

**C L I F F O R D
C H A N C E**

NAVIGATING PRIVATE PLACEMENTS – GERMANY

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NEW YORK, 20 MARCH 2017**

AIMA

TABLE OF CONTENTS

- 1. German concept of fund marketing**
- 2. Notification process**
- 3. Alternative routes to Germany?**
- 4. Questions?**



GERMAN CONCEPT OF MARKETING

GERMAN CONCEPT OF MARKETING (1)

"Marketing" is defined as direct or indirect offering or placement of units or shares of a fund.

Offering	means any offer to subscribe, including: (i) <u>contractual offers</u> that can be accepted by a potential investor and form a binding contract; and (ii) <u>invitations to the investor to make an offer</u> to subscribe for the units or shares of a fund
Placement	means active distribution. Reacting to an (unsolicited) order / offer made by the investor does not constitute marketing
"Indirect" offering / placement	refers to situations where a manager distributes units or shares of a fund through (a chain of) intermediaries

Not limited to public offering or placement / no private placement exemption.

- Under the former German private placement rules no notification / approval was required for marketing to a restricted circle of persons. A circle of persons was deemed restricted if:
 - (i) the persons were individually known by the offeror; and
 - (ii) they were addressed by it on the basis of a selected choice according to individual aspects, and
 - (iii) they required no information by means of a prospectus as investors usually do.
- Already the intention to market units or shares of a fund in Germany has to be notified to BaFin and marketing may only be commenced upon BaFin's approval.

GERMAN CONCEPT OF MARKETING (2)

German statutory exemptions from the definition of marketing are very narrow, e.g.:

- only the name of the fund is published; or
- only the NAV is published; or
- only the tax reporting is made; or
- the fund is described in the offering documents for fund-linked securities.

Marketing to professional and/or semi-professional investors only occurs if:

- it is made at the initiative of the manager or on behalf of the manager, and
- the professional and/or semi-professional investors are domiciled or have their registered office in Germany or another EEA member state.

GERMAN CONCEPT OF MARKETING (3)

Only fund-specific information may constitute marketing.

- Strictly manager related information (bios, track record, deal pipeline etc.); or
- strictly strategy related information; or
- general overview on the trends of the investment market and presenting potential investment opportunities does not constitute marketing.

BaFin takes the view that marketing requires the "existence" of a fund.

For these purposes, the "existence" of a fund is in particular assumed in cases where:

- the fund has already been established; or
- the fund is ready for offering, i.e. where the fund documentation is in materially final form.

Approaching potential investors with fund documentation in draft form, which provides for gaps to be negotiated with potential investors (and, hence, upon which no investment decision can be made), does not constitute marketing.

The designation of a name (e.g. "XY Equity Chance Plus") constitutes a rebuttable presumption that the fund is "existing".

GERMAN CONCEPT OF MARKETING (4)

Marketing to an existing investor?

- According to BaFin, the offering or placement of additional units or shares of the same fund to an existing investor does not constitute marketing.
- No marketing occurs if the manager only complies with information requirements towards existing investors under the KAGB or the law of its home jurisdiction.

Transfer of units or shares of a fund by an existing investor (secondary trading)?

- In principle, secondary trading does not relate to the capital raising in that fund and does, hence, not constitute marketing.
- It is not intended by the German legislator to hinder trading between investors, unless the German marketing rules are (intended to be) circumvented, e.g. where the units or shares of a fund are temporarily purchased by an investor with the objective of distributing them to a wider investor base provided that such initial investor is acting at the initiative or on behalf of the manager.

GERMAN CONCEPT OF MARKETING (5)

Passive marketing / Reverse solicitation

- Distribution at the unsolicited initiative of the investor does not constitute marketing.
- Only available in relation to professional and semi-professional investors.
- BaFin follows a conservative approach and interprets reverse solicitation very narrowly. In the absence of clear guidance from BaFin the exact scope of reverse solicitation is left to interpretation taking into account the facts and circumstances on a case-by-case basis.
- Cannot be reverse engineered after the fact – must be genuine.

To do / Compliance requirements

- Manager must maintain full audit trail of, and sufficiently document and prove, the unsolicited contacts by the professional and/or semi-professional investors.
- Confirmation from the investor that the offering or placement of units or shares of the fund was made at its initiative should be helpful to demonstrate that this is the case, provided, however, that the German marketing regime is not (intended to be) circumvented.
- Confirmation should be obtained before the offer or placement takes place.

GERMAN CONCEPT OF MARKETING (6)

Open questions in the context of reverse solicitation

- Tainting effect of pre-marketing activities? Cooling-off period required?
- Specific versus general enquiries? “send me information on your latest real estate debt fund” versus “do you have information on funds currently being raised”
- Websites accessible from Germany as marketing in Germany?

Finalising "draft documentation"

- Professional and/or semi-professional investors have been approached with fund documentation in draft form (which provides for gaps to be negotiated with potential investors and, hence, upon which no investment decision can be made).
- Fund documentation may be finalised and subscribed by these investors without any BaFin notification being required.
- Concept, however, assumes that investors are able to negotiate / influence the structure and, hence, do not need the protection by a formal notification procedure. No pre-defined limitation of investors, but factual limit.



NOTIFICATION PROCESS

CLASSIFICATION OF INVESTORS

Professional Investors

Professional investors within the meaning of AIFMD also qualify as professional investors under German law. This includes all professional investors within the meaning of Annex II of the European Markets in Financial Instruments Directive (MiFID) or who have opted for the status of professional investor.

This category captures, in particular, banks, investment firms, insurance companies, national and regional governments but also corporates exceeding certain thresholds.

Retail Investors

While AIFMD treats all investors who are not professional investors as retail investors, German law splits this category into two sub-categories: semi-professional investors and private investors.

Semi-professional investors include (among others):

- investors with a committed investment amount of at least EUR 200,000 and in respect of which the manager or its distributor has confirmed the suitability of the investment; and
- investors with a committed investment amount of at least EUR 10,000,000.

MARKETING TO PROFESSIONAL INVESTORS IN GERMANY (1)

Minimum Requirements under Art. 42(I) of the AIFMD (1)

MoU

- There must be a cooperation agreement between the competent authorities of the non-EU manager (and non-EU fund, if different from the location of the manager) and BaFin.
- BaFin has already entered into Memoranda of Understanding with several supervisory authorities of the non-EEA countries, including in the USA: SEC, CFTC and FED/CC.

FATF

- The home country of the non-EU manager (and non-EU fund, if different from the location of the manager) must not be classified as a "Non-Cooperative Country and Territory" by the Financial Action Task Force (FATF).
- This is understood to be a reference to jurisdictions that appear in either part of the list of "High-Risk and Non-Cooperative Jurisdictions" which is published and updated by FATF from time to time.

Annual Report

- The non-EU manager must provide BaFin and, upon request, investors with an annual report for each of the funds it markets in Germany no later than six months after the end of the fund's financial year.
- The annual report must contain, inter alia, financial statements, a description of the activities of the manager for that financial year and information about the remuneration paid by the non-EU manager to its staff, including the total amount of carried interest payments and the aggregate amount of remuneration broken down by senior management and certain other members of staff.

MARKETING TO PROFESSIONAL INVESTORS IN GERMANY (2)

Minimum Requirements under Art. 42(I) of the AIFMD (2)

Disclosure to Investors

- The non-EU manager must provide prospective investors with the latest annual report and certain information about the proposed investment.
- Pre-investment disclosure must be made available in accordance with the fund rules and includes, inter alia, a description of all fees, charges and expenses (including maximum amounts) borne by investors, details of any preferential treatment and information about brokerage relationships.
- Requirements for periodic disclosure relate to, inter alia, material changes and the percentage of the fund's assets subject to side pockets and similar arrangements.

Periodic Reporting

- The non-EU manager must regularly report to BaFin various information relating to both the manager and the fund on the basis of a form specified by ESMA.
- The reporting items are similar to Form PF, but valuation and leverage calculations are made differently.
- Private equity type funds are subject to annual reporting. In other cases the frequency is quarterly or half yearly depending on the AuM of the non-EU manager and the fund.

Acquisition of Major Holdings and Control

- The non-EU manager must comply with specific disclosure obligations if the fund invests in a non-listed EU company (above certain thresholds) or an EU issuer. For a period of 24 months following the acquisition of control any 'asset stripping' is prohibited.
- The acquisition of substantial stakes in a non-listed EU company must be notified to the company, its shareholders and BaFin. If the funds acquires control in a non-listed EU company, the intentions with regard to the future business of the company and the likely effects on employment must be disclosed to the company, its shareholders and its employees.

MARKETING TO PROFESSIONAL INVESTORS IN GERMANY (3)

German Gold-Plating in § 330 KAGB

Notification Procedure

- The notification must include detailed information and documents on both the fund and the manager. The non-EU manager must inform BaFin about all material changes of circumstances described in the notification and must provide BaFin with information on request.
- BaFin will review whether the submitted documents are complete and request any missing documents within 20 business days. After the submission of the complete notification BaFin will inform the manager within two months whether marketing of the fund may be commenced.

Depositary Lite

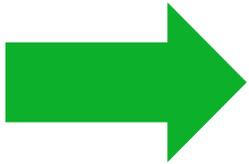
- The non-EU manager must appoint one or more entities to perform certain depositary functions.
- These functions include: (i) monitoring of the fund's cash; (ii) safe-keeping of assets (holding in custody / verifying the fund's ownership); and (iii) general oversight matters such as the NAV valuation (if applicable), compliance with investment restrictions and calculation of distributions made to investors.
- The relevant entities do not need to be located in the same country as the non-EU manager or the fund.

Retail Barrier

- The non-EU manager needs to put in place arrangements which are appropriate to prevent the fund from being marketed to retail investors, including cases where the manager relies on activities of independent entities for marketing purposes.
- The non-EU manager needs to enter into appropriate agreements with all marketing partners and include appropriate legends into all offering documents and advertising material.
- If the marketing is conducted via the Internet or other electronic systems, there must be separate access channels for each type of investor (retail, semi-professional and professional investors).

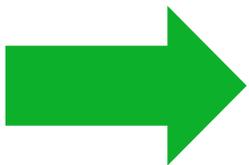
MARKETING TO RETAIL INVESTORS IN GERMANY

Semi-professional investors: Full AIFMD compliance required



- The non-EU manager needs to manage the fund in full compliance with AIFMD.
- No depositary lite regime available, depositary is subject to full AIFMD regulation.
- In addition to the AIFMD minimum requirements, the manager needs to comply with, inter alia, remuneration and delegation requirements.
- The notification must include additional information and documents setting out how the manager intends to comply with its duties under AIFMD.
- The review period of BaFin is four months. This period is reduced to two months for all funds intended to be marketed after the first notification.

Retail investors: Full AIFMD Compliance plus “comparability” required



In addition, structure of the fund, e.g.

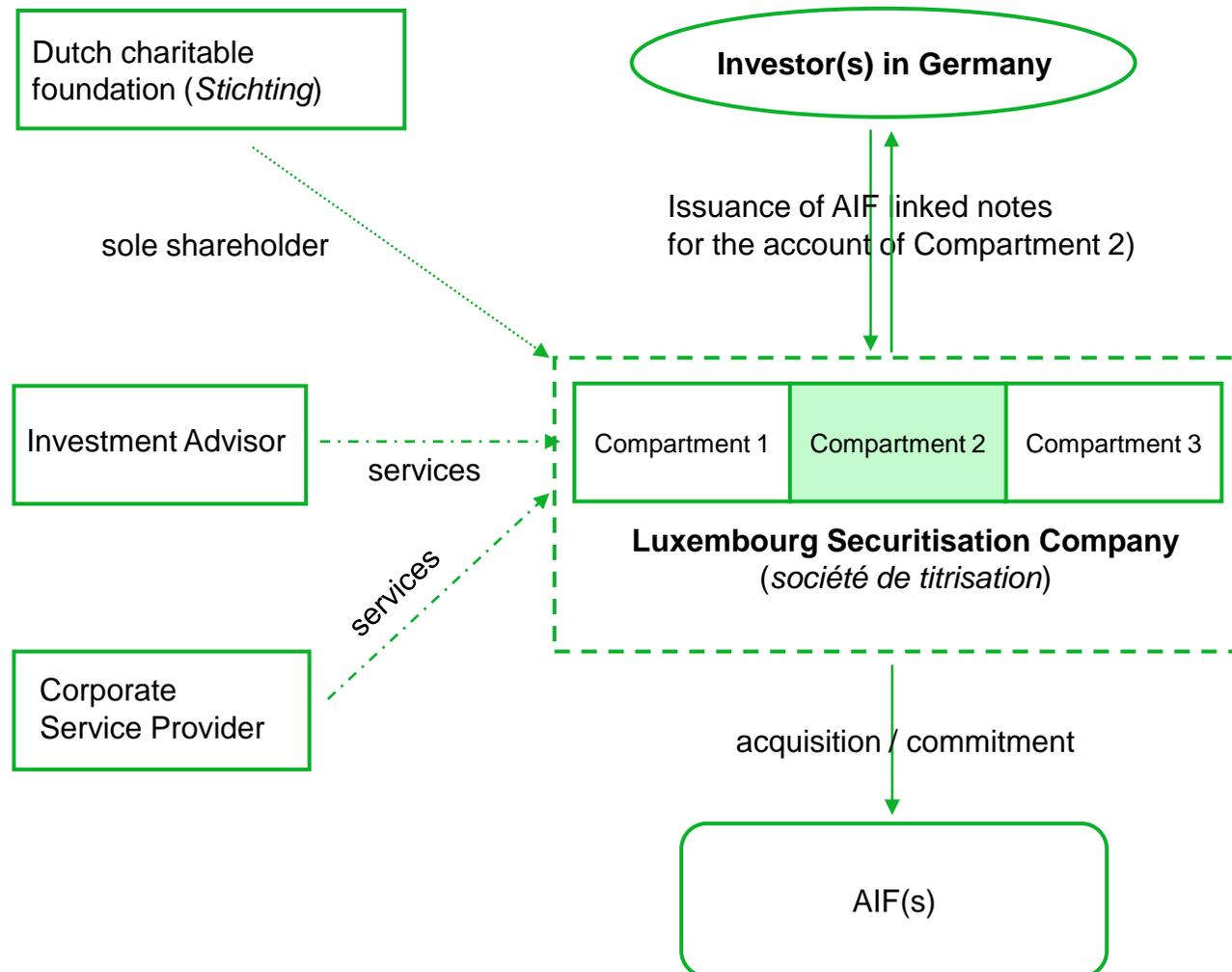
- Investment universe / restrictions,
- Principle of risk diversification,
- Restrictions on leverage, and
- Prohibition of short selling

...must be comparable to German fund type.



ALTERNATIVE ROUTES TO GERMANY

BASIC STRUCTURE (SIMPLIFIED)



CONSIDERATIONS ON THE ISSUER (1)

Typically established in the legal form of a Luxembourg *société anonyme*....

- Minimum share capital of EUR 30,000; to be (partly) paid up to at least 25%.
- The *société anonyme* can be established by a sole shareholder. Typically in an orphan structure, the shares will be held by a [Dutch Stichting] as sole shareholder.

.... with a compartment structure

- Compartments are independent parts of the estate of the *société anonyme*, distinguishable from the other estate of the *société anonyme* and any other compartment of the *société anonyme*.
- Each compartment shall be treated as a separate entity.
- A separate compartment will be created for each issuance of (AIF linked) notes.
- Rights of holders of (AIF linked) notes issued for the account of a compartment are limited to the assets of that compartment.

CONSIDERATIONS ON THE ISSUER (2)

...and as securitisation company (*sociétés de titrisation*) ...

- The securitisation company which meet the definition provided for by the Luxembourg Securitisation Law benefit from a specific legal framework to carry out their activities.
- Securitisation companies subject to the Luxembourg Securitisation Law enjoy high legal certainty because the Luxembourg Securitisation Law expressly lays down the principles of recognition of subordination, limited recourse and non-petition provisions, as well as segregation of compartments, aiming to ensure the securitisation undertaking's bankruptcy remoteness.

.... might be able to benefit from the “securitisation special purpose entities” exemption under the AIFMD

- Pursuant to Article 4 para. 1 lit. (an) of the AIFMD, "securitisation special purpose entities" means entities whose sole purpose is to carry on a securitisation or securitisations within the meaning of Article 1 para. 2 of Regulation (EC) No 24/2009 of the European Central Bank of 19 December 2008.
- In item 19 of its questions and answers on securitisations, the CSSF confirms that a Luxembourg securitisation company under the Luxembourg Securitisation Law benefits from the "securitisation special purpose entities" exemption provided that it carries on a securitisation within the meaning of Article 1 para. 2 of Regulation (EC) No 24/2009.

FURTHER CONSIDERATIONS

Marketing in Luxembourg?

- Reverse solicitation scenario? Marketing questionable where Issuer and the AIF are part of the same structure, established and controlled by the same initiator (the issuer does not have the possibility to decline the subscription).
- Prior to AIFMD passport extension for non-EU AIF/AIFM: Under AIFMD minimum requirements to professional investors only (*cf.* Art 42 AIFMD) (thereafter: Member State of Reference / passport).

Offering of AIF linked Notes in Germany as (indirect) marketing?

- Conflict between the transparency regarding the description of the underlying AIF and a (possibly inadmissible) marketing of such AIF in Germany.
- The German legislator made a decision in favour of transparency and confirmed that the description of an underlying fund in a securities prospectus does not constitute marketing of such AIF. Explicit exemption from the definition of marketing in the KAGB.

Investor's expectations?

- Treatment under Solvency II.
- Treatment under Investment Ordinance (*Anlageverordnung*).
- Tax considerations.



QUESTIONS?

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Gregor Evenkamp advises domestic and international banks, insurance companies and financial services institutions in capital markets, banking supervisory and investment laws. He frequently advises on the structuring of collective investment schemes, structured products and alternative investments.

His practice has a particular focus on German investment laws and the implementation of the AIFMD in Germany (fund management, fund administration, fund regulation, outsourcing, Solvency II, MiFID II).

Gregor Evenkamp is an active member of the Association of Non-Tradeable Closed-End Funds (Bundesverband Sachwerte und Investmentvermögen e.V. – bsi).

Relevant experience :

- Structuring and documentation of open and closed-end collective investment schemes, in particular real estate, infrastructure and private equity as well as debt funds)
- Advising on the impact of the German implementation of the AIFMD on collective investments (transitional provisions, investment guidelines, investor qualification, outsourcing etc.)
- Advising on notification procedures as well as other ongoing regulatory advice
- Advising numerous German institutional clients (in numerous single and club deals) investing in structured notes issued by Luxembourg securitisation companies and repackaging the performance of (domestic, European and US) infrastructure, private equity or debt funds.)
- Advising numerous sponsors / initiators on the set-up and structuring of several issuance platforms for repack transactions.

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