

Marketing AIF in Germany

The new German Capital Investment Act (*Kapitalanlagegesetzbuch*, KAGB) that will come into force on 22 July 2013 provides for the implementation of the Alternative Investment Fund Managers Directive (**AIFM-Directive**) and a number of modifications to the regime of marketing and distribution of units in funds in Germany.

On 16 May 2013, the German Federal Parliament (*Bundestag*) adopted the AIFM Implementation Act (*AIFM-Umsetzungsgesetz*) that provides for the replacement of the German Investment Act (*Investmentgesetz*) by the German Capital Investment Act (*Kapitalanlagegesetzbuch*, **KAGB**). The vote was based on a draft recommended by the Financial Committee of the German Parliament (*Finanzausschuss des Deutschen Bundestages*) on 15 May 2013. On 7 June 2013, the AIFM Implementation Act will be on the agenda of the Second Parliamentary Chamber, the Federal Council (*Bundesrat*). If the Federal Council raises any objections, the AIFM Implementation Act will become subject to a mediation procedure conducted by the Mediation Committee (*Vermittlungsausschuss*), a joint committee of Federal Parliament and Federal Council.

Even if the AIFM Implementation Act becomes subject to a mediation procedure, significant material amendments are unlikely. Accordingly, we expect the current draft to most likely be the final draft.

If the AIFM Implementation Act passes the Federal Council, the Act will soon be signed into law by the Federal President (*Bundespräsident*) and published in the Federal Gazette (*Bundesgesetzblatt*). It is planned that the AIFM Implementation Act and, accordingly, the German Capital Investment Act will come into force on 22 July 2013.

I. Marketing

Pursuant to the definition in section 293 para 1 sentence 1 of the KAGB, "distribution" is any kind of targeting of investors, i.e., direct and indirect offering and placement of units in investment funds, similar to what is understood as a public offer under the current regime. The deletion of the section "as well as advertising" is not supposed to change this broad view, as this is also covered by the current wording. Even though there will be some simplifications in respect of distribution to professional clients and semi-professional clients, private placement as it has been known in the past will no longer be possible.

According to the KAGB, semi-professional clients are clients who meet, inter alia, the following criteria: They are qualified and experienced investors, they have committed themselves to invest at least EUR 200,000 and have signed a special declaration acknowledging their awareness of the risks involved in the investment.

In addition to this general definition of the term "semi-professional client", the KAGB explicitly determines that the following two categories of investors qualify as semi-professional clients:

- each private investor who commits himself to invest at least EUR 10 million;
- board members and other employees of an AIFM who have responsibility for the risk profile of an AIFM and/or an AIF (risk takers) and who personally invest in an AIF affected by this risk profile.

II. Duties for AIFMs

In order to distribute units in AIFs, an AIFM has to comply with, e.g., the following requirements:

- investment rules (*Anlagebedingungen*) of each AIF to be distributed have to be approved by the German Federal Financial Services Supervisory Authority (*Bundesanstalt für Finanzdienstleistungsaufsicht*, **BaFin**) before pre-marketing or distribution is possible;
- a sales prospectus as well as a Key Investors Information Document (**KIID**) will be mandatory for each AIF;
- application for a licence to distribute units in the AIFs is necessary; within such application process, the sales prospectus will be subject to BaFin's approval; and
- duties regarding ongoing investors' information have to be complied with.

In particular when targeting retail clients the AIFM has to comply with the following information duties:

1. When/before subscribing for units in the AIF

- sales prospectus, investment rules and KIID;
- most recent annual and semi-annual reports of the AIF;
- information on the most current Net Asset Value NAV or market value of the units;
- information on any limitation of liability of the depository, and
- Articles of Associations, Trustee Agreement (if any).

2. Ongoing information duties

- percentage of assets hard to liquidate;
- amendments to the AIF's rules regarding liquidity management;
- current risk profile and risk management system;
- details regarding leverage;
- amendments to the liability of the depository.

All information has to be provided in a durable medium or on the homepage of the AIFM and, if requested by the investor, on paper. Current investors' information has to be disclosed on the homepage of the AIFM.

Limiting distribution to professional clients and to semi-professional clients only reduces the information requirements with regard to the prospectus. In such case providing the "Information pursuant to section 307 of the KAGB" will be sufficient. However, the "Information pursuant to section 307 of the KAGB" is very similar to the information the AIFM has to disclose to private clients (retail investors in the terminology of the KAGB) in a prospectus.

III. German system of the EU Passport regarding the distribution of units in AIF (Outgoing)

1. German AIFM/EU AIF

A German AIFM that intends to distribute units in a German AIF or in an EU AIF *vis-à-vis* professional clients has to file a corresponding application with BaFin. The application itself is not subject to formal requirements. However, the following information and documents have to be disclosed to BaFin:

- a business plan regarding the AIF in question (incl. information on the registered office of such AIF);
- the investment rules (*Anlagebedingungen*), articles of association of the AIF;
- the name of the depository of the AIF;
- description of the AIF as well as all information available for investors regarding the AIF;

- registered office of the Master-AIF and its management company in case the AIF is a Feeder-AIF;
- the information as requested pursuant to section 307 of the KAGB (prospectus for professional clients);
- description of the measures that have been taken in order to avoid distribution to retail clients.

Approval for a Feeder-AIF is only possible if the Master-AIF also qualifies as a German or EU AIF managed by a German AIFM or an EU AIFM.

2. German AIFM/Non-EU AIF

Passporting the right to distribute units in non-EU AIF towards professional clients will also be possible in case the following requirements are met:

- an existing Memorandum of Understanding regarding an efficient exchange of information between BaFin and the home state regulator of the non-EU AIF is in force;
- the home state of the non-EU AIF is not on the FATF blacklist of Non-Cooperative Countries or Territories;
- several requirements regarding information exchange for tax purposes are met;
- the management company of the non-EU AIF complies with all requirements the AIFMD sets out regarding the management of such AIF in a comparable manner;
- the same information and documents have to be disclosed to BaFin as regards EU AIF.

It is worth noting that at the current stage only distribution *vis-à-vis* professional clients is subject to passporting. Distribution to semi-professional and private clients is subject to local provisions of the target member state.

IV. German system of the EU-Passport regarding the distribution of units in AIF (Incoming)

1. EU AIF

The KAGB provides for different approval procedures when targeting German investors:

- distribution of units in EU-AIF to German semi-professional and professional clients by an EU-AIFM is subject to the AIFMD passport system;
- section 329 of the KAGB provides for a special approval process in case an EU AIFM wants to distribute units in EU Feeder-AIF, whose Master-AIF is not based in the EU or EEA or not managed by a

German or an EU AIFM to semi-professional and professional clients.

If certain requirements are met it is also possible to distribute units in non-EU AIF to German retail clients.

2. Non-EU AIF

If a German or an EU AIFM intends to distribute units in non-EU AIF to German investors the same approval process applies as the one for distributing EU AIFs. However, additional documents and information have to be disclosed to BaFin, in particular, but not limited to the following:

- a certificate stating that the home state of the non-EU AIF is cooperating with BaFin;
- declaration of the AIFM to file its annual reports with BaFin and disclose any material changes on the documents and information provided during the approval process and further information regarding its business to BaFin upon request.

Section 330 of the KAGB provides for a special approval process in case a non-EU management company intends to distribute units in a non-EU AIF to semi-professional and professional clients. The approval process is similar to the one for distributing units in EU AIF, however, additional documents and information have to be disclosed to BaFin, in particular, but not limited to the following:

- an existing Memorandum of Understanding regarding an efficient exchange of information between BaFin and the home state regulator of the non-EU AIF is in force;
- the home state of the non-EU AIF is not on the FATF blacklist of Non-Cooperative Countries or Territories;
- measures have been taken in order not to distribute to retail clients;
- appointment of a depository; and

- in case of also targeting semi-professional clients it has to be ensured that certain information and notification duties will be complied with.

If certain requirements are met it is also possible to distribute units in non-EU AIF to German retail clients. If this is intended a German representative as well as a depository have to be appointed. However, distribution to retail clients has to be based on a prospectus and is only permissible if the non-EU AIF as well as the non-EU AIFM have their registered office within the same state and both are subject to public regulation. This leads to the conclusion that it is not permissible to distribute units in a German special AIF by a non-EU management company.

V. Grandfathering rules

In general, an AIFM intending to distribute units in AIF has to comply with the provisions of the KAGB as of 21 July 2013. However, if such AIF has been set up (exists) before 21 July 2013 and some other criteria are met it may benefit from grandfathering rules. According to the KAGB a 'German' AIF is deemed to be existing if the first investor (whether the investor is a German investor or not is irrelevant) has entered into a (binding) commitment.

On a best efforts basis German AIFM have to comply with the provisions of the KAGB from 21 July 2013. In addition, a German AIFM has to apply for a licence under the KAGB by 21 July 2014 at the latest. This leads to the requirement of notifying each intention to distribute units in AIF with BaFin, as except for the reverse solicitation exemption, private placement will no longer be possible under the new regime. Until such application is filed with BaFin and until 21 July 2014 at the latest, they are allowed to distribute units in their AIFs in accordance with the old regime, e.g., on a private placement basis, if at the current stage, the requirements of the old regime are fulfilled.

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