 2008 global financial crisis, aimed to provide a harmonized, stringent and more transparent regulatory and supervisory framework for both EU alternative investment managers ("**EU Fund Managers**") and non-EU Fund Managers.

Further rules and regulations from the European Parliament and the Council of the European Union in relation to the cross-border distribution of funds were published on 2 August 2021[3] ("**Rules**"), which amend the AIFMD. The Rules were implemented in order to address the divergences in the different pre-marketing conditions between EU Member States and create a harmonized definition of "pre-marketing" and the conditions under which an EU Fund Manager can engage in pre-marketing.

However, despite the objective of the Rules, there is still much uncertainty as to the impact of the pre-marketing rules on reverse solicitation (i.e. where a prospective investor approaches an investment fund or its manager, by the investor's own exclusive initiative) in each Member State, in particular in relation to non-EU Fund Managers.

2. What is "pre-marketing" and who does it impact?

The pre-marketing provisions in the Rules apply directly to EU Fund Managers. The Rules are silent on the application to non-EU Fund Managers.

Pursuant to the Rules, pre-marketing is addressed to a potential professional investor and concerns an investment idea or investment strategy in order to test an investor's interest in an alternative investment fund ("**Fund**").

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[1] Directive 2011/61/EU of The European Parliament and of The Council of 8 June 2011 on Alternative Investment Fund Managers and amending Directives 2003/41/EC and 2009/65/EC and Regulations (EC) No 1060/2009 and (EU) No 1095/2010

[2] EU Member States given until 22 July 2013 to implement its requirements

[3] Rules (EU) 2019/1160 and Regulation (EU) 2019/1156 of the European Parliament and of the Council of 20 June 2019 amending Rules 2009/65/EC and 2011/61/EU

The definition of pre-marketing is broad enough (i) to encompass fundraising roadshows, a due diligence questionnaire requested by potential investors, a teaser document and any other materials which refer to the investment strategies of a Fund, and (ii) to capture a Fund which has not even been incorporated at the time of such activity.

3. What are the restrictions in relation to pre-marketing?

(a) Documents circulate to investors

During the course of pre-marketing, an EU Fund Manager is not permitted to distribute subscription forms (including in draft form) and facilitate a subscription into the Fund. If an offering document is issued to a potential professional investor during pre-marketing, this should not contain sufficient information to allow an investor to take an investment decision and must include certain disclosures which emphasize that the offering document does not constitute an offer or invitation to subscribe and is subject to change.

(b) Duration of pre-marketing

Any subscription by professional investors within 18 months of the EU Fund Manager starting pre-marketing of a Fund is automatically considered as a result of the marketing and is subject to notification procedures in the EU, as set out under paragraph (c) below.

(c) Notification procedure

An EU Fund Manager is required within two weeks of commencing pre-marketing in an EU Member State to send an informal letter to the competent authorities of its home Member State specifying (i) the Member States in which it is or has engaged in pre-marketing, (ii) the periods during which pre-marketing is taking place or has taken place, and (iii) details of the Fund. It then becomes the responsibility of the competent authorities of the home Member State of the EU Fund Manager to promptly inform the competent authorities in the EU Member State in which the EU Fund Manager is or has pre-marketed a Fund.

4. Who can pre-market?

The Rules restrict the ability of EU Fund Managers to appoint non-EU distributors or placement agents to conduct pre-marketing on behalf of a Fund. EU Fund Managers are only permitted to appoint certain types of authorised EU financial institutions to engage in pre-marketing activities ("**Third Party AIFM**").

5. Do the Rules impact non-EU Fund Managers?

The Rules apply to EU Fund Managers and are not intended to apply to non-EU Fund Managers (e.g. fund managers from the Cayman Islands, U.K., U.S., and the British Virgin Islands) that pre-market their funds into Member States using (i) the relevant National Private Placement Regime of each Member State, or (ii) a Third Party AIFM.

However, a non-EU Fund Manager that has established a Fund managed by a Third Party AIFM that wishes to market the Fund to investors in Member States will be affected by the Rules indirectly, as the Third Party AIFM will need to comply with the Rules.

It is also important to note that it is up to each Member State to pass implementing legislation to confirm whether the Rules (including the pre-marketing provisions) apply to non-EU Fund Managers. For example, Germany, The Netherlands and Luxembourg have passed laws to confirm that the Rules will apply to non-EU Fund Managers. In such a case, as a non-EU Fund Manager will not have a home Member State regulator, a pre-marketing notification will be made to the regulator of the Member State where the non-EU Fund Manager is applying to market to investors.

6. Has there been any further guidance issued in relation to reverse solicitation?

Following the Rules, the European Commission wrote a letter to request for further guidance on reverse solicitation from The European Securities and Markets Authority ("**ESMA**") on 24 September 2021 ("**EC Letter**"), in order to submit a report of the European Parliament and the Council. The EC Letter requested input from the national competent authority of each Member State (together, the "**NCAs**"), in particular in relation to data from asset managers on the use of reverse solicitation.

ESMA responded to the EC Letter on 17 December 2021, in a response which stated that almost all NCAs have no readily available information on the use of reverse solicitation from asset managers and investor associations. However, the absence of figures on reverse solicitation was noted to be explained by the fact that under EU law, asset managers are not subject to any obligation to report any information on subscriptions from reverse solicitation to the applicable NCA.

ESMA has hinted at the possibility of introducing new reporting requirements in order to facilitate the collection of information on reverse solicitation across the EU.

7. Any further amendments to AIFMD?

The European Commission published a proposal on 25 November 2021 to further amend AIFMD ("**AIFMD II**"). However, AIFMD II does not provide for further measures to clarify and harmonize the application of the reverse solicitation regime under AIFMD (as amended by the Rules).

AIFMD II includes a condition that non-EU Fund Managers and non-EU Funds must not be established in jurisdictions identified as high risk under the EU's anti-money laundering rules.

8. Practical considerations

The Rules mean that each EU Fund Manager and non-EU Fund Manager will need to carefully select the EU jurisdictions in which it intends to pre-market to investors and to obtain advice in respect of the specific local laws.

It is advisable for an EU Fund Manager and any non-EU Fund Manager that is caught by the implementing legislation of a Member's State, as set out in paragraph 5 above to (i) seek appropriate advice in order to comply with the applicable local law, (ii) conduct due diligence on any Third Party AIFM used (i.e. to check it has the appropriate regulatory license), and (iii) make sure that any pre-marketing is adequately documented.

9. Is any notification of marketing to EU investors required to be made to CIMA in respect of a Cayman Fund?

Part IIIA (EU Connected Funds) of the Cayman Islands' Mutual Funds Act (As Revised) ("**MFA**") and certain amendments to the Cayman Islands' Securities Investment Business Act (As Revised), which came into force on 1 January 2019 ("**Amendment Laws**"), were implemented in order to ensure consistency with the AIFMD.

The key changes brought into effect by the Amendment Laws include (i) the creation of a framework for Cayman Islands Funds and managers to voluntarily "opt-in" and be licensed by the Cayman Islands Monetary Authority ("**CIMA**"), via a passport regime, to the AIFMD system in order to manage or market funds to investors in the EU, and (ii) the introduction of a definition of "**EU Connected Fund**".

An EU Connected Fund is:

- a company, unit trust or partnership carrying on business in or from within the Cayman Islands, which issues shares, units or partnership interests that carry an entitlement to participate in the profits or

gains of the fund (whether open or closed-ended) the purpose of which is the pooling of investor funds; and

- is either (i) managed by a person whose registered office is in an EU Member State (being either a member of the EU or a part of the EEA in which the AIFMD has been implemented) and whose regular business is managing one or more alternative investment funds, or (ii) marketed to investors or potential investors in an EU Member State.

If a Cayman Islands Fund meets the definition of an "*EU Connected Fund*", it is required to notify CIMA within 21 days of the commencement of marketing in a country or territory within the EEA, that it is marketing in a country or territory within the EEA.

Furthermore, as an EU Connected Fund, the Fund is required to comply with the following on-going notification obligations (i) notify CIMA of any changes to the particulars previously submitted to CIMA, (ii) notify CIMA when it has ceased marketing in all Member States of the EEA, and (iii) provide written confirmation to CIMA on an annual basis that there has been no change to the particulars previously submitted to CIMA.

The MFA also introduced a formal procedure for EU Connected Funds to request attestations or confirmations of status from CIMA (where required to be submitted to regulators of particular Member States in which it is proposed to market the EU Connected Fund) upon the submission of certain details and payment of a fee to CIMA.

This publication is not intended to be a substitute for specific legal advice or a legal opinion. For specific advice on Pre-Marketing and Reverse Solicitation in the EU, please contact your usual Loeb Smith attorney or:

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