The Alternative Investment Fund Managers Directive;

An assessment on the impact on domiciliation of alternative investment funds

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1. Table of acronyms and abbreviations

AIF	Alternative Investment Fund
AIFM	Alternative Investment Fund Manager
AIFMD	Alternative Investment Fund Managers Directive
AIG	American Investment Group
ALFI	Association of the Luxembourg Fund Industry
C.R.	Czech Republic
CIMA	Cayman Island Monetary Authority
Directive	Alternative Investment Fund Managers Directive
EC	European Commission
EEA	European Economic Area
EFAMA	European Fund and Asset Management Association
ESMA	European Securities and Markets Authority
ELTIF	Regulation on European Long-Term Investment Funds
EU	European Union[1]
EUR	Euro
EuVECA	Regulation on European Venture Capital Funds
EuSEF	Regulation on European Social Entrepreneurship Funds
EU AIFM	AIFMs with a registered office in an EEA state
FATCA	Foreign Account Tax Compliance Act
HNWi	High Net-Worth individuals
IORPD	Institutions for Occupational Retirement Provision Directive
JOBS Act	Act on Jumpstart Our Business Startups
LLC	Limited Liability Company
Member State	Any country that is a member of the European Union
MFL	Mutual Funds Law (2013 Revision)
MiFID	Markets in Financial Instruments Directive
Non-EU AIFM	AIFMs without a registered office in an EEA state
OECD	Organisation for Economic Co-operation and Development

[1] In the context this thesis, the EU includes the entire EEA (similar to the scope of the AIFMD 2011).

OEREF	Open-ended real estate fund
PD	Prospectus Directive
S&P	Standard and Poor’s
SEBI	Securities and Exchange Board of India
SEC	Securities and Exchange Commission of the United States
Solvency II	Directive on the taking-up and pursuit of the business of Insurance and Reinsurance (recast)
SPE	Special Purpose Entity
TD	Takeover Directive
UCITS	Undertaking for Collective Investment in Transferable Securities
UCITSD	European Directive on Undertakings for Collective Investment in Transferable Securities
U.S.	United States of America
USD	U.S. Dollar
U.K.	United Kingdom

"Be the change you wish to see in the world"

Mahatma Gandhi

2. Acknowledgements

Dear reader,

Well, in front of you lies the master piece that ought to be the crowning glory on my days as a student at Tilburg University. While it has been a highly educational period of six years, I am very eager to implement the accumulated knowledge and capacities on both Dutch- and international business law in daily practices. In the process of composing this research, I have had the honour and pleasure of many enlightening and enthusiastic conversations regarding the subject, with among others lecturers Dirk Zetzsche and Sebastiaan Hooghiemstra and several lawyers of Clifford Chance, that have contributed to the content of this research.

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It seems that the only thing left for me to say, is that I hope that you, the reader, will enjoy reading this research and that it provides you some food for thought.

Margot Besseling

June 13, 2014

3. Introduction

It is the year of 2007, globalization is at a truly unprecedented performance and by suppressing signals of factors that could contribute to a financial crisis, a positive atmosphere among financial markets is widely prevalent.[2] In the aftermath of the global Great Depression around 1929, many Western countries, but foremost the U.S., imposed strict regulations on stock markets and restricted the elbow-room of financial institutions as banks through legislation. As from that moment, banks were no longer free to make high risk investments that could threat the stability of the financial system and the savings of common investors. The flexible and inventive market however has shifted the supply of credit and capital towards investment banks and alternative investment funds, e.g. hedge funds, that were operating on international markets with practically no regulation or at least avoidable regulation. The lack of oversight that aroused due to globalization implied that international currency speculators were unable to operate with an oversight of the market. Funds became heavily overleveraged [3] and risk was severely diversified through the use of "derivatives", which made it impossible for investors to determine the subjacent value of their assets.[4] In 2007 this market-made unregulated financial industry bubble encountered inevitable problems that eventually resulted in the collapse of entire financial systems, taking large institutions such as Lehman Brothers in the U.S. with it. Due to the cross-border use of credit and foremost leverage, the crisis quickly scattered across the rest of the world. Once the crisis got global, governments across the world had to step in and take measures to save the financial world and the real estate industry, e.g. by insuring savings and through injecting large amounts of money. [5]

After the apocalypse of the credit market's ill-performing regulators jumped in, in order to find their most suitable approach to the crisis through intensive regulation. In Europe, the EC published in April 2009 a proposal for future regulation of alternative investment funds such as hedge funds and private equity funds, in the form of the AIFMD.[6] The substratum is dual, on the one hand the EC strives for increasing investor protection and reducing systemic risk through stringent regulation, but on the other hand the EC aims at making the establishment of (alternative) investments in the EU more appealing in order to achieve the strategy of 'Europe 2020', which is fully devoted to increasing growth and innovation in the EU. [7] It seems to be an eternal struggle to achieve the delicate balance between over- and under-regulating and so it is on this matter.

Ten months after the AIFMD came into force, there is no denying that the Directive stirred up contradictory reactions, both of disappointment and satisfaction. Prior to the implementation, critics as well as defenders of the AIFMD made predictions about the presumed effect of the Directive on the

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[2] Spence & Leipziger 2010, p. 3.
[3] For example through Ponzi schemes.
[4] Creamer 2009.
[5] Available at: [http://www.rijksoverheid.nl/onderwerpen/kredietcrisis].
[6] European Commission 30 April 2009.
[7] Available at: [http://ec.europa.eu/europe2020/index_en.htm].

industry. Especially with respect to the anticipated alterations in the domiciliation of the funds, opinions differed widely. While defenders were convinced that the created safe environment, in combination with a level playing field across the EU, would be irresistible to portfolio managers, critics attached more value to the high compliance costs and the complicated structure of the Directive. In a survey set out by Deloitte among U.K. based asset managers from across the hedge fund, private equity and real estate sectors in May and June 2012, 61% of the respondents estimated that the AIFMD will affect their choice of fund domicile, and the majority of these managers were looking to continue establishing their funds outside the EU or move their funds offshore[8]. [9] Despite their experience with AIFs, EU regulation or any other financial professionalism, all the scientists, regulators and market participants could only speculate about the impact of the AIFMD on the industry.

This research is performed only ten months after the implementation of the Directive in national laws. Although not all AIFs are by this time obliged to comply with the AIFMD due to an extensive transactional period, this research is based on the first signs of alterations that are already visible on the financial markets. This research provides the reader with an assessment of the current financial markets in order to be able to answer the following research question:

What are the impact of the implementation of the Alternative Investment Fund Managers Directive on the domiciliation of alternative investment funds in Europe?

First, the process that led to the implementation of the AIFMD as well as the Directive itself will be discussed. This provides the reader with more insight on the conditions that were prevalent on the financial markets prior to the implementation of the Directive and the extent to which the AIFMD imposes new regulations on the industry. Consequently, chapter 5 will address the alternative investment funds, their specific characteristics and the broad variety of different types of funds. Following, the behaviour of domiciliation of AIFs will be discussed, particularly their motives to establish a fund in a specific jurisdiction and the incentives for re-domiciliation. In chapter 0, based on data on fund domiciliation, I will perform an assessment on the first visible signs of the impact of the AIFMD on the domiciliation of funds. Are there any significant alterations visible? Furthermore, I will make some predictions on the development of the AIF market in the EU in the upcoming years.

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[8] In the context of this research; offshore countries must be interpreted as jurisdictions that are low on regulation and tax, e.g. Jersey, Guernsey, the Cayman Islands and the British Virgin Islands. Onshore countries are meant as being the U.S. and EU Member States such as the Netherlands, the U.K, Germany and France and the U.S. The categorization of some locations is questionable however, because they contain elements of both, such as Ireland, Luxembourg and the U.S. state of Delaware. Funds in these jurisdictions typically do not base their choice of domiciliation on the existence of a large domestic market, but on a large variety of reasons, e.g. regulatory framework, distribution channels or infrastructure. In respect to this research, we consider these places to be onshore. Besides, regarding the perspective of this research, we mainly focus on the U.S. and EU market, rather than including the Asian and South American markets as well. (ALFI 2011, p. 1.)

[9] Opp & Hartwell 2012, p. 4.

4. The Alternative Investment Fund Managers Directive

4.1. The financial crisis in Europe

The financial crisis that emerged in the U.S in 2007 and quickly spread to Europe and the rest of the world, is, only seven years after its emergence, already considered to be economic history and has led to an astonishing amount of discussions and descriptions in books, articles and legislation across the world. Within these dissections, a comparison of the 2007 crisis (the Great Recession) with earlier equal financial-stress driven periods of recession, such as the Great Depression of 1929, is easily made.[10] Even though this comparison can be justified on many levels, certain developments prior to the 2007 crisis are attributable to the specific nature of the financial world of the recent decades and the size and global reach of the Great Recession is extraordinary. However, preliminary to the Great Recession as well as to other periods of recession, there had been an identifiable period of rapid credit growth, strong use of leverage, low risk premiums, mounting assets prices, copious availability of liquidity and a development of bubbles in the real estate sector. These developments were enhanced due to a high level of financial deregulation and a concentration of power of banks as a result of a large amount of mergers in the late 1990s, which amplified moral hazard and incentives for risk taking among financial institutions. The extent of the scope of the Great Recession across the world became inevitable due to the interwoven financial systems and the use of foreign leverage. The general discussed opinion is that a combination of these factors provided such a toxic mixture, that a financial crisis eventually became inevitable. [11]

However, the crisis would not have reached that unprecedented size across the world, if not one of the most important factors on which the entire financial system is based, had been destroyed: 'trust'[12].[13] Because of the over-stretched leveraged positions of financial institutions, even the smallest alterations in trust in parts of the asset markets were able to make the entire structure collapse. [14] When, prior to 2007, market conditions for the exchange of financial institutions' short-term debt became harder and the institutions faced an acute liquidity problem, the awareness grew that the economies needed alterations in order to be able to change the staggering position of financial institutions. Institutions were taking increasingly more measures to stabilize their position on asset markets, e.g. the Federal Home Loan Mortgage Corporation: Freddie Mac that announced early 2007 that it ceased to buy the most risky subprime mortgages and mortgage-related securities. [15] Although the system began to show high levels of unstableness, the financial system still showed opportunistic behaviour that originated from the earlier

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[10] Aizenman & Pasricha 2012, p. 347-372.
[11] European University Institute 2010, p. 2-6.
[12] In the context of this research, trust is interpreted as "the belief that an opponent in a relationship behaves accordingly to what he promises and does not take advantage of the person he is trading with. In other words: trust is A's probability that B will not "cheat"." (European University Institute 2010, p. 7.)
[13] European University Institute 2010, p. 2-6.
[14] EaFA & EC 2009, p. 1-3.

[15] Available at: [http://timeline.stlouisfed.org/index.cfm?p=timeline; http://freddiemac.mwnewsroom.com/].

decades of economic prosperity; the high levels of trust remained present and very few were suspecting that a systematic collapse was about to happen. In the summer of 2008, like opening a shaken bottle of sparkling soda, the bomb inevitably bursts. This destroyed not only the high profits of institutions but foremost liquidated the entire system of trust. At first, the trust that intermediaries had in each other was diminished, e.g. the Madoff fraud, and quickly thereafter, the trust of investors in the financial industry was wiped out, e.g. the collapse of the Lehman Brothers. The overly-opportunistic behaviour of many financial institutions was brought to the attention of the greater public, to which the collapse of the Lehman Brothers and the Bernard Madoff fraud became emblematic. [16]

4.1.1.Lehman Brothers

In September 2008, the U.S. financial markets met with disaster when Lehman Brothers, a major investment bank in the U.S., collapsed. Less than two weeks prior to the collapse, the U.S. government had saved two major mortgage corporations: Freddie Mae and Fanny Mac with a financial injection of USD 200 billion, but the problems around the ever so reliable Lehman Brothers however, were of such a scale and aroused so unexpectedly that the U.S. government was not able to rescue the investment bank to any further extent. The sheer size of the fall of Lehman ushered the collapse of the U.S. financial system. On even the next day, other large financial institutions, e.g. the largest American insurance company AIG, were in trouble and had to be saved. Stock prices dropped heavily and the lack of trust between banks rose to a new height, or better described as an all-time low. The U.S. government tried to save whatever could be saved and announced in October that it had reserved USD 700 billion for the sole purpose of providing support to the financial market. Due to the large amount of investments of EU corporations in U.S. institutions, it did not take that long for the crisis to hit Europe after the fall of the U.S. financial markets. Only three weeks after the collapse of Lehman Brothers, two major Dutch banks, Fortis and ABN Amro, had to be nationalised by the Dutch government for over EUR 30 billion.[17]

Despite the struggling of Lehman Brothers, three weeks prior to the collapse due to a debt of over USD 600 billion, the fall of the investment bank came as a brusque development for the majority of the involved parties. The level of disbelief among stockholders can be traced back to the high level of trust that still predominated the financial markets. In the case of Lehman Brothers, this trust was strengthened by S&P that still gave Lehman's securities an A rating only a few months prior to the fall. [18] The system of trust in the U.S. was (and in a way still is) being enforced through rating agencies, which categorize investments based primarily on the amount of risk that they imply to investors. The A rating kept the trust-bubble around Lehman unimpaired, providing the suggestion that Lehman's securities were remarkably safe, which stimulated investors to continue investing. [19] Once it became clear that the

[16] European University Institute 2010, p. 7-10.
[17] Algemene Rekenkamer 2012, p. 5.
[18] Available at: [http://www.standardandpoors.com/ratings/articles/en/us/?assetID=1245210943266].
[19] European University Institute 2010, p. 7.

estimated safe investment in Lehman turned out to be, in fact, a bad investment, the majority of the investors felt "cheated" and their trust in financial markets dropped heavily.

4.1.2. Bernard Madoff

When, due to the financial crisis, many financial institutions made a clean breast of their malfunctioning, many cases of financial fraud which originated from opportunistic behaviour were revealed. The disclosure of these cases, in which intermediaries of investment institutions turned out to be acting far from in the investors best interest, reduced the level of trust in the market to an all-time low across the world. Due to the carte blanche that most financial advisors had, based on the lack of regulation on the market, the advisors were able to misuse their position of trust. They advised many investors across the world to hold actually poorly diversified portfolios, which eventually led to intense losses for the investors when the financial system collapsed. [20] A luminary example of such a fraud that shook the entire financial industry was the fraud of Bernard Madoff.

Madoff Securities ran the world's most extensive Ponzi scheme [21], which eventually resulted in heavy losses in economies across the globe. When Madoff started his hedge fund in the sixties, with a capital of only USD 5000, he could not possibly have foreseen the fund's growth to an astonishing USD 50 billion in 2008. The tragedy of the Madoff fraud is that the SEC had already received several warnings about a possible fraud scheme in the period from 1992 to 2008. [22] The most widely known notice is the memorandum to the SEC of financial analyst Harry Markopolis, in which he provided robust evidence that Bernard Madoff was running a Ponzi scheme. [23] In 2007, two years after the initial reception of the memo, the SEC decided that: "the staff found no evidence of fraud" [24], but ultimately, in December 2008, Madoff confessed and was arrested after all. [25] Next to the impact of the sheer financial losses, the discovery of the Madoff fraud had a major elaboration on the level of trust on the financial markets, especially on the amount of trust of investors in intermediaries such as Madoff. For decades, Madoff had been a respectable broker; he was even the former Chairman of the NASDAQ Stock Exchange. The fact that he, of all people, had been running a Ponzi scheme for almost 20 years, came as a shock to experts as well as to non-professional investors. After the disclosure of the fraud, the trust of stockholders in intermediaries dropped heavily. If respectable hedge funds as Madoff Securities

[20] European University Institute 2010, p. 7-8.
[21] A Ponzi scheme is an investment fraud that includes the payment of alleged returns to existing investors from funds subsidized by new investors. Ponzi scheme organizers often acquire new investors by promising to invest funds in opportunities that are supposed to create high returns with little or no risk. In many Ponzi schemes, the impostors focus on attracting new capital to make promised payments to earlier-stage investors to generate the false appearance that investors are benefiting from a legitimate business. [http://www.sec.gov/answers/ponzi.htm].
[22] Rhee 2009, p. 365.
[23] SEC 2005, p. 1-5.
[24] SEC 2006, p. 1; SEC 2007, p. 1.
[25] Rhee 2009, p. 366.

appeared to be involved in this kind of business, the whole financial market could be expected to play comparable games.[26]

Not only the U.S. financial market took a direct hit from the fraud, also the EU markets were impacted. Heavy losses occurred in Luxembourg, Switzerland, the U.K. and France, as is also presented in Appendix A. [27] This was, among other things, the incentive for the EC to launch public consultations on strengthening and harmonizing legislation on UCITS and increase the supervision on UCITS depositaries as well as ensuring a level playing field in terms of UCITS investor protection across all Member States. [28] The widely dispersed approaches to the occurred financial losses, in combination with the bruised levels of trust among the EU financial market players, were incentives to Christine Lagarde [29] to express her discontent towards the large variety of approaches to depositary liability and investor protection, among the Member States.[30] Lagarde suggested the introduction of a more comprehensive system to address these issues, for example under the pending Securities Law Directive, and some depositary liability provisions in the UCITSD. The letter from Christine Lagarde had a major influence on the newly introduced depositary liability provisions. [31]

4.2. *Process leading to the AIFMD*

The intention to draw a regulation on AIFs found its challenge in having to regulate the relatively unknown. In 2006, the EC already attached value to restricting the unregulated playing-field of AIFs, but after 2008, due to the sheer size of the crisis, a large variety of parties with divergent interests was starting to interfere with the EC and intense discussions on both national and supranational level aroused. Within these discussions, two major camps with opposite extremes were identifiable. The preferences of the previous unregulated private equity and hedge funds for light touch regulations with pro-market policies were contradictory to the preferences of politicians with a particular outrage against the financial markets, for rigorous regulatory oversight. [32] According to Dirk Zetzsche [33], this remarkable disgruntlement of politicians against AIFs is based on two major developments over the past few years. After the fall of many financial institutions, politicians and regulators were made a scapegoat for the market's failure. Politicians and regulators were trying to oppose these (silent) imputations, by showing strength and competence to their constituencies in their act against the negligent behaviour of funds. [34]

[26] European University Institute 2010, p. 7-8.
[27] Schwartz 2008, p. 1-2.
[28] CESR 2009, p. 1-4; European Commission 2010, p. 2-7.
[29] Christine Lagarde was, at that moment, the Finance Minister of France and as of 2011 also the Managing Director of the International Monetary Fund (IMF).
[30] Zetzsche 2012, p. 4; Lagarde 2009.
[31] Zetzsche 2012, p. 4; Lagarde 2009.
[32] Zetzsche 2012, p. 2-3.
[33] Prof. Dr. Dirk A. Zetzsche holds the Propter Homines Chair for Banking and Securities Law at the University of Liechtenstein and is also a Director of the Center of Business and Corporate Law at Heinrich Heine University Dusseldorf and is considered to be a specialist on the AIFMD.
[34] Zetzsche DK 2009, p. 147-159; Zetzsche 2012, p. 2-3; Zetzsche NZfG 2009, p. 692-693.

Secondly, stakeholders wanted to pursue a concept that is particularly common in criminal law: 'repercussions'. The investment industry is being accused of threatening the corporate and political establishment in the EU, through its involvement in the acquisition of 'national crown jewels' and by showing misconduct through the misuse of corporate directors, to support their investment decisions. [35]

In 1985, the majority of European investment funds became subject to legislation when the UCITSD was introduced. The implementation of the UCITSD had, however, no significant impact on the collective investment markets, because the popularity of the use of UCITS in the EU remained prevalent. In June 2013, a month before the implementation of the AIFMD, UCITS funds managed EUR 6,559 billion of the total EUR 9,197 billion of all European money held in funds, a stake of roughly 71.3 percent. [36] Over the years, the UCITSD has been adjusted, but the basic characteristics remained unchanged. UCTIS are open-ended entities that aim to raise capital among the public and collectively invest this obtained capital in a variety of financial instruments, for which it is possible to obtain a EU passport. With the UCTISD, the EC distinguished the regulated UCITS funds from the somewhat 'forgotten' unregulated other types of investment funds. In order to lawfully market in the EU, these 'other funds' had to depend on a vague mixture of various European regulations such as the MiFID [37] and the PD [38], in combination with a wide variety of national laws.[39]

In 2005, the EC has published a paper on the Enhancement of the EU Framework for Investment Funds, which entailed statements of experts who believed that disorganizations in the market for non-UCITS funds would have a severe impact on European growth.[40] Considering the special focus on growth and innovation in the EU, the EC subsequently set up three working groups with each a different perspective on the investment industry. Each of the working groups performed an analysis on the most desired approach concerning AIF regulation in the EU; one researched the preferences of hedge funds, the other of private equity and the third of OEREFs.[41] The scope of the recommendations of the working groups differed widely, but the common denominator was that something had to change. The high-level working group on financial supervision in the EU, which was chaired by Jacques de Larosière, confirmed some of these findings and paid additional attention to the possibility of systemic risk. The high-level working group recommended: *"that appropriate regulation must be extended, in a proportionate manner, to all corporations or entities conducting financial activities which may have a systemic impact (i.e. in the form of counterparty, maturity, interest rate risks…) even if they have no*

[35] Zetzsche 2010, p. 2; Zetzsche 2012, p. 2-3.
[36] EFAMA 2013, p. 1.
[37] Many asset managers were licensed under the MiFID, in order to execute portfolio management and/or investment advice.
[38] Funds had to be compliant with the PD for the sale of fund units that are qualified as securities.
[39] Zetzsche 2012, p. 1.
[40] European Commission 2005, p. 1-8.
[41] European Commission 2006, p. 4-5.

direct relations with the public at large." [42] In their recommendation, the high-level working group attached great value to the role of the managers of the funds, rather than the investment funds themselves. By doing so, the group aimed at reducing the risk of moral hazard that exists if there is a conflict of interests between the powerful decision-making directors and the general risk-averse investors, and the phenomenon of shadow banking [43] in the EU. [44]

Taking all the considerations of the working groups into account, the EC chose to design a new regulation on AIFMs, rather than broadening the scope of the already established UCITSD. On 30 April 2009, a first proposal of the AIFMD was issued by the EC. [45] After a period of intense debating on the intensity and the scope of the proposed Directive, the AIFMD was officially published on 21 July 2011. [46]

4.3. Objectives

The drafting period of the AIFMD is being characterised by competing political intentions. These, widely divergent and sometimes unclear, political intentions prevented the objective to be clearly outlined and subsequently have led to delays during the drafting and approval of the Directive. [47] The lack of an unambiguous objective after all the compromises that have been made, is visible in the AIFMD: "*This Directive aims to provide for an internal market for AIFMs and a harmonized and stringent regulatory and supervisory framework for the activities within the Union of all AIFMs, including those which have their registered office in a Member State and those which have their registered office in a third country.*"[48] In his book on the AIFMD, Dirk Zetzsche addresses four major political views on AIFs that predominated the drafting process.

The first and foremost obvious objective can be directly deviated from the feeling of shock that prevailed among politicians and regulators after the financial crisis. In their opinion, investment funds were left a considerable amount of freedom that had to be restrained through risk management. The proposed measures of risk management entails two competing interpretations with various scopes, on the one hand the perspective of systematic risk and on the other hand the perspective of investor protection. Prior to the crisis, and subsequently to the implementation of the AIFMD, financial experts and stakeholders in the investment industry were convinced that the market itself, with its ability to freely adjust to changing circumstances, was in fact the preferred party to absorb the systematic risk. The well-

[42] European Commission February 2009, p. 23.
[43] Shadow banks is one of the definitions that aroused during the financial crisis. Shadow banks are nonbank financial institutions that raise short-term funds in the financial markets and use these funds to buy assets with long-term maturities. Because they are not subject to (strict) bank regulation they are not able to borrow in emergencies from central banks and do not have familiar depositors whose funds are covered by insurance.
[44] Kalinowski 2012, p. 3.
[45] European Commission 30 April 2009.
[46] Zetzsche 2012, p 6; AIFMD 2011.
[47] Sender& Amenc 2011, p. 7-11.
[48] AIFMD 2011.

experienced institutional investors were considered to be able to sufficiently protect themselves without any regulatory assistance. Due to the disclosure of cases such as the previously discussed fall of the Lehman Brothers and the Madoff fraud, the system of trust in self-made risk management schemes is abandoned. In order to enhance the control on risk management, the EC included several provisions in the AIFMD. An example is the registration period, as set out in Article 3a up to 8 of the AIFMD, which is considered to be a severe measure of risk management that aims at recognizing systematic risks. Next to the improvement of the control of systematic risk, the EC adds value to investor protection through provisions on disclosure and transparency.[49]

The second objective of the AIFMD that has led to intense public debates concerns the creation of a single EU market providing AIFMs the ability to freely market across the financial markets of all Member States, once strict requirements are fulfilled. If AIFMs are able to obtain such a carte blanche, they are able to provide cross-border management to funds that are domiciled in other Member States or market AIF units to institutional investors in the entire EEA. In the end, the ability to obtain such a passport is included in the AIFMD, but several aspects, such as the 'third country rule', still rely on evaluations of the EC.

Subsequently, discussions on the level of protection of the intensely regulated, AIFMD-obedient European fund industry against the probably lighter regulated competitors from third countries aroused. Some parties consider these protectionist measures against third countries essential for the EU investment market, since the introduction of a European passport can introduce an increase of competition. Whether the AIFMD is in fact that attractive to AIFs across the world is disputed, as a high degree of harmonization and regulation can discourage or reduce financial innovation. Given the EU's particular interest in enhancing financial innovation and growth in the EEA, it is crucial for the EC to find the delicate balance between harmonization and freedom in the AIFMD.

And lastly, the EC debated about the possibility of increasing coherence in the exchange of tax information. Such a system reveals the fiscal benefits of Member States and subsequently increases the pressure on offshore domiciled funds.

In many areas the AIFMD highly resembles the already established UCITSD; some provisions are even directly copy-pasted into the new Directive. The UCITSD has a clear objective, allowing collective investment schemes to operate freely throughout the EU, after having complied with several governance and information requirements. After the realisation of several compromises, the AIFMD chose for a similar objective: (i) bring a previous light regulated AIF market in a legislative framework, in order to decrease the gap with UCITS; (ii) realize harmonization through creating a single EU market and

[49] Bhagat & Romano 2009, p. 1-5.

common guidelines on supervision and authorization for AIFMs; (iii) increase the protection of- and transparency towards investors and other stakeholders; (iv) provide the proper governance resources to supervisors, to enable them to control systemic risks and increase responsibility and accountability of AIFMs.

4.4. Contents

4.4.1. Law subjects

For the extent of the AIFMD, the EC made a profound decision to regulate the AIFMs over regulating the investment funds themselves. In practice, it is the fund manager that is responsible for key decisions on the management of the fund, e.g. on the investment strategy. [50] These key decisions, that particularly entail decisions on financial stability, investor risk and the amount of risk that the fund will face, originate first and foremost from the conduct and organisation of the AIFM in combination with the providers of main services, such as the depositary and valuation agents. [51] In order to meet the objectives of the AIFMD and to reduce the principal-agent problems in the investment industry, the most 'effective' approach is to regulate the highest entities in the 'decision-making chain'. By submerging the information-rich and decision-making AIFMs to stricter regulation, the managers will be less able to exploit their powerful position for self-enrichment and investor-abusive practices. Considering this introduction of solid regulation for the managers, in combination with the current absence of direct AIF legislation, the benefits of including AIF registration would likely be overshadowed by the added burden on AIFs and the regulators. Besides, the implementation of an AIF registration system could be an initiator of moral hazard amongst the investors. The investors may think that the regulators exercise better direct control over the AIF than actually will happen. This might lead to investors moving past the essential due diligence and exposing themselves to greater investment risks. [52]

With the publishing of the proposal of the AIFMD in 2009, a large part of the investment market was surprised by the extent of the scope of the Directive. Based on the relative large amount of private equity and hedge funds in the alternative investment industry, a vast stake of speculators and participants of public discussions expected these types of funds to become subjected to the AIFMD. However, in 2009 it became clear that the EC chose for a more one-size-fits-all approach in their explanation of an AIF, as an investment fund that does not qualify as an UCITS.[53] The EC stated that they found it both 'ineffective' and 'short-sighted' to limit any legislative initiative for the alternative investment industry to only hedge funds and private equity. It would be ineffective for the industry, since any arbitrary

[50] Sustmann, Neuhaus & Wieland 2012, p. 78-90.
[51] European Commission 30 April 2009.
[52] European Commission 30 April 2009.
[53] However, the EC strongly counters the opinion that a one-size-fits-all approach has been implemented. The EC is of the opinion that the AIFMD provides enough tailored provisions for different types of AIFMs in order for irrelevant and inappropriate requirements to not be imposed on investment policies for which they make no sense. (European Commission 30 April 2009.)

definition of these types of funds might not sufficiently capture all the relevant actors, and could therefore easily be avoided. The perspective would be short-sighted since many of the fundamental risks also exist in other kinds of AIFM activity. The EC concluded that, therefore, the most enduring and productive solution would be to capture all AIFM activities that give rise to these kind of controversial risks. [54]

4.4.1.1. *Alternative Investment Fund Manager*

Under the Directive, an AIFM is considered to be a person, either legal or natural, whose regular business activity entails the administration of one or more AIFs. [55]

4.4.2. *Territorial scope*

Prior to the approval of the Directive there has been much disagreement about the scope of the Directive. Should it be accessible to non-EU AIFMs as well? Should we make the European market some kind of fortress or should we enhance competition by letting non-EU managers enter the European market? As we have seen on other matters, the Directive is being characterised by compromises. And a similar fate did not befall the choice for a territorial scope. The result of the compromises that have been made is presented in the timeline of the implementation of the AIFMD in Appendix B.

Pursuant to Article 2, the Directive applies to both EU AIFMs and non-EU AIFMs and thus the territorial scope is not bound by merely the EEA. Non-EU AIFMs will have to comply with the AIFMD: (i) when they manage either one or more EU AIFs; or (ii) when they market one or more AIFs in the EU, irrespective of whether such AIFs are EU AIFs or non-EU AIFs. [56] However, in order to (partly) satisfy the conservative camp that wanted to close the EU investment industry from non-EU immigrants, the EC chose for a graduate approach to the territorial scope. As of 22 July 2013, after the transposition of the AIFMD into domestic law, EU AIFMs who market EU AIFs are able to obtain a EU passport. [57] Two years after that implementation, the ESMA shall critically evaluate the functioning of the EU passport for EU-AIFs and their EU managers and will advise on the implementation of the passport to third country entities. [58] In the context of the AIFMD and subsequently of this research, a third country can be interpreted as ‘any country that will fall outside the scope of the EEA’, e.g. the U.S. and any other country of the discussed offshore centres of domiciliation. In order to be able to comply with the AIFMD, a depositary must not be established in a third country that is listed as a Non-Cooperative Country and Territory by the FATF. [59]

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[54] European Commission 30 April 2009.
[55] Article 3 under 1 under c AIFMD 2011.
[56] Article 2 AIFMD 2011.
[57] Next to setting up a single rule book, the EC wanted to set up a single authorization scheme, this scheme is called a EU passport.
[58] Article 67 under 1 AIFMD 2011; Zetzsche 2012, p. 19.
[59] Article 21 under 6 under c AIFMD 2011.

In anticipation to the evaluation of the ESMA, which is scheduled on 22 October 2018, the Directive allows Member States to continue pursuing a national placement regime, providing each country in the EEA the opportunity to have its own authorization scheme for third country entities. Based on the evaluation of the ESMA, the EC will decide on the termination of the private placement regimes. [60]

4.4.2.1. A desired cross-border approach?

Although the large amount of concessions that had to be made in the period prior to the AIFMD may have been inevitable, due to the large amount of parties involved, and given their considerable disagreements on the scope of the proposal, the AIFMD might turn out to be overly-compromised. Due to decisions on allowing national regimes to maintain their private placement regime, and the choice for a slow implementation of the Directive that is subjected to a lot of advice from the ESMA, it seems like a one-size-fits-all model has turned into one-size-fits-none regulation. Although they provide the flexibility to adjust to any forthcoming (unexpected) post-crisis situations, the vague clauses of the Directive also add complexity and most importantly, they lack certainty. Some of the heavily debated clauses actually only raise more questions, instead of providing answers. Which is remarkable given the objective of the Directive, on creating more certainty and practical guidelines for the alternative investment industry in the EU.

An example of such an overly-complicated matter, is the position that has been given to the ESMA. The ESMA has been (and still is) heavily involved with the drawing, implementation and after-care of the AIFMD, but has only been given an advisory role instead of a power of making decisive decisions. This can be blamed to the lack of trust that has predominated the financial markets and the national regimes after the crisis. No party is willing to relinquish their rights to make final decisions, even if that relinquishment turns out to be in the better interest of the transparency of the Directive.

Another illustration is the level of submissiveness of the Directive to the advice of the ESMA and further decisions of the EC towards, for example, the implementation of a third country regime. The fact that still no decisive decisions have been made on whether the entire regime will, at some time, come into force, introduces a lot of uncertainty to non-EU managers. In their decision to make no decision at all, the EC sends a discouraging signal to non-EU AIFMs, restraining them from being incentivised to prepare for compliance, or to even consider heading their business to the EU at all. Given the particular importance that the EU is attaching to any deficits or crumbly grows of the EU investment markets in comparison to e.g. the U.S. market, it is paradoxically to create barriers in the form of a cloud of uncertainty and complexity around the AIFMD, as a result of which investment funds will be discouraged to choose for the EU. On the other hand, the additional high compliance costs and the strict requirements of the AIFMD, can outweigh the advantages of obtaining a EU passport and can result in

[60] Article 68 under 6 AIFMD 2011; Zetzsche 2012, p. 19.

scaring offshore funds away, where they would otherwise keep their business in the EU. In this respect, restricting the scope to EU-AIFMs can turn out to be the preferred option. Whether post-crisis investors that prefer an AIF operating on a costly and supervised, but -in theory- more secured regulated investment market could tip the balance away from investors that prefer an AIF operating with more liberty and possible higher returns on a, -in theory- riskier market, will be subjected to the evolvements of the upcoming years.

Regarding a tax aspect of the AIFMD, it is predicted that investors will most likely favour a less regulated investment market over the EU. The Directive is one of many examples of absence of harmony on how to deal with taxation issues in the EU. The AIFMD requires non-EU AIFMs to comply with the standard, as set out in Article 26 of the OECD Model Tax Convention on Income and Capital, but does not oblige Member States to comply with these OECD standards regarding national authorization. [61] The advantage of choosing for a secured regulated jurisdiction can diminish if there are still too many uncertainties considering important factors such as taxes. [62] The question that remains, however, is how much weight investors, and subsequently AIFMs, attach to these tax aspects, for them to be of any influence on their choice of domiciliation.

4.4.3.Exemptions

At first, limiting the scope of the AIFMD might appear to be the opposite of the intention of the EC to establish a somewhat one-size-fits-all Directive that suits the entire alternative investment industry in the EU. However, in order to make the very broad Directive effective for a large variety of AIFs, with different intentions, sizes and financial structures, the EC included several exemptions to exclude some AIFs from unnecessary onerous measures.

The scope of the AIFMD is limited to entities managing AIFs in the execution of their regular business and which raise, in that capacity, capital from a number of investors with the intention to invest that raised capital for the benefit of those investors, in harmony with a defined investment policy. These entities are subjected to the Directive, regardless of whether the AIF is either an open-ended or closed-ended fund [63], whether the fund is listed or not and apart from any legal form of the AIF. [64]

This limitation on the scope of the AIFMD does not change the fact that still a vast amount of different funds are subjected to the Directive. In order to increase the efficiency of the regulation and to respond to the aspirations of the smaller and/or specialised AIFs, the EC included several exemptions in Article

[61] Article 35, 37 and 40 AIFMD 2011.
[62] De Manuel Aramendia 2010, p. 3.
[63] The EC distinct open-ended funds from closed-ended funds in de AIFMD, although the Directive provides no definition to these terms. The ESMA defines open-ended funds as funds that are characterised through their not-fixed capitalization, they can issue more shares if investors want to increase their investment in the fund. Open-ended funds (that can be listed on a stock exchange) typically sell their own new units to investors and are prepared to buy back their old units. [http://www.esma.europa.eu/content/Open-ended-funds].
[64] Recitals 6, AIFMD 2011.

2 AIFMD. Article 2 states that the Directive shall not apply to: "(i) holding companies; (ii) institutions for occupational retirement provisions, which are covered in the IORP Directive [65]; (iii) supranational institutions, in the event that such institutions or organisations manage AIFs and in so far as those AIFs act in the public interest; (iv) national central banks; (v) national, regional and local governments and bodies or other institutions which manage funds supporting social security and pension systems; (vi) employee participation schemes or employee savings schemes and (vii) securitisation SPEs."[66]

4.4.3.1. Threshold Exemption

AIFMs that initially are subjected to the scope of the Directive can be still exempted from compliance, provided that they meet the threshold of Article 3 AIFMD, called the 'de-minimis-rule'. The de-minimis-rule applies to all AIFMs that either directly or indirectly manage portfolios of AIFs, whose assets under management, including any assets acquired through the use of leverage, in total do not exceed the threshold of EUR 100 million. Subsequently, the rule applies to all AIFMs that either directly or indirectly manage portfolios of AIFs, whose assets under management in total do not exceed a threshold of EUR 500 million, on the condition that these portfolios involve unleveraged AIFs and have no redemption rights exercisable during a period of five years following the initial investment in each AIF. [67] Article 3 AIFMD consequently subjects AIFMs that manage portfolios, whose assets under management exceed EUR 500 million and all portfolios that are open-ended and/or leveraged, whose assets under management exceed EUR 100 million, to stringent regulation and the opportunity to obtain a EU Passport.

AIFMs that invoke the de-minimis-rule are subjected to registration at the competent authorities of their home Member State. These AIFMs can, however, still opt-in for the Directive, but in that case they will have to fully comply with all the requirements of the Directive and cannot cherry-pick those requirements that are in their favour. In the period prior to 22 July 2015, the de-minimis-rule can turn out to be another highly emotive subject on which the Member States must decide, especially if the scope of the AIFMD will be extended to third countries. Should the de-minimis-rule, in that case, also become available for non-EU AIFMs? If the Member States decide to preserve the de-minimis-rule only for the use of EU managers, the EC will have to substantiate that decision with profound arguments, in order to justify that kind of discrimination. On the other hand, if the EC allows these 'small' managers to be exempted from the scope of the AIFMD, these managers will only be subject to the regulatory

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[65] IORPD 2003.
[66] Article 2 AIFMD 2011.
[67] The EC distinct open-ended funds from closed-ended funds in de AIFMD, although the Directive provides no definition to these terms. According to the ESMA, contrary to open-ended funds, the shares in closed-ended funds are not readily transferable on the market, especially if the funds may not be listed on a stock exchange. However, the capitalisation of these funds is the same as for open-ended funds and the shares that are issued are bought and sold similarly. The major difference is in the increasing of the capital.
[http://www.esma.europa.eu/content/Closed-ended-funds]

oversight of their jurisdiction of domiciliation. Given the large amount of smaller investment funds in the EU and the existent large amount of funds having assets under management of up to EUR 500 or 100 million, the potential risk of a lack of- or an impropriate ‘offshore’ regulatory oversight, can be exactly that risk that the EC wants to avoid with the implementation of the AIFMD. Given the importance of these ‘small’ funds for the growth of innovation in the EU, e.g. the role of these funds in the development of high-tech spin-offs, the EC has to attach great value to attracting these smaller non-EU funds to the EU investment market. In this perspective it is hard to say if either one of these scenarios, i.e. being AIFMD compliant or unregulated, is the desired path for smaller non-EU AIFMs. A possible solution for these smaller managers is to set up a special regime for non-EU venture capital, in order to avoid strict regulatory burdens that potentially can kill any initiatives in the EU. Such out-of-the-Directive solutions correspond with the aim of the EU to reach more smart, sustainable and inclusive growth in 2020. [68]

4.5. Effects of the Directive

4.5.1. Compliance costs

In order for AIFMs to be compliant with the Directive, certain requirements must be met. The downside of having to meet these requirements is the significant increase in compliance costs that particularly, reporting requirements, depositaries and the use of an administrator impose on AIFMs. These costs can put a substantial burden on the funds both in the initial stage of authorization, as well as in any continuous stages of the fund’s lifetime. The requirement of having to appoint a single depository for each fund which is managed by the AIFM, is actually borrowed from the UCITSD. [69] The appointment of a depository, who is primarily concerned with the safekeeping of the assets of the AIF, is one of the included measures to protect investors against losses that ascend from fraud of the AIFM. [70] Another cost-inducing measure is the obligation for AIFMs to establish suitable and consistent procedures for the valuation of the assets under management, of each AIF. [71] The sheer size of the costs that compliance with the AIFMD imposes on the investment industry in the EU does put the benefits of a more stringent regulatory framework in the shade. Although the passport opportunities of the AIFMD can, for some funds, slightly reduce capital-gain tax burdens on investors.

4.5.2. Safer environment for investments

Despite the vast amount of critique on the content of the AIFMD, the implementation of the Directive does go with several advantages, which the EC aimed to create for the investment industry in the EU. The EC intended to create a safe(r) single EU market for AIFs and their investors. In order to achieve

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[68] De Manuel Aramendia 2010, p. 4.
[69] Article 18 UCITSD 2009.
[70] Payne 2011, p. 18.
[71] Article 16 AIMFD 2011.

this, the AIFMD provides the industry with two major tools, to reduce systemic risk and to increase transparency.

The AIFMD consists of various provisions that explicitly are designed to reduce systemic risk. In the context of this research, systemic risk can be defined as: '*a risk of disruption to financial services that (i) is caused by an impairment of all or parts of the financial system and (ii) has the potential to have serious negative consequences for the real economy*'. [72] The EC attempted to facilitate the detection, valuation and monitoring of systemic risks in the AIFMD, with provision on, for example, disclosure requirements on the use of leverage [73], some internal risk management requirements [74], the appointment of independent depositories [75], and internal or external valuers [76]. [77]

In addition to reducing systemic risk, the EC also aimed at attaining more transparency on the investment markets through, for example, disclosure obligations. [78] AIFMD-compliant fund managers have to comply with certain provisions concerning disclosure obligations, e.g. the disclosure of information to investors prior to their investment [79], ongoing disclosure through annual reports (to regulators) [80], and periodic statements to investors and acknowledged authorities [81]. The requirement of an additional disclosure to regulators is a cost-inducing novelty on the financial markets. However, the EC justifies the introduction of this new requirement, on the basis that it provides regulators the opportunity to perform supervision on potentially abusive practices, throughout the system. [82] Despite the nobility of the objective of the EC, the actual efficacy of the ramifications is questionable. An example is the requirement to disclose in case of any acquisition of control of a non-listed company, of Article 28(4) AIFMD: "*the AIF, or the AIFM acting on behalf of the AIF, discloses its intentions with regard to future business of the non-listed company and likely repercussions on employment, including any material change in the conditions of employment (...)*".[83] For any accurate reader with a particular interest in EU financial directives, the wording of this article might look familiar. The phrase of Article 28(4) AIFMD is actually borrowed from Article 6 of the Takeover Directive. [84] If lessons can be learned from the actual impact of Article 6 on the takeover market, it is plausible to conclude that a similar interpretation

[72] Zetzsche 2012, p. 21.
[73] Article 7, (3)(a) & Article 23(1)(a) & Article 24 AIFMD 2011.
[74] Article 9, 13 & 15 AIFMD 2011.
[75] Article 21 AIFMD 2011.
[76] Article 19 AIFMD 2011.
[77] Zetzsche 2012, p. 33-34.
[78] Payne 2011, p. 18-20.
[79] Article 20 AIFMD 2011.
[80] Article 19 AIFMD 2011.
[81] Article 20 & 21 AIFMD 2011.
[82] Payne 2011, p. 20-22.
[83] Article 28(4) AIFMD 2011.
[84] Takeover Directive 2004.

of the wording will lead to required disclosures that consist of fair, but in fact too general, information that will not materially improve the position of stakeholders in a portfolio company. [85]

Article 28(4) AIFMD is an illustration of the struggles the regulators had to face in the process of drawing legislation for a previous self-regulating market. Given the tremendous broad scope of the Directive, it was highly predictable that the regulators would duplicate already existing provisions in other financial directives, and that they would make minor inevitable flaws throughout the process. The EC deliberately chose to keep the wording of the AIFMD relatively vague and to include several widely-interpretable guidelines, in order to facilitate the market to create the standard. In the upcoming years, many of these shortcomings or uncertainties are expected to be revealed and corrected, when the regulators have obtained important practical experience. Despite these teething problems, the estimations are that the AIFMD will have a major impact on the investment industry. In a case where a market relies this heavily on trust and reputation, the vast amount of rumours about a future implementation of stringent regulation and subsequently the creation of a safer regulated investment market, may already have had more impact on the industry, than the actual implementation of the Directive will have.

4.5.3.Alternatives to AIFs

With the introduction of specialised regulations such as the AIFMD and the UCITSD, there is a trend towards the use of an extensive range of financial instruments. When the UCITS III Directive [86] was implemented in 2001, fund managers were given a new variety of tools, which were previously only available in the alternative asset market, to be used in the conduct of their investment business. When the investor's demands altered, after many jurisdictions provided more stringent regulation on investment funds in the aftermath of the financial crisis, new players that tried to avoid being subjected to regulations such as the AIFMD entered the UCITS market. New tools were introduced to meet with the demands of the investors that particularly asked for an increase in returns based on reducing the returns on deposit accounts, and at the same time required an increase in capital security. It is nearly impossible to meet with both of these demands because in practice they turned out to be each other's opposite. Through the interchangeable use of fund regulation, funds can meet the specialised demands of their investors.

An example of such 'new' players on the investment markets, are hedge funds that rather comply with the UCITD. In vernacular speech, these funds are called 'newcits'[87]; funds that make use of typical

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[85] Payne 2011, p. 23.
[86] UCITSD 2001.
[87] According to EFAMA, this label of newcits is a product of the media, and the industry as well as regulators should avoid the use of this term because it would be pointless to create a special label or regulation for these funds. and in the end they all are UCITS. (EFAMA 2011).

hedge fund strategies but are packed in the wrapper of an UCITS. [88] Prior to the AIFMD, newcits made use of the strong investor protection provisions and the reputational value of the UCITS, to comfort their investors. With the implementation of the AIFMD, provisions on investment protection and any relating costs became somewhat similar to those of the UCITSD. In the assessment of whether or not newcits will remain popular once the AIFMD has come into force, the outcome is mostly dependent on how the EC will put the passport-regime into place. However, due to the expected evaporation of the current cloud of uncertainty around the AIFMD, once the market has created standards on compliance, the AIFMD will increasingly provide a feasible framework for hedge funds in the EU. Therefore it is plausible that the phenomenon of newcits will lose their practical advantages. [89]

5. Alternative Investment Funds

Prior to 22 July 2013, collective investments that marketed across the EU had to comply with the detailed UCITSD, or were otherwise at the mercy of national regimes. After the fall of many large financial institutions in the crisis and the eruption of the generated outrage against investment funds, many experts and market players expected the AIFMD to be drawn for only private equity and hedge funds. When not only private equity and hedge funds, but any AIF appeared to be subjected to the Directive, many of these speculators were heavily surprised.

The AIFMD differentiates two types of collective investment funds: (i) UCITS, and (ii) all funds that do not qualify as such. Apart from the exemptions as discussed in 4.4.3, it is a fund that falls under the second category that generally qualifies as an AIF. Therefore, as of July 2013, there are two different types of funds: (i) open-ended UCITS and (ii) all-inclusive AIFs, either open-ended as well as closed-ended, whether the investment strategy relies on the use of leverage or not, and with either shares or units that are listed as well as unlisted on regulated capital markets.[90] This impressive broad scope is an illustration of the EC's aim to keep up with the flexibility of the industry and the entities' indefatigable ability to find loopholes in regulations. In order to provide the industry with the most efficient regulation on alternative investments, the EC subjected the influential conducting businesses of AIFMs to the Directive and made no attempt to regulate the AIFs themselves. Therefore, the EC stays away from making any difference between types of AIFs that are commonly known in vernacular speech. The categorization of AIFs that will be used in respect to this research is therefore not a legal technical distinction, but is included to provide an insight in the alternative investment market that is subjected to the AIFMD. Regarding the perspective of this research, as there is no coherent general view, the distinction in types of AIFs is based on a study of Dirk Zetzsche on the AIFMD. [91]

[88] Lyons 2012, p. 3.
[89] Lyons 2012, p. 50-53; Sender 2011, p. 10.
[90] Zetzsche 2012, p. 10.
[91] Zetzsche 2012, p. 10-14.

5.1. Hedge Funds

Although the expression 'hedge fund' was already used in the 1950s, to describe any investment fund that made use of incentive fees, short-selling systems and leverage, the definition of the term hedge fund is still not a globally accepted technical term which definition is legally enshrined in regulation.[92] Many organizations as well as persons, and even laws [93], have tried to provide an explanation for the term hedge fund that can serve as a one-size-fits all definition. [94] The definition of the U.S. President's Working Group of 1999 is regularly used in, as well the industry, as in literature and comes down to: '*any pooled investment vehicle that is privately organised, administered by professional money managers, and not widely available to the public*'. [95] The U.K.'s Financial Services Authority created their own definition, based on some characteristics of hedge funds: *'(i) funds that are organised as private investment partnerships or offshore investment corporations; (ii) funds that use a wide variety of trading strategies involving position-taking in a range of markets; (iii) funds that employ an assortment of trading techniques and instruments, often including short-selling, derivatives and leverage; (iv) funds that pay performance fees to their managers; and (v) funds that have an investor base comprising wealthy individuals and institutions and a relatively high minimum investment limit (set at US$100,000 or higher for most funds)*'. [96] Considering the broad scope of the AIFMD, the definition of hedge fund in respect to this research is the extensive explanation of Dirk Zetzsche: '*hedge funds are investment policies that employ a higher-than-average level of leverage and derivatives for adjusting, and often increasing, exposure*'. [97] Given the divers interpretations of the definition of hedge funds, it is challenging to provide an exact number on the amount of hedge funds across the world, but the number is estimated to be around 10,000 in December 2013. [98] Based on the data of the same sources, there was an observable growth of the hedge fund industry in the past years. The global hedge fund capital raised to a new record of USD 2.70 trillion in the first quarter of 2014. [99]

Not only the definitions of hedge funds differ widely, there is also a large variety in opinions on hedge funds. Defenders of these funds attach great importance to the financial injection that hedge funds provide to developing organizations, and to the influence of these organizations on innovation and growth in the EU. Prior to the financial crisis, hedge funds mostly dodged the strict-regulation-bullet. When the EC expressed their intention to draw a directive for the alternative investment market, defenders of hedge funds were emphasizing to maintain their freedom through deregulation. The working group of experts, which performed an evaluation on hedge funds in 2005, had a similar vision

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[92] FSA 2002, p. 8.
[93] S. 112 et seq. Investmentgesetz 2004.
[94] Vaughan 2003, p. 1.
[95] PWG 1999, p. 1-4.
[96] FSA 2002, p. 8.
[97] Zetzsche 2012, p. 11.
[98] Siegman, Stefanova & Zamojski 2013, p. 2.
[99] HFR 2014.

as these defenders and recommended a pan-European private placement regime without extra manager regulation, such as the one in the PD. [100] In literature, authors supporting the concept of hedge funds are widely prevalent, for example T. Bullman, who wrote: *'[…] the association of high risk or financial instability with hedge funds is a misperception, as hedge funds employ strategies that are often market neutral, meaning the fund has been constructed in a way that it will benefit, in either form, a rising or a falling market. Also hedge funds bring liquidity to markets in recessionary periods and therefore represent a stabilizing mechanism*.' [101] Critics, however, have stated that hedge funds can be in fact hazardous to the stability of financial markets, because they might, as Pearson and Pearson state: *'create financial shock and disrupt the stable functioning of the financial markets, more than other financial products, because they involve greater leverage and risks*'. [102] This is one of the main reasons that, across the world, hedge funds are increasingly more subjected to regulation. Not only in the EU, under the AIFMD, but for example also in the U.S. under the JOBS Act in 2013.

5.2. Private Equity

The nature of private equity firms and hedge funds is actually quite similar. Both fund types make use of roughly the same manager compensation schemes (the 2/20 rule) [103] and a wide variety of investment strategies. Whilst some private equity firms merely concentrate on (leveraged) buy-outs of listed companies, and others rather on obtaining non-controlling stakes and syndicated structures, the common denominator is the creation of value using non-listed (private) firms.[104] Compared to hedge funds, private equity funds are relatively illiquid. Hedge funds, in most cases, favour to invest in public securities, and therefore typically have more liquid assets in which they, already in the first stages of the lifetime circle of the fund, will immediately invest (nearly) their entire capital. Private equity companies, however, generally invest in more mature companies [105] and therefore typically postpone the investment of their capital, in order to be able to perform a proper due diligence on their investment targets. Because they do not immediately appeal to the entire investment portfolio, investors usually commit to a certain amount of money that is not instantaneously deposited in the fund. [106] When the private equity firm finds an interesting investment, the manager will make a 'capital call' to their investors in order to receive the requested amount of the bound committed capital.

[100] European Commission IMSDG 2006, p. 4-9.
[101] Bullman 2008, p. 14.
[102] Pearson & Pearson 2007, p. 32; Zetzsche 2012, p. 11.
[103] Phalippou 2007, p. 12.
[104] Zetzsche 2012, p. 11-12.
[105] The private equity firm will buy these mature companies in order to turn them around, or inject a lot of money in capital-needing-companies in order for them to grow very fast.
[106] The fund managers will receive their management fee based on the committed money.

5.2.1. Venture capital

Venture capital is in fact a form of private equity, however, when most people talk about private equity, they do not immediately allude venture capital. Evidentially, being a form of private equity, venture capital funds typically only invest their capital once due diligence on the portfolio company is performed. Though contrary to private equity firms, venture capital funds typically invest in early-stage, innovative portfolio companies. [107] Because venture capital funds are in an early-stage involved with portfolio companies, they do not only fulfil the role of money-supplier, but in most cases also provide management assistance and advice to the entrepreneur. Due to the, in most cases, smaller size of venture capital funds, the amount of assets that is managed by most AIFMs is not sufficient to become subject to the AIFMD. [108] To meet the requests of these special cases, the EC came up with the EuVECA, to support the small managers with adequate regulation, and to provide them the opportunity to obtain a EU passport.[109]

5.3. Real Estate

Given the broad scope of the definition of an AIF, and the variety of structures and vehicles that are present in the different national real estate markets, real estate funds may also have to comply with the Directive. Real estate funds typically invest in real estate or real estate holding companies, and they aim at providing investors with exposure to real estate markets, with a regional or international focus. [110] Although the definition of real estate funds is shared among the Member States, the types of real estate vehicles and the applicable regulatory framework differ widely. Where in the Netherlands the majority of the real estate funds are considered UCITS and were already subjected to a EU regulatory framework, Member States as France, Germany, Ireland and the U.K. have a large variety of real estate vehicles that do not all qualify as UCITS.[111] For real estate funds it is essential that the AIFMD provides enough clarification on definitions to enable the Directive to provide a broad platform, with a level playing field for all the different real estate vehicles.

Real estate funds are often considered to be ‘safe’ investments, this is partly due to the illiquid long-term nature of real estate. The funds will, however, not be that safe when: (i) debt is loaded on the fund; or when (ii) a macro-economy downswing makes it unable for tenants to pay their rent. Moreover, the illiquid investment products, in combination with an open-ended fund structure, can set real estate investment funds into a liquidity crisis. The liquidity crisis arises when redemptions of a major fraction of fund units stream back into the fund. [112]

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[107] Gompers & Lerner, p. 21; Zetzsche 2012, p. 12.
[108] Zetzsche 2012, p. 12.
[109] EuVECA 2013.
[110] Zetzsche 2012, p. 12.
[111] Veris & Goddet, p. 6-8.
[112] Zetzsche 2012, p. 12.

Regarding the limited size of this research, in the following chapters, profound attention will be given to the popular hedge funds, private equity and real estate funds. The specific interests of the AIFs, as discussed in 5.4 and 5.5, will be left out of this research.

5.4. *Special Funds*

Next to the familiar and popular hedge funds, private equity and real estate funds, there are a few more funds that are prevalent on the EU financial market and that may have to comply with the AIFMD.

5.4.1. *Special funds for professional investors*

The AIFMD enables institutional- as well as private investors to invest in AIFs. However, due to the specified nature of certain funds, there are special funds that are reserved for professional investors. Examples of these funds are pension funds, insurance companies and firms that aim at investing their excessive cash in suitable investments. Although some funds can be exempted from the Directive, e.g. pension funds according to Recitals 8 [113], professional investors may see the fund structure under the AIFMD as an appropriate way to approach the valuation problems of illiquid assets, and contemporaneously meet regulatory requirements that are compulsory by Solvency II and IORPD. [114]

5.4.2. *Funds tailored to the needs of High Net-Worth individuals*

HNWi funds are also known as billionaire funds and do frequently attract family offices. Although HNWis operate as private individuals, they can hardly be seen as non-professional investors. HNWis tend to aim at co-investments that are professionally managed, and make use of intelligent strategies or invest large stakes in illiquid assets. Due to the professional approach of these HNWis, they consider the heavy protection for retail investors, when investing in these types of assets, as exceedingly onerous. [115]

5.4.3. *Other types of investors*

Due to the decision of the EC to hold on to the use of national regimes next to the AIFMD in the first stages of the transactional period, some jurisdictions invoke a third group of 'other' investors. In order to attract other types of investors, some Member States extend the discrepancies from investor protection rules that are established under HNWi funds, to these 'third schemes'. The qualification requirements for these investors prevaricate from the requirements that are set out in the PD. An example of such a duplicated requirement, is an, in some Member States, applied scheme, where clients of authorised investment advisers and portfolio managers are reduced protected, based on the assumption that they depend on the investment intermediary for choosing the investment fund. [116]

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[113] AIFMD 2011.
[114] Zetzsche 2012, p. 12.
[115] Zetzsche 2012, p. 12 – 13.
[116] Zetzsche 2012, p. 13.

5.5. *Other*

Although the specification of AIFs as discussed in chapter 5, is extensive, the enumeration is yet not conclusive. The varieties in investment funds that are subject to the Directive are in fact unlimited, which contributes to the challenge of the EC to provide a one-size-fits-all regulation, and a level playing field that suits every type of fund. AIFs typically invest in art, intellectual property, commodities, ships, emerging markets, cash or any other liquid or illiquid assets. Each different market on which the AIF is active and each different jurisdiction of domiciliation defines the character of the fund and subsequently the need for regulation. The EC continuously tries to meet each specialised need of every type of AIF, e.g. through the implementation of the ELTIF, EuVECA and the EuSEF.

6. Domiciliation of funds

6.1. *Incentives of domiciliation*

Investment funds that are being marketed face both national and supranational competition. National funds are only sold to investors in the country of fund domiciliation and, contrary, supranational funds are sold beyond national borders. Due to the decrease in barriers in the cross-border sale of investment funds, the cross-border distribution of funds has amplified across the world over the past decades. As a result of this increased cross-border distribution, competition among fund managers has intensified and incentives on relocating their practices aroused, e.g. to domicile funds in countries that provide the most favourable regulatory regime. Subsequently, this has led to an increase in competition between countries seeking to attract fund managers into their financial market. [117] In their function as suppliers of a platform for funds, a distinction can be made between onshore and offshore jurisdictions. Generally speaking, onshore countries, such as the U.S. and Member States, provide a ‘safer’ environment for funds, due to higher governance and marketing requirements and stricter regulatory frameworks with taxable accounts. For example, in the U.S. The Investment Company Act of 1940 requires managers of hedge funds, who try to avoid registration and substantive regulation, by limiting both the number and type of fund investors, excluding them from making public offers of shares, and enabling them to only use private placements to solicit U.S. investors. Offshore countries, such as Jersey and the Cayman Islands, can be defined by means of providing low regulatory and tax requirements on funds. [118]

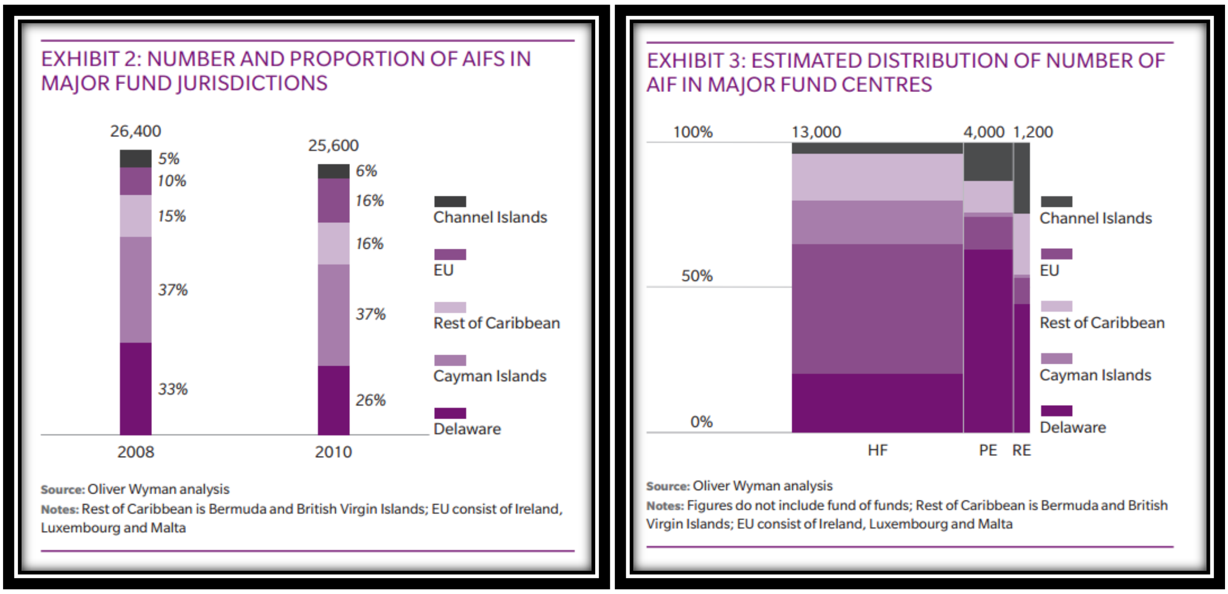
Up until a few years back, the choice of domicile was considerably influenced by tax and regulatory deliberations, and was therefore making a lot of AIFs choose for offshore domiciliation. However, after the collapse of the financial markets, and subsequently the drop in trust among- and towards investment funds, the onshore market regulators heavily increased the pressure on offshore funds. Whether it is justified or not, especially offshore centres took the bullet, and their existence was profoundly discussed.

[117] Lang & Köhler 2011, p. 6.
[118] Aragon, Liang & Park 2014, p. 74-91.

At the same time, onshore market regulators were eager to act upon the recent development through levelling the playing field, making onshore investment markets, in certain respects, more attractive than ever before.[119]

Commissioned by the ALFI, Oliver Wyman performed an analysis on the domiciliation of AIFs in different major fund jurisdictions in the EU and American area. Although this survey was executed in 2011, it provides a general insight in the post-crisis alterations in the industry between 2008 and 2010. Besides, at the time of this analysis, new post-crisis regulations, e.g. the Dodd-Frank Act, were already introduced and rumours about an upcoming implementation of the AIFMD and a revised UCITSD were prevalent among the industry. As is also presented in Appendix E, a remarkable finding based on this analysis was that the Cayman Islands, together with Delaware, topped the list as AIFs domiciles, with a domiciliation rate of over 60% of all AIFs. Compared to 2008, in 2010 The Cayman Islands had been able to maintain their market share of 37%, while Delaware, however, had lost around 21.22% of AIFs. It is also stringent to see that the EU, or better said, Luxembourg, Ireland and Malta, had gained a considerable market share in that same time period. This might be attributed to their increased attention to AIFs, and to their massive efforts to attract funds to their jurisdiction. The significant decrease of more than a fifth in Delaware can be accredited to the severe hit that U.S.' AIFs had had to take after the financial crisis. The fact that most of the funds in Delaware originate from U.S. AIFMs contributed to the substantial decrease of AIFs. As is also presented in exhibit 2 of Figure 1, the domiciliation of onshore funds actually dropped from 2008 to 2010. [120]

Figure 1: Number and proportion of AIFs in major fund jurisdictions



Source: ALFI 2011, p. 2.

[119] ALFI 2011, p. 2.
[120] ALFI 2011, p.2.

6.1.1.Regulatory

The familiar proverb: “the customer is king” that you often find, written on the wall, in shifty restaurants can also be considered rule number one in the “managing investment funds for dummies handbook”. In their business, an AIFM is dependent on investors providing capital for the funds. It is therefore of main importance for managers, as well as regulators, to gain or maintain high levels of trust and confidence on the market. After the collapse of the financial markets during the crisis, both the investors’ and the intermediaries’ confidence in the AIF market had diminished. Fund managers had to increase their efforts to gain the trust of investors through presenting that (i) the fund is integer; and (ii) the fund is cost efficient, which eventually shall result in high sustainable profits for the investors. Although the actual effect of a regulated market, rather than that of an unregulated market, on the integrity of funds may be questionable, AIFMs can send out a strong signal, and thereby appeal to the investors’ confidence if they explicitly choose for a regulated jurisdiction. In their choice of domiciliation, all AIFMs will eventually try to find a balance between gaining investors’ trust and being cost efficient. In this belief, it might be more conclusive to say that AIFMs are looking for more supervision instead of regulation. According to Dermot Butler [121] in 2009, only recent after the Madoff fraud: “*I am pleased to see that investors are taking the administration side of the industry more seriously, however I find it extraordinary that so many hedge fund investors are “jumping up and down” saying that they will not invest in hedge funds any more after the Madoff fraud, unless they are independently administrated. The Madoff scandal was a failure of due diligence and, given how the operation functioned, had nothing to do with a lack of independent administration. In the end, no regulation is going to stop a crook*.” [122] In line with the considerations of Butler, it is likely to conclude that the simple fact of being subjected to regulation does not guarantee that the fund will stay away from any fraudulent activities. However, having to obtain authorization and being closely supervised by financial institutions does initially provide a safer environment.

6.1.2.Tax

As investment funds are about money, investors aim at the interest of the fund and the managers are satisfied in their capitalistic needs through fees and agreed percentages of the interest. In order to generate the highest interest for their own- and the investors’ interest, the managers will keep the costs of the funds as low as possible. One major aspect that can significantly affect the funds’ costs and subsequently has a great influence on the choice of domiciliation is each jurisdictions’ tax regime.

[121] Mr. Dermot S.L. Butler is at the moment Chairman of Custom House Global Fund Services Ltd and has over 40 years of experience in the financial services industry and setting up different AIFMs in different jurisdictions, both off- and onshore. (QFCA 2009, p. 20-22.).
[122] QFCA 2009, p. 20-22.

The legal structure of a fund can have a substantial influence on the choice for a jurisdiction, c.q. a tax regime. AIFs try to avoid any subjection to a two-layered taxation scheme, in the event of investors who have typically invested in a fund that consecutively invests in portfolio companies. The investor has to pay taxes both on the sale of the interests in the portfolio companies by the fund, including the distribution of those profits to investors, as well as in the event of the sale by the investor of its interest in the fund company.[123] In many countries, however, the distribution of proceeds of sale of single investment throughout the lifetime of the fund will rather be considered as a 'dividend' than as a 'partial realisation of capital'. Therefore, any capital gains that go with the profitable sale of any investments will be converted into income. Although particular fund investors see this as an advantage, in the private equity industry it is considered to be a common standard. It is in the interest of the majority of the investors, to use a system that promotes them when they invest through the indirect use of a fund, rather than it would have, had they been investing in the investee companies themselves. Jurisdictions in which the common standard does not apply, and thus provide systems that enhance the position of fund investors investing directly in the investee company do occur, but these systems are usually not widely accepted. [124]

In order to increase tax efficiency, fund managers can choose between two structures. For example, managers can choose for a system that exempts the gains of the fund from tax burdens, whereupon the tax only impedes the distribution of profits to investors. These schemes regularly include the use of a corporation that is established in a tax haven or in any country that offers a discharge from tax on capital gains and sometimes income, e.g. the Dutch participation privilege. While this scheme can serve the funds, notice must be given to the highly non-transparent character, and to the high risks that are related to having to pay double taxes in case of e.g. a lack of a double tax treaty between the country of domiciliation of the AIF and that of the portfolio companies. Therefore, a second, more transparent tax-efficient structure might serve the majority of the funds better. This system involves legal structures such as a limited partnership, where, with the use of a distinction between general- and limited partners, on the sale of an investment by the AIF, investors are accounted liable for the tax obligation on their share of the profit, notwithstanding whether the sale was directed to them. This system will evade the double tax charge, while simultaneously, the capacity of the investors to use the advantage of any double tax treaty between its country of residence and the country of domiciliation of the portfolio corporation, is well-looked-after. Sometimes, however, a problem arises when the involved jurisdiction does not recognise the used structure. Even in the jurisdictions that are familiar with these transparent systems, a certain amount of care needs to be provided to guarantee that the fund does not constrain the investors

[123] Berwin 2006, p. 15-16 & 191.
[124] Berwin 2006, p. 15-16 & 207-208.

into another investment in an alternative jurisdiction, where the investor will be liable for greater tax burdens than in their home domicile. [125]

Many highly regulated onshore AIFs are structured in limited partnerships, and subsequently entail general partners and limited partners. In this example, the AIFM will function as the general partner, which, for liability purposes, can be organised in the form of a limited liability company. Given U.S. tax regulations, a limited partner structure can serve the fund, because in such a structure the taxable income can be “passed through” to fund investors, rather than taxed at both the investor and the entity levels.[126] This can, in fact, be less attractive to U.S. tax-exempted investors, since they will have to face unrelated business taxable income from leveraged investments. [127] Offshore funds, however, are normally organised under a legal structure that avoids this unrelated business taxable income, making these funds more interesting to tax-exempt investors, e.g. endowments and pension funds, as well as for non-US investors.[128] The table in Appendix D provides a percentage on the amount of legal structures of hedge funds in the U.S. compared to those in offshore countries. Although this table only provides an insight in the hedge fund market, and the comparison is restricted to offshore funds and U.S. domiciled funds, and therefore the exact ratios on private equity and real estate funds may differ, Appendix D does provide a partly general insight in the distribution of legal structures.

Regulatory provisions can provide a basis for a more governed AIF market, but the effects will not be as substantial when global taxes are left out of account and no deliberations on a global level playing field take place. Over the past few years, a variety of initiatives aroused across nations and supranational institutions, in which they expressed their intention to bring an end to tax havens. In March 2010, the U.S. has introduced the FATCA, with the aim to detect taxpayers that evade tax with offshore holdings. The FATCA, subjects certain accounts of foreign financial institutions to several reporting requirements. In February 2012, the U.K., Germany, France, Spain and Italy have expressed their support to the underlying goals of the FATCA and, together with the U.S., they have committed themselves to work on an intergovernmental approach to improve international tax compliance and implement the FATCA. [129] Furthermore, the U.S. attempts to gain even more awareness for tax havens, through the implementation of the “Stop Tax Haven Abuse Act”. [130] Next to the U.S., the U.K. has also increased its attention on preventing tax evasion, and made offshore tax evasion a criminal offence, through making any offences on undeclared foreign income subject to a prison sentence, irrespective of any good- or bad faith. [131] The U.K. is actually rather serious in their hunt for tax evasions, as George

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[125] Berwin 2006, p. 16.
[126] McCrary 2002, p. 43; Aragon, Liang & Park 2014, p. 74-91.
[127] LePree 2008, p. 807-853; Aragon, Liang & Park 2014, p. 74-91.
[128] Aragon, Liang & Park 2014, p. 74-91.
[129] GOV.UK 2012.
[130] Levin 2013.
[131] Fund Domiciles 15 April 2014.

Osborne [132] stated: "*It is totally unacceptable for people not to pay the tax that is due and the message will be clear now with this new criminal offence that if you're evading tax offshore, there is no safe haven and we will find you*". [133] However, while the U.K. attaches great public importance to punitive activities on offshore tax evasion, at the same time, the U.K. focusses on attracting corporations to their financial market by copying European tax haven systems, such as those of Ireland and the Netherlands.

Next to national jurisdictions, supranational bodies, such as the G20, increasingly express their intolerance against tax havens. With the introduction of a Financial Action Task Force black list and an OECD black and grey list, international oversight on evading taxes is increasing.

6.1.3. Other

The majority of the authors in fund literature consider deliberations on tax and legislative regimes of main importance in the choice of domiciliation of AIFMs. But in reality there are many other additional factors which can be of influence on that decision. In a debate on fund domiciliation in London in 2009, David Woodhouse[134] stated that: "*Investors do not really care where funds are domiciled; the choice of domiciliation only becomes important if something bad happens to the fund*" [135] As a hedge fund investor, Woodhouse attached great value to the insolvency regime of a jurisdiction, rather than tax and legislative regimes.

Another factor that can be influential on the decision on domiciliation of AIFMs is the previous familiarity of that manager with that particular jurisdiction. Being familiar with the market culture in a jurisdiction and/or having obtained a large pool of contacts in a country can be the decisive factor in the choice of domiciliation of an AIFM. Due to their substantial dependence on trust, investors attach great importance to good reputations. The familiarity of an AIFM with a specific jurisdiction or a specific service provider, in combination with a good reputation on that market, can send exactly the desired signal of trust to investors. For example, Guernsey, one of the Channel Islands, is well-known among private equity funds and has built, over the years, a web of well-respected service providers with many years of experience. The Cayman Islands have obtained a similar reputation in the offshore hedge fund industry.[136] A jurisdiction with a good reputation is generally a jurisdiction with good relations with international regulators as IOSCO and the OECD, and does not appear on any blacklist.

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[132] George Osborne is UK Chancellor of the Exchequer and Second Lord of the Treasure since 2010. (QFCA 2009, p. 20-22.)
[133] Financial Times 2014.
[134] David Woodhouse has, as being an investor in hedge fund himself and via his position as Chief Due Diligence Officer at Fauchier Partners LLP, a lot of experience on alternative investment markets. (QFCA 2009, p. 20-22.)
[135] QFCA 2009, p. 20-22.
[136] IFI 2012, p. 5-6.

A third factor that can influence the decision of the AIFM to domicile in a specific jurisdiction is the geographical location of that jurisdiction. Why choose for a domicile centre on the other side of the world in an unfamiliar country with different cultures, if there is one around the corner?

6.2. Alternative Investment Funds

Despite the similar basis that defines each type of AIF, the market behaviour of hedge funds, real estate funds and private equity can show major differences. Each of these funds differentiates themselves through their investment portfolio and their intended investment period, and these differences can have implications on the preference for a jurisdiction for fund domiciliation. Where, for several investors, the level of familiarity with a centre of domiciliation can be decisive, for other investors the level of regulatory measures or tax arrangements can be of main importance.

Hereafter, the reader is provided an assessment on major fund centres for respectively hedge funds, private equity funds and real estate funds. This assessment is for a large part based on an analysis that was performed in 2011 by Oliver Wyman, on the request of the ALFI. Due to the limited availability of public data on the domiciliation of AIFs across the world, the research in chapter 6.2 of this thesis is based on data that was collected before the actual implementation of the AIFMD. Although this survey does not provide an insight in the current distribution of AIFs in 2014, it does shed a light on the post-crisis alterations in the industry between 2008 and 2010. Besides, at the time of this analysis, new post-crisis regulations, e.g. the Dodd-Frank Act, were already introduced and rumours about an upcoming implementation of the AIFMD and a revised UCITSD were prevalent among the industry. As Marc Saluzzi [137] stated: "*Whilst it was widely believed within Europe that a consequence of the AIFMD and the related regulatory pressure exercised by the G20 countries, would be widespread re-domiciliation of funds into EU domiciles, and a fall in the number of offshore funds, this report demonstrates that the offshore landscape in the last two years has remained stable.*" Due to the relative minor alterations in the landscape of domiciliation of AIFs between 2008 and 2010, the analysis of Oliver Wyman will provide a general insight in the fund hot spots in early 2014.

6.2.1. Hedge Funds

As is also presented in Appendix F, the Cayman Islands are by far the most popular jurisdiction for hedge funds, holding 52% of all the assets under management. Both U.S. and U.K. established managers often choose for the strong infrastructure of the Cayman Islands, based on their reputation and familiarity with hedge fund managers and institutional investors. However, U.S. based managers do also often choose for Delaware, as it has a similar strong hedge fund infrastructure. Delaware has the reputation of being a business-friendly legal system and that, in combination with the fact that domiciliation in the U.S. provides institutional investors with a considerable degree of confidence, makes Delaware a

[137] Marc Saluzzi is chairman of the Association of the Luxembourg Fund Industry. (QFCA 2009, p. 20-22.)

popular destination. The British Virgin Islands and Bermuda are popular among both EU and U.S. based managers, due to their geographical location being close to the U.S. and their historic ties to the EU. EU hedge fund centres, such as Luxembourg, Ireland and the Channel Islands (e.g. Guernsey and Jersey), are primarily chosen by EU managers who often prefer EU domiciliation. In reality, less than 15% of the total assets under management are domiciled in the EU. Ireland is, however, the world's leading jurisdiction for the registration of UCITS and does, at the moment, attach great value to attracting AIFs to their investment market. [138] And next to that, as is provided in Appendix F, Ireland is the second preferred centre of hedge fund domiciliation.

6.2.2.Private Equity Funds

Contrary to hedge funds, Delaware is by far the most popular centre of domiciliation for private equity funds, as is provided in the graphs in Appendix G. Considering that private equity investors are generally more risk-averse than hedge funds, it makes sense that they prefer an onshore domiciliation over an offshore domiciliation. The vast U.S. private equity industry holds 72% of all private equity assets under management in Delaware, and around 90% of the non-U.S. private equity funds are domiciled in onshore jurisdictions. The majority of the EU based managers chooses for Jersey and Guernsey, due to their sophisticated private equity infrastructure and their geographical proximities to financial centres such as London. [139]

6.2.3.Real Estate Funds

The choice for domiciliation of real estate funds is somewhat comparable to that of private equity funds, due to their similar fund structure and fund life cycles. However, real estate funds often choose for a different fund distribution, since the choice for domiciliation for real estate funds can be more complicated, due to special tax deliberations that are relevant for real estate in some countries. For example, there is the fact that in order to comply with the UK REITS, a real estate fund needs to be tax resident in the U.K.. The Channel Islands were the frontrunners in attracting U.K. real estate funds because of these tax benefits. The majority of the advantages of these tax regimes were recently diminished, and therefore it is expected that their position as major real estate fund centre, will eventually slowly weaken. As is also provided in Appendix H, Delaware is the main centre of real estate domiciliation with 65% of all the real estate assets under management. Many EU real estate funds choose for Luxembourg as jurisdiction of domiciliation. Luxembourg offers an extensive range of structures that are appropriate for real estate investments, such as the SICAF, SICAV and FCP.[140]

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[138] ALFI 2011, p. 3; ALFI November 2011, p. 1-3.
[139] ALFI 2011, p. 4.
[140] ALFI 2011, p. 5; ALFI November 2011, p. 1-3.

6.3. Re-domiciliation

In the aftermath of the crisis on the financial markets, the prevalent opinion among experts is that the era of offshore domiciliation is on its retreat. To support this opinion, in the past decade, there were several trends visible on the investment markets. There has been an increase in managers who considered establishing a fund outside of the popular offshore centres of domiciliation, and in managers who gained interest in the opportunity of re-domiciling their already established funds to regulated jurisdictions. In response to the aspirations of these fund managers, several EU jurisdictions enabled fast track procedures to welcome the anticipated large number of refugee AIFs that are 'escaping' the offshore centres in e.g. the Cayman- and Channel Islands. [141]

Fund managers can achieve re-domiciliation through several ways: "(i) the transfer of a registered office of a fund to another country; (ii) fund A contributes its asset and liabilities to another entity which is domiciled in the favoured nation, in exchange for shares in that entity; and (iii) a cross border fund merger."[142] Regarding the first track, major EU fund domiciliation centres, such as Luxembourg, which had already established a legal basis on which funds are allowed to re-domicile many years ago, are post-crisis getting competition from other major fund centres, such as Ireland, which also start to adopt legislation to enable re-domiciliation to their jurisdiction. An example of a large fund that aimed at domiciliation in the EU is Amundi Alternative Investments. As of 2010, Amundi has started to re-domicile to France, Ireland and Luxembourg in order for the manager to be able to obtain an AIFMD licence, which was actually received on 12 December 2013. [143]

Although there is no public data supporting any major trend towards re-domiciliation, the fact that several jurisdictions provide its possibility and that fund managers are known to make use of it, results in the fact that re-domiciliation is a factor that needs to be taken into account when assessing shifts on the investment markets. Michael Wilson, a fund manager that is known to have re-domiciled several of his funds stated: "*there is a certain degree of "paralysis through analysis" over where to domicile. Some accounting firms, lawyers, consultant etcetera have made a career out of promoting one domicile over another but at the end of the day this is pretty simple. When deciding where to domicile, you need to look at who is the fund's end client, where they are located and what kind of product you plan to bring out. Once you have done that you have narrowed the choices considerably. On top of that you look for real regulation, good infrastructure and good service providers. But, "it is not rocket science". You can have all the regulation in the world but you have to be able to enforce it".*[144]

[141] IFI 2012, p. 14.
[142] Carne 2011, p. 4.
[143] Amundi 2013., p. 1-2.
[144] QFCA 2009, p. 20-22.

6.3.1. *Co-domiciliation*

Typically, together with an increase in fund legislation, there will be an increase in schemes on avoiding the burdensome strict regulations, and the AIFMD is no exception to this. An example of such a scheme is co-domiciliation. After the financial crisis, there has been an increase in co-domiciliation, where AIFs continue to function from offshore jurisdictions, but establish clone- or feeder funds in regulated onshore jurisdictions. [145] An example of such a scheme is a hedge fund manager who runs both a Cayman-domiciled offshore fund as well as a clone Luxembourg-domiciled onshore fund.

Co-domiciliation provides AIFMs an option to escape from the strict regulations of the Directive, while still serving their EU investors, but the scheme imposes, at the same time, some challenges on the managers. A major challenge is to maintain synergies in similar investment strategies between the onshore regulated fund, with more stringent requirements on leverage and reporting, and the offshore fund. If the manager is unable to create or maintain these synergies, the consequences might impact the performance of the AIF. Next to that, compliance with the regulatory requirements, such as reporting requirements, depositaries and the appointment of an administrator, can impose significant higher costs on the onshore fund in respect to the offshore fund. [146]

An analysis performed by RBC Dexia Investor Services in combination with KPMG in 2011 showed that of the 24% of their respondents that already had re-domiciled hedge funds to the EU, 55% has done this through setting up a clone fund in the EU to complement existing offshore funds (co-domiciliation). In a second survey among respondents who were considering re-domiciling their hedge funds to the EU in the (nearby) future, 69% of the respondents indicated that they would rather transfer their domicile to the EU. [147] The same report indicated that, despite the deliberations on co-domiciliation, actually a small number of managers planned to replace offshore fund domiciles, such as the Cayman Islands, for EU domiciliation. Co-domiciliation is expected to be a complementary alternative rather than a substitute for complete EU domiciliation. [148]

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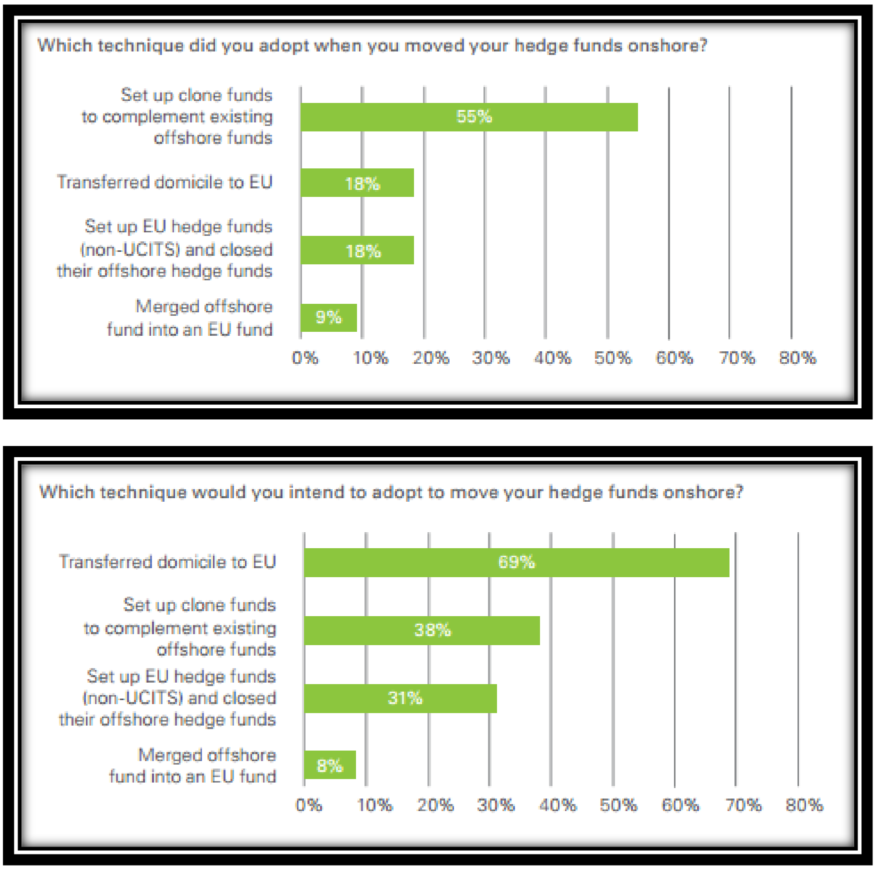
[145] ALFI 2011, p. 7-8.
[146] AAA 2012.
[147] KPMG 2011, p. 23-26.
[148] AAA 2012.

Figure 2: Used and intended techniques for re-domiciliation of hedge funds to onshore jurisdictions



Source: KPMG 2011, p. 23-26.

7. Impact of the AIFMD on domiciliation

As a result of regulatory harmonization on EU financial markets, competition between investment fund managers in the EU has risen greatly in the past decade. With the intention of profiting from economies of scale, fund managers have increasingly concentrated their practices to a single location. This has led to amplified competition between countries across the world that pursue to attract these fund managers. Within the EU, especially Luxembourg and Ireland are globally familiar as specialised financial centres. [149] Appendix C provides data on the large amount of mutual funds in Luxembourg and Ireland that is domiciled in foreign countries, in comparison to the amount of domestic companies. Over the past few years, the choice of domiciliation became increasingly more important to investment funds. Since the implementation of the UCITSD, compliant funds were able to obtain a passport, allowing any UCITS that is registered in at least one Member State to be marketed in another Member State, without additional lengthy authorization proceedings. The attention around AIFs in jurisdiction all over the world increased in the aftermath of the crisis of 2007. Today, in their choice of domiciliation, portfolio managers have to weigh the (dis)advantages of a regulated investment market against the

[149] Lang & Köhler 2011, p. 4.

(dis)advantages of an unregulated market. In, for example, the EU, where the AIFMD aims to create a safer environment for investors, but also introduces burdening regulatory oversight and high costs on compliant fund managers.

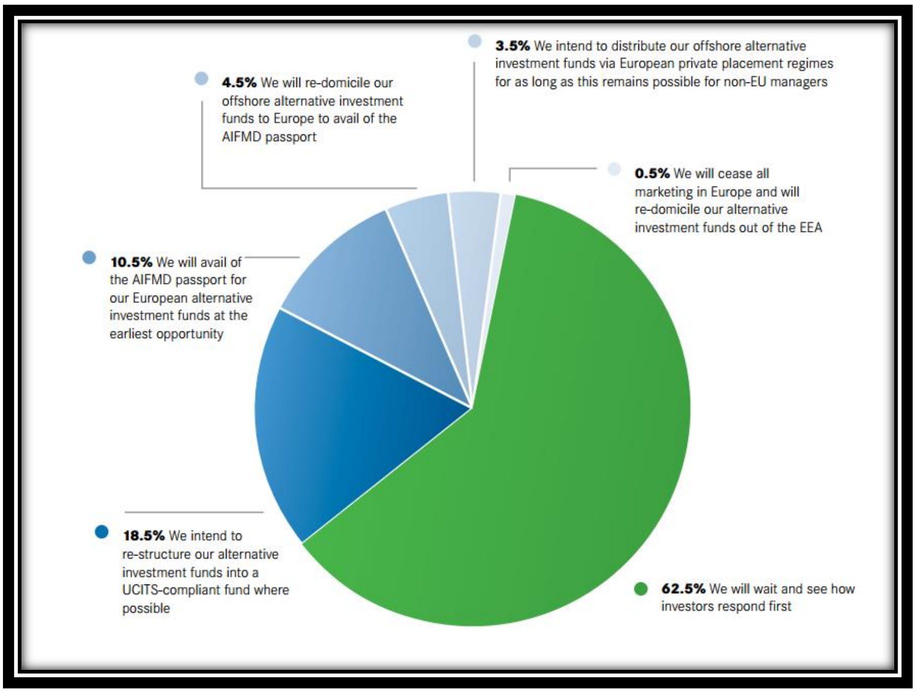
In order to be able to make an assessment on the behaviour of the fund managers, it is important to identify the factors to which fund managers attach the greatest importance in their choice for domiciliation. A survey performed by the Economist Intelligence Unit on behalf of Matheson, set out in June and July 2013 among 200 senior asset management executives who were headquartered in North-America, Western Europe, Asia-Pacific, Latin America, the Middle East and Africa, provides insight on the valuation of managers of certain legal, financial and distribution factors, in their choice for a European fund domicile. The results of this survey are included in Appendix I. Regarding legal and regulatory factors, the assets managers attached the greatest importance to the approach to the AIFMD and the sophistication of the national regulator, and less importance to the range of fund vehicles and the presence of a stock exchange in the country of possible future domicile. Concerning financial and business factors, the assets managers ranked the cost of doing business by far as the most important factor. Giving considerably less weight to tax treatment of fund vehicles and double tax treaties. Conspicuously, the managers attached less importance to having existent fund ranges or business relationships in a specific jurisdiction. And in relation to market and distribution factors, assets managers chose for speed to the market and the investors' perceptions of a jurisdiction, over the reputation of a jurisdiction as a global distribution hub and access to a large domestic (national) market.

Given earlier findings on, for example, the Cayman Islands as a major hedge fund domicile, some of these findings may be remarkable. The fact that the majority of hedge funds is domiciled on the Cayman Islands, seems to be, at least for a great part, dependent on the geographical location of- and the reputation and managers' experience with that jurisdiction. Therefore it is important to remain critical to some of the findings of this survey. The assets managers were able to rank, from one to three, the most influential decision-making factors in their choice for a European jurisdiction. Considering the decision of the survey-makers to focus on the specific choice for a EU jurisdiction, and the fact that 65% of the participating asset managers are domiciled outside Western-Europe, it is likely that, based on factors as reputation and geographical location, the EU would not have been their first choice of domiciliation. When they are then asked about the influential factors in case of their choice for a EU domiciliation, the decisive factors on that decision may differ from the factors that are influential on a choice for a non-EU domicile. Therefore the survey is not a completely reliable reflection of the practice, in terms of non-EU fund domiciliation.[150] Regarding the perspective of the research of this thesis, however, the survey performed by the Economist Intelligence Unit, does provide an insight on the decisive factors that influence the fund managers decision on EU domiciliation. Asset managers in that

[150] Matheson 2013, p. 29.

same survey were asked about their expectations on the reaction of their organisation to the implementation of the AIFMD. The results are included in Appendix J and figure 3. The majority, 62,5%, stated that they expected to wait and see how the investors would respond first. 18,5% indicated that they estimated their organisation to restructure existing future AIFMD-compliant funds into UCITS-compliant funds in the cases that it was possible, and only 10,5% suggested that they expected their firm to take the earliest opportunity to benefit from the new AIFMD passport. With respect to re-domiciliation, 4,5% indicated that they estimated their organisation to re-domicile their offshore AIFs to the EU in order to profit from the AIFMD passport, and a remarkable 1 of the 200 responsive asset managers expected their firm to end the marketing in the EU and to re-domicile their AIFs out of the EU. 29% of the asset managers expect that in 2016, their organisation will have over $1 billion assets under management in EU AIFs, where only 16% has that amount in 2013. [151] This last finding may delight the EC in their indefatigable hunt for growth and innovation in the EU in 2020.

Figure 3: Reaction of asset managers to the AIFMD



Source: Matheson 2013, p. 32.

In January 2009, the Qatar Financial Centre Authority hosted in London a debate on fund domiciliation. A large group of fund investors, -managers and -experts from all over the world participated in that debate, and deliberated about the question on what the effects of the increase in AIF regulation on the world's fund domiciles would be, and if any changes in patterns of fund domiciliation would likely occur. Dermot Butler: '*I am convinced that EU domicile centres, particularly Malta, will stand to benefit*

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[151] Matheson 2013, p. 14.

from these changes'.[152] Karl McEneff [153] : '*investors are the ones that ultimately matter and they are going to ask for regulated products'*. David Woodhouse: '*I do not think that patterns of fund domiciliation will change as a result to what has happened, unless there are changes will be made to the tax code*'. Gavin Farrel [154]: '*there will be changes to fund domiciliation patterns but they will not be substantial and may not last for that long'*. Gordon Wilson [155]: '*I think that there will be changes to the way funds are put together and that what has happened has been "a great learning curve"*.' [156] The large diversity of the opinions in this debate is a projection of the very diverse estimations on fund domiciliation that are present on the investment market. The fact that so many managers indicated that they would not immediately respond to regulations as the AIFMD and that they wanted to wait and see how the investors would respond first, can be credited to this large diversity of expectations among both investors and fund managers.

The regulatory cost burden may have a different effect on each type of AIF. Leveraged funds that are just over the EUR 100 million threshold will be much more affected by the recurring costs than the funds that have ten times their size. [157]

7.1. Data analysis

Given the highly diverse speculations on fund domiciles, and the fact that there seems to be some truth in the majority of the arguments, the only clear assessment of the response of the investment markets to the AIFMD can be found within the industry itself. Not on the basis of the opinions of market players in questionnaires or debates, but through the use of incontrovertible data on investment markets. Due to the only recent implementation of the AIFMD, it is, however, quite a challenge to obtain data on fund domiciliation, since only limited public data exists. At the moment, several research centres are collecting data and performing surveys and assessments on the impact of the AIFMD on fund domiciliation. For example The NED and ADI are conducting the first detailed survey on the impact of the AIFMD on EU's fund business. [158] Considering the fact that the Directive only recently came into force, and assuming that the AIFMD does have any impact on fund domiciles, it is not likely that that particular impact will be immediately observable. Besides, due to the substantial reliance of the

[152] QFCA 2009, p. 20-22.
[153] Karl McEneff serves as Managing Director and Director at Daiwa Securities Trust Europe Limited. (QFCA 2009, p. 20-22.)
[154] Gavin Farrel is partner at Mourant Ozannes, an executive member of the Guernsey Investment Fund Association (GIFA) and a member of the Finance Sector Group (FSG). (2014 QFCA 2009, p. 20-22.) "Gavin Farrell is in 'high demand' for his investment funds expertise and emerges as one of our most highly nominated offshore lawyers due to his 'technical prowess, attention to detail and commercial approach'." (International Who's Who of Private Funds Lawyers)
[155] Gordon Wilson has been the Managing Director of Caledonian Fund Services (Europe) and is now Adivosry Directive at PwC. (QFCA 2009, p. 20-22.).
[156] QFCA 2009, p. 20-22.
[157] IFI 2013, p. 12-14.
[158] Fund Domiciles 25 April 2014.

investment industry on reputation and trust, the widespread rumours about a regulation on the EU alternative investment market in the period prior to the implementation, may already have had impact on the domiciliation of funds. However, the premature and early impact of the AIFMD are expected to be modest, due to the hesitant behaviour of investment funds, like many of the portfolio managers in the survey performed by the Economist Intelligence Unit have indicated. Next to that, it is important to bear in mind that the financial crisis of 2007 also had its impact on the distribution of AIFs on the investment market, which might cloud the data on fund domiciliation.

Despite all these deliberations, it is still rewarding to assess the alterations in the distribution of alternative funds on different investment markets. Several national and supranational financial authorities collect data on the number and size of established investment funds in different jurisdictions, and based on these databases singular results on domiciliation are visible. Note that the data that is used in the context of this research includes data on domiciliation, as well as re-domiciliation and co-domiciliation, and that for the purpose of chapter 7.1 these matters are consolidated to 'domiciliation'.

7.1.1.The EU

Given the large variety of jurisdictions within the EEA with different levels of activity in the investment industry, it is important to realize that all of these jurisdictions should be taken into account in the assessment on the impact of the AIFMD on fund domiciliation. The Directive can benefit the one jurisdiction, but at the same time, detriment the other. For the EC it is important that the AIFMD will eventually provide a positive contribution to growth and innovation in the EU as a whole, but that is a question that should be subject of another research. In the context of this research, a lot of attention has been given to popular fund domiciles: Ireland and Luxembourg [159]. Despite the large differences in culture, legal systems and economies, these countries have investment fund servicing as a large common denominator. Due to synergies in intermediaries' charges for servicing, the combination of both jurisdictions is also considered to be the 'duopoly in EU fund domiciliation'. This, however, also creates options for emerging EU domiciliation centres other than Luxembourg and Ireland.

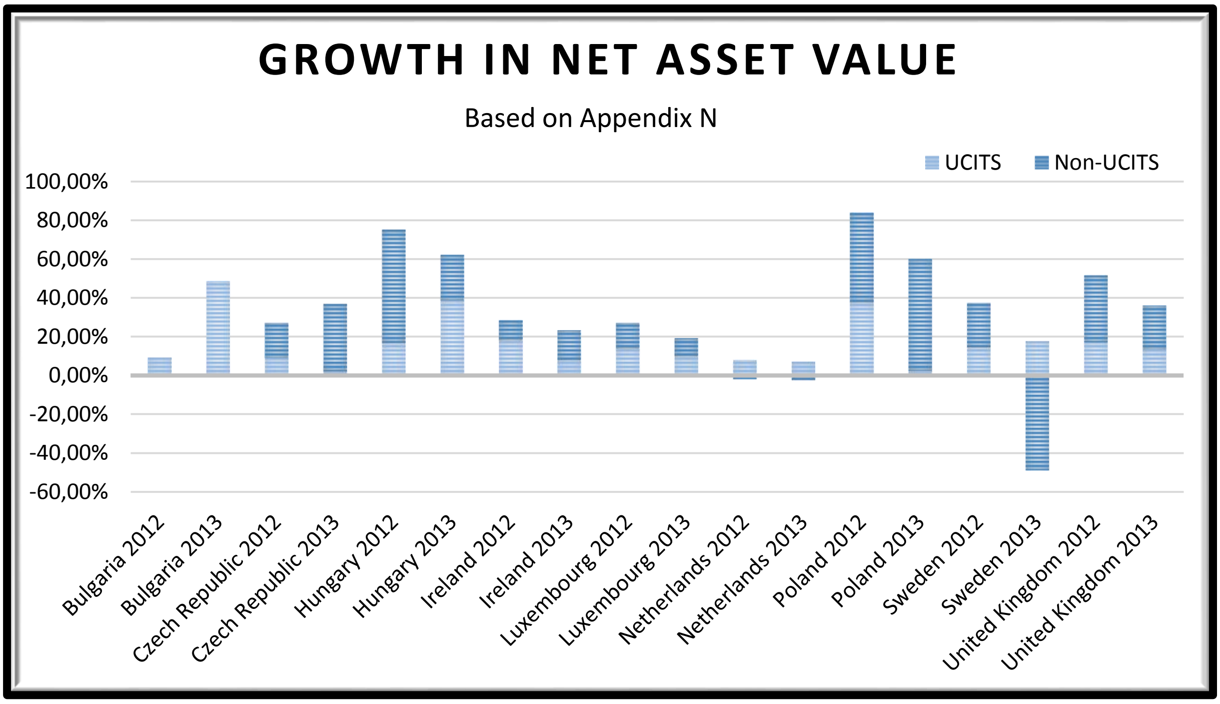
EFAMA[160] releases monthly and quarterly statistical papers on the trends in the European and international investment fund industry. With the use of the -by the EFAMA- disclosed data, an assessment was made on the either positive- or negative growth in number of funds, net asset value of funds and the average value per fund of every jurisdiction within the EU. The data released by the EFAMA are provided in Appendix K (the number and net asset value of UCITS and non-UCITS funds in the EU). With the use of this data, I have made a table and several graphs on growth, which are

[159] Prior to the AIFMD, Luxembourg already implemented special laws for particular investment products (for example Partie II for retail funds, SICARs for private equity (and venture capital funds), SIFs for special funds) some of which imposed stricter, and some a lighter degree of manager regulation. [www.efama.org].
[160] Available at: [www.efama.org].

included in Appendix L (the growth in 2012 and in 2013, in comparison with the previous year, of investment funds in the EU), Appendix M (the growth in the number of funds), Appendix N (the growth in net asset value) and Appendix O (the growth in net asset value per fund).

In the assessment on the data of Appendix K to O, and subsequently in the context of chapter 7.1.1, the conception of 'EU' is different from the one that was used for the purpose of this thesis. Due to an absence in data, Iceland, Estonia, Latvia and Cyprus were left out of the assessment and Switzerland and Turkey were, on the contrary, included. Next to that, given the scope of the AIFMD, non-UCITS are equal to AIFs.

Figure 4: Growth in net asset value of several EU jurisdictions



Source: own analysis on data of EFAMA.

In the 'EU', there has been a notable growth in number of AIFs in both 2012 and 2013. The growth in number of AIFs is actually bigger than the overall growth in number of UCITS. The number of UCITS, in fact, declined, in December 2011, EFAMA counted 36.175 UCITS and in December 2013, only 35.618 remained. At the same time, the 18.219 AIFs in December 2011 grew to 19.524 in December 2013. The growth in net asset value of the AIF market in the 'EU' is remarkable, with 16% in 2012 and another 10% in 2013. The net asset value of the UCITS market also raised, even with the decline in number of UCITS in 2012. The effect that this growth of net asset value of the market has on the average net asset value per fund is significant. In December 2011, the average net asset value per UCITS in the 'EU' was EUR 155,74 million and in December 2013 it was EUR 192,76 million. The average net asset value per AIF in December 2011 EUR 125,49 million raised to EUR 149,69 million in December 2013. This implies that an average UCITS in the 'EU' holds relatively more value that the average AIF.

Although the alterations in the entire 'EU' are highly interesting for any assumptions on the role of the EU in the investment industry, the numbers of growth of some individual jurisdictions can also be of added value in the assessment on the impact of the AIFMD on fund domiciliation. Luxembourg, for example, showed, in general, equal values of growth as the entire 'EU'. Ireland, on the other hand, experienced mostly a higher growth than the growth of the 'EU', and particularly the number of AIFs in Ireland grew twice as much as the average AIFs in the 'EU'. In Bulgaria the non-UCITS industry remained flat, the one fund continued to be the only player of the same size, but the net asset value of the UCITS market grew with almost 50% in 2013. In the Czech Republic were neither in 2012 nor in 2013 any new AIFs registered, but the net asset value of the AIF market did grow significantly with respectively 18% and 35%. Of all the jurisdictions that were included in this analysis, Hungary must be the most remarkable one. In 2012, the number of AIFs grew with an astonishing 130%, and the net asset value did grow significantly but not nearly as much as the amount of registered AIFs. Moreover, also the growth of the net asset value of the UCITS market showed a remarkable increase in both 2012 and 2013. Not only Hungary, but also Poland experienced noteworthy growth rates. In 2012, the number of UCITS in Poland grew significantly and the net asset value of both the UCITS and the AIF market showed an even greater growth. The growth rates in the U.K. are consequent; in 2012 and 2013 there was a small decline in their number of UCITS and a small growth in their number of AIFs. In both years there was a significant growth in net asset value on the AIF as well as the UCITS market. Sweden on the other hand, experienced a rather remarkable negative growth. The number of AIFs declined in both 2012 (-17%) and 2013 (-53%) and the net asset value of the AIF market in 2013 correspondingly declined with nearly 50%. Lastly the Netherlands, where there was in fact no significant growth or decline, except for the noteworthy decline of nearly 20% in number of AIFs and the small decline of the net asset value of the AIF market in both 2012 and 2013.

7.1.2.<u>The Cayman Islands</u>

Contrary to the onshore EU jurisdictions, the Cayman Islands are considered to be an offshore fund centre. Particularly hedge funds admire domiciliation on the Cayman Islands, as is provided in exhibit 3 of appendix E. Although the Cayman Islands implemented their Mutual Funds Law on 26 July 1993 and implemented the revised version in 2013, in vernacular speech, the Caymans are still referred to as an unregulated investment fund Utopia. The Cayman Islands Monetary Authority defines a mutual fund as: '*any company, trust or partnership either incorporated or established in the Cayman Islands, or if outside the Cayman Islands, managed from the Cayman Islands, which issues equity interest redeemable or repurchasable at the option of the investor, the purpose of which is the pooling of investors' funds with the aim of spreading investment risk and enabling investors to receive profits or gains from investments*'.[161] Under the MFL, there are several categories of funds to be identified: (i) licensed-; (ii)

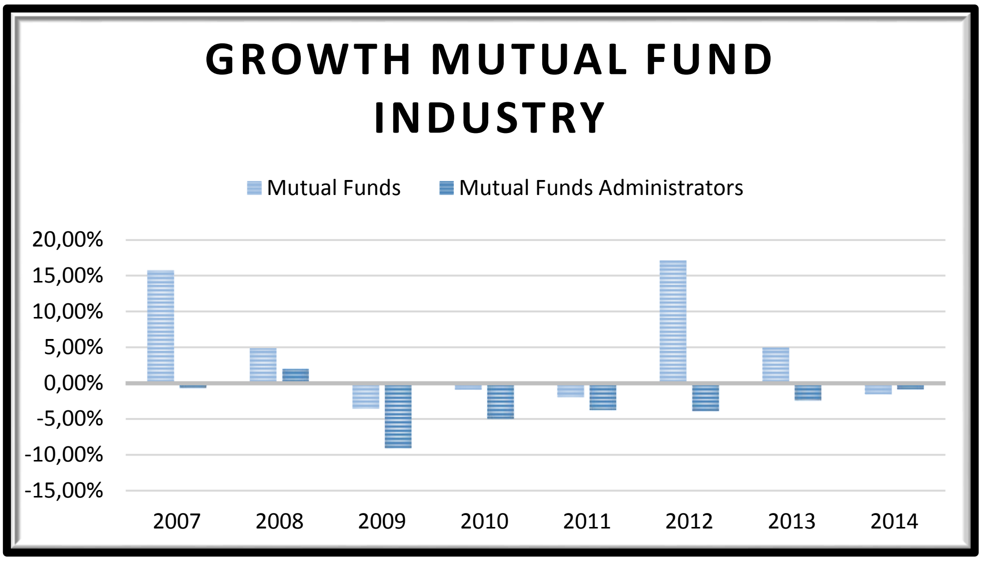
[161] Available at: [http://www.cimoney.com.ky/regulated_sectors/reg_sec.aspx?id=96].

administered-; (iii) registered- and (iv) master mutual funds. Under section 4(1), a mutual fund that operates in and from the Cayman Islands must have a license, except if the fund falls under the exemptions of section 4(3) and (4). To be considered an administered mutual fund, the fund must be in the possession of a CIMA-licensed mutual fund administrator who provides his principal office. A registered mutual fund must have either a minimum aggregate equity interest of CI$ 80,000 (or US$ 100,000) purchasable by a prospective investor or the equity interests must be listed on a stock exchange approved by CIMA. A master mutual fund must have either a minimum aggregate equity interest of CI$ 80,000 (US$ 100,000) purchasable by a prospective investor in the master fund or the equity interests of the master fund must be listed on a stock exchange approved by CIMA.[162] Under the MFL, there are also three categories of mutual fund administrators: (i) full-; (ii) restricted-; and (iii) exempted fund administrators. Full fund administrators can perform administration on an unrestricted number of mutual funds, whereas restricted fund administrators can only provide services for maximum 10 funds and must receive an approval from the CIMA for each fund for which they provide administration. An exempted company may redeem or purchase its own shares. [163]

An assessment on the data provided by the CIMA, reveals that the Cayman fund industry experienced several noteworthy developments as of 2006. With the use of the data of the CIMA, I have made a table and a graph on the growth rates, which are included in Appendix P and figure 5. The total growth in mutual funds, particularly registered funds, in 2007, in comparison to 2006, is remarkably high (16%). A similar significance is experienced in the growth of the total amount of mutual funds in 2012 (17%). The 1,891 master funds that entered the investment market in 2012, contributed to this substantial growth. In relation to the steady growth in mutual funds from 2006 to 2014, it is especially remarkable that, in general, the number of mutual fund administrators shows a major decline. In 2006, 153 administrators were observed on the Cayman fund market, and in 2014 this number has declined to 120. Especially in 2009, in comparison to 2008, there was a vast decline of 9% in mutual fund administrators. Although it is remarkable that this decline was visible shortly after the beginning of the financial crisis, it is impossible to accredit the decline to this event only.

[162] Available at: [http://www.cimoney.com.ky/regulated_sectors/reg_sec.aspx?id=96].
[163] Available at: [http://www.cimoney.com.ky/regulated_sectors/reg_sec.aspx?id=96].

Figure 5: Growth in mutual fund industry on the Cayman Islands



Source: own analysis on data of Cayman Islands Monetary Authority

8. Conclusion

Prior to the financial crisis of 2007, there had been a period of rapid credit growth, strong use of leverage, low risk premiums, mounting assets prices, copious availability of liquidity and a development of bubbles in the real estate sector. These developments were enhanced due to a high level of financial deregulation and a concentration of power of banks as a result of a large amount of mergers in the late 1990s, which amplified moral hazard and incentives for risk taking among financial institutions. The levels of trust and confidence, on which the entire financial system operates, had been severely corroded. Due to the over-stretched leveraged positions of financial institutions, even the smallest alterations in trust in parts of the asset markets were able to make the entire structure collapse. The trust that intermediaries had in each other was diminished, e.g. the Madoff fraud, and quickly thereafter, also the trust of investors in the financial industry was wiped out, e.g. the collapse of the Lehman Brothers.

Regulators were quick in their response to the financial crisis, and particularly the EC used the opportunity to subject the previous light-regulated alternative investment market to more stringent regulatory oversight. After a process of heavy debating on the scope and the objective of the Directive, Member States made several compromises on the AIFMD and introduced a long transactional period subject to advices of the ESMA. In anticipation to the evaluation of the ESMA, which is scheduled on 22 October 2018, the Directive allows Member States to continue pursuing a national placement regime, providing each country in the EEA the opportunity to have its own authorization scheme for third country entities.

In order for AIFMs to be compliant with the Directive, certain requirements must be met. The downside of having to meet these requirements is the significant increase in compliance costs that, particularly, reporting requirements, depositaries and the use of an administrator, impose on AIFMs. Despite the vast amount of critique on the content of the AIFMD, the implementation of the Directive does create several advantages for the EU investment industry. The EC intended to generate a safe(r) single EU market for AIFs and their investors. In order to achieve this, the AIFMD provides the industry with tools to reduce systemic risk and to increase transparency.

The AIFMD distinguishes two types of collective investment funds: (i) UCITS, and (ii) all funds that do not qualify as such. Apart from the exemptions as discussed in 4.4.3, it is a fund that falls under the second category that generally qualifies as an AIF. This impressive broad scope is an illustration of the EC's aim to keep up with the flexibility of the industry and the entities' indefatigable ability to find loopholes in regulations. The EC subjected the powerful and decision-making AIFMs to the Directive, and avoids making any difference between types of AIFs that are commonly known in vernacular speech. But to be able to make a more substantiated assessment on the impact of the AIFMD, a distinction must be made between the various types of alternative funds that have different investment cycles and portfolios. Hedge funds, private equity and real estate funds are the most familiar in the investment industry. Hedge funds generally make use of incentive fees, short-selling systems and leverage. Private equity funds, however, usually invest in more mature companies and therefore typically postpone the investment of their capital, in order to be able to perform a proper due diligence on their investment targets. Venture capital is in fact a form of private equity, though contrary to private equity firms, venture capital funds typically invest in early-stage, innovative portfolio companies. Real estate funds generally make illiquid long-term investment in real estate. Next to these types of AIFs, the investment industry is also made up of other, perhaps less-common, alternative funds such as special funds for professional investors, HNWis, and funds under the ELTIF, EuVECA and EuSEF.

All these AIFs make different choices on domiciliation. Up until a few years back, their choice of domicile was considerably influenced by deliberations on tax and regulatory cost-efficiencies, that made a lot of AIFs, particularly hedge funds, choose for offshore domiciliation. However, after the collapse of the financial markets, and subsequently the drop in trust among- and towards investment funds, the onshore market regulators heavily increased the pressure on offshore funds. Fund managers had to increase their efforts to gain the trust of investors through realising high sustainable profits by presenting the fund's integrity and cost-efficiency to investors. Although the actual impact of a regulated market, rather than that of an unregulated market, on the integrity of funds may be questionable, AIFMs can send out a strong signal, and thereby appeal to the investors' confidence if they explicitly choose for a regulated jurisdiction. Favourable tax regimes and treaties of jurisdictions can significantly reduce costs on funds, but AIFMs must consider the increase in supervision on tax evasion. Another factor that can be influential on the decision on domiciliation of AIFMs, is the previous familiarity of that manager with that particular jurisdiction. Due to their substantial dependence on trust, investors attach great importance to good reputations, familiarity with the market culture and a large network in a jurisdiction. A combination of these factors can send exactly the desired signal of trust to investors. Besides, aspects such as a geographical location and insolvency regimes can also influence the decision of the AIFM to domicile in a specific jurisdiction. The question that is substantial, in this respect, is how much weight investors, and subsequently AIFMs, attach to these matters, for them to be of any influence on their choice of domiciliation.

In their choice for EU domiciliation, 200 assets managers have expressed their deliberations. Regarding legal and regulatory factors, the managers attached the greatest importance to the approach to the AIFMD and the sophistication of the national regulator. Concerning financial and business factors, the managers ranked the cost of doing business by far as the most important factor. And in relation to market and distribution factors, the managers chose for speed to the market and the investors' perceptions of a jurisdiction. It is obvious that pre-AIFMD the majority of the managers are biding and attach great value to the response of investors to the implementation.

There have been some significant changes in major fund domiciles over the past few years. Despite the deliberations on the level of unbiasedness of the data, e.g. due to the only recent financial crisis that also can have had its impact on the market, several alterations were perceptible. In the 'EU', there has been a notable growth in number of AIFs in both 2012 and 2013, where the number of UCITS, declined. The growth in net asset value of 'EU' funds is remarkable and significantly increases the average net asset value per fund. In December 2011, the average net asset value per UCITS in the 'EU' was EUR 155,74 million and in December 2013 it was EUR 192,76 million. The average net asset value per AIF in December 2011 EUR 125,49 million raised to EUR 149,69 million in December 2013. On the Cayman Islands however, a major global fund domicile, the number of mutual fund administrators shows a major decline. Especially in 2009, in comparison to 2008, there was a vast decline of 9% in mutual fund administrators. Compared to 2008, in 2010 The Cayman Islands had been able to maintain their market share of 37%, while Delaware, lost around 21.22% of AIFs. The EU, or rather an accumulation of Luxembourg, Ireland and Malta, had actually gained a considerable market share in the same time period.

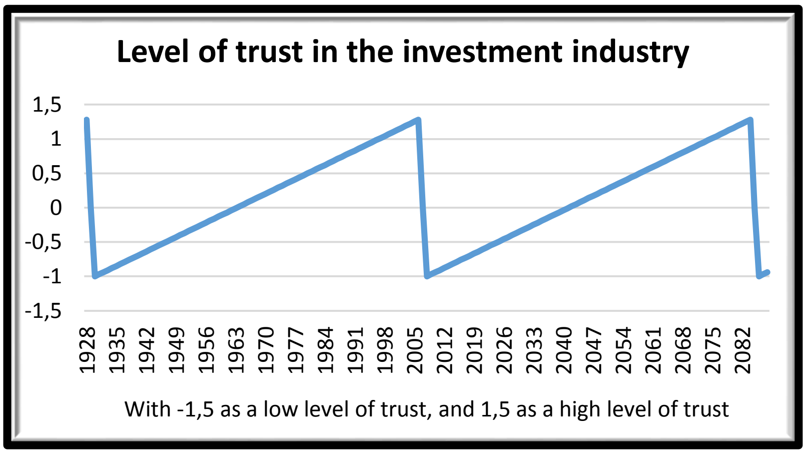
The findings in this research provides some preliminary insights on the impact of the implementation of the Alternative Investment Fund Managers Directive on the domiciliation of alternative investment funds in Europe. Regarding the performed research, it is obvious that no straightforward answer can be given to this research question. Several events have influenced the investment industry in the past few years, it was not only the implementation of the AIFMD that could have been of influence on the domicile behaviour of AIFs. Besides, due to the substantial reliance of the investment industry on reputation and trust, the widespread rumours about a regulation on the EU alternative investment market in the period prior to the implementation, may already have had impact on the domiciliation of funds. Bearing this in mind, it is still possible to provide an answer to the research question. That the major fund domiciles of the investment industry showed small alterations over the past few years can be ascertained. Especially the net asset value of the European fund market has significantly increased.

Whether this change can solely be accounted to the implementation of the AIFMD is impossible to determine, because all the recent major events in the fund industry are correlated. In my opinion, it is therefore possible to say that the increase in domiciles in the EU of the fund industry is in fact an impact of the implementation of the AIFMD.

8.1. *The future perspective for AIFs*

Based on the current limited amount of available data on the impact of the AIFMD on the alternative investment market that exists to date, it is challenging to make concrete expectations on the behaviour of investors, funds and fund managers in the future. However, based on the findings in this research it is likely to say that the observable small alterations to the investment industry will continue in the upcoming years. The graduate increase in both the number of UCITS and AIFs and the net asset value of these markets in the EU, as well as the decline of mutual fund administrators on the Cayman Islands, will most likely proceed. Particularly during the course of the transactional period of the AIFMD, and in the event where the EC decides to allow non-EU AIFMs to obtain a EU passport. Due to the large amount of stakeholders and the large variety of jurisdictions involved, it is not plausible that any impact on the investment market will be immediately observable.

Figure 6: Estimated levels of trust in the investment industry



Source: own analysis.

Subsequently, I expect that the financial markets will show an ever continuous fluctuation regarding the levels of trust. I have provided a broad outline of this expected fluctuation in exhibit 3. Fund managers that market in an industry with low amounts of trust will generally be more attracted to stricter regulations and safer investment environments to reassure their investors. Fund managers that market in an industry that is driven by overconfidence, of both managers and investors will, on the contrary, usually be attracted to jurisdictions that impose low levels of stringent regulation and costs on the fund. The market that is driven by overconfidence eventually will collapse due to excessive risk taking, leading to regulators that consequently will jump in with new stringent regulation.

Furthermore, notice must be given to the rise of the emerging markets. As of 2003, investors show increasingly more interest in emerging markets. Being involved in emerging markets can be a hazardous and opaque business, due to e.g. social and political instability and a heavily dependence on natural resources. Regarding a long-term perspective, however, emerging markets can be very rewarding for long-term investments due to the potential lion's share of growth across the world of large countries as Brazil, Russia, China, and India in the decades to come. [164] India, for example, has recently increased its attention on attracting funds and has implemented regulation to support this. With the introduction of the Securities and Exchange Board of India in 1993 and the SEBI Mutual Fund Regulation in 1996, mutual funds increased in popularity. As a counterpart to the EC's ELTIF Regulation, the SEBI Board has recently approved a Long Term Policy for Mutual Funds in India to achieve a continuous sustainable growth of the mutual fund industry. [165] It is not unlikely that major fund domiciles, as the Cayman Islands, Luxembourg and Ireland, will face increased competition from these emerging markets in the future.

8.1.1.Recommendations

Regarding the desired increase in growth and innovation in the EU, the EC will have to proceed to attach great importance to fund regulation and continue to meet the specialised needs of smaller investment funds. Moreover, I would recommend is that the EC would open the EU investment market for non-EU AIFMs through the implementation of the third-country-rule. And the EC should remain critical towards the advantages of strict regulation over increasing supervision on funds.[166]

[164] Forbes 2013.
[165] SEBI 2014.
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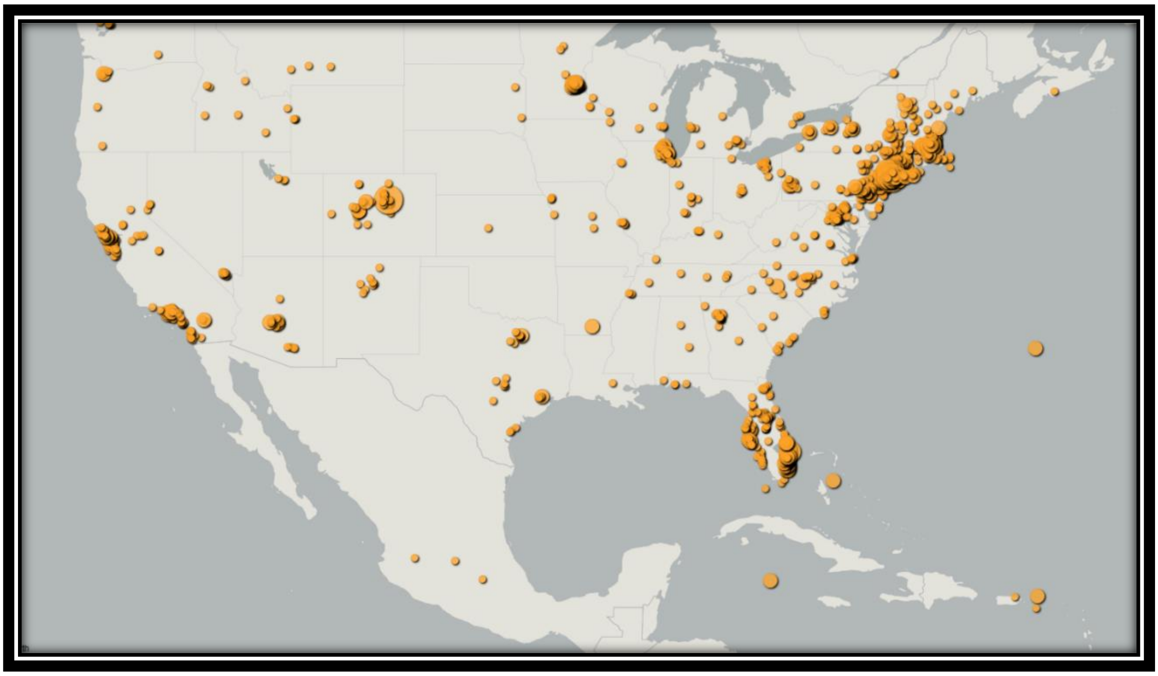
http://geocommons.com/maps/2888

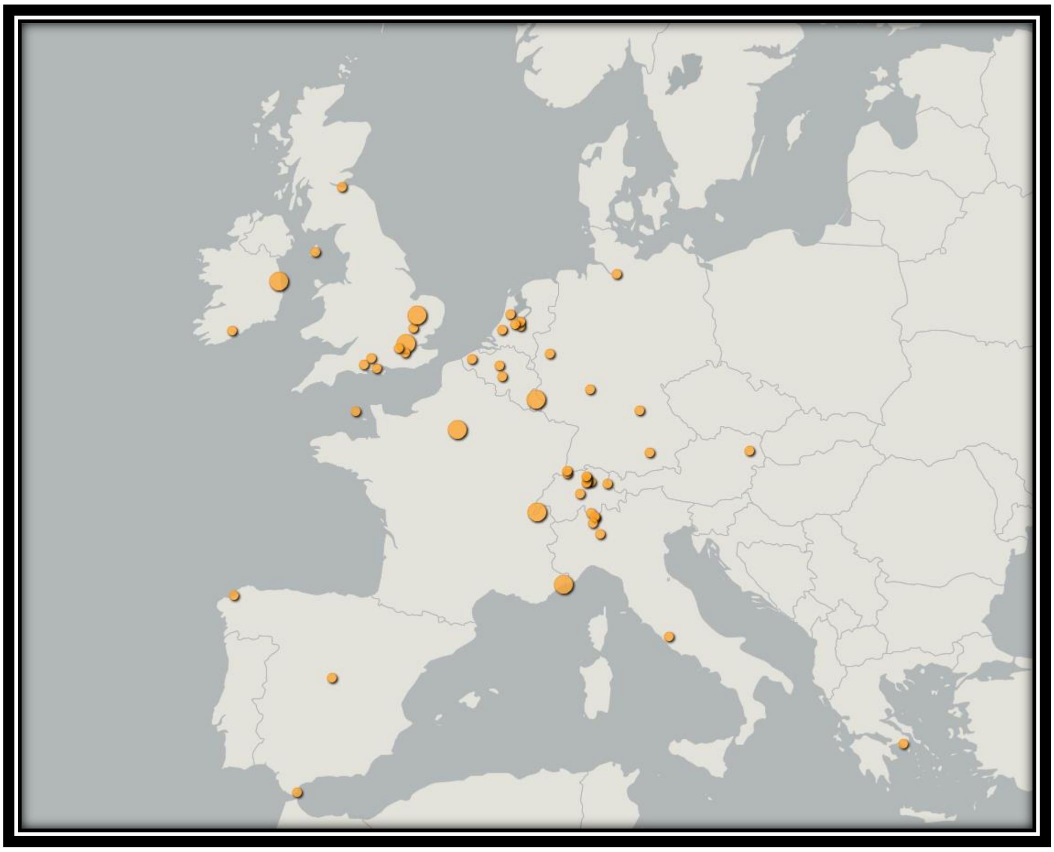
10. Appendices

10.1. *Appendix A: Madoff Clients Worldwide*

10.1.1. United States



10.1.2. Europe



Source: [http://geocommons.com/maps/2888].

10.2. *Appendix B: AIFMD Timeline*

AIFMD Timeline[91]

Date	*Event*	
21 July 2011	Entry into force of the AIFMD (Art. 70 AIFMD)	
22 July 2013	Deadline for Member States to implement AIFMD in domestic legislation (Art. 66(1) AIFMD)	**EEA entities**[92] Passport available, no national placement **TC entities**[93] No passport, national placement available
22 July 2014	Deadline for AIFMs to submit an application for authorization to their Competent Authorities (Art. 61(1) AIFMD). Member States must provide to the Commission and ESMA certain information regarding the marketing of AIFs to retail investors on its territory (Art. 43(2) AIFMD).	
22 July 2015	ESMA issues an opinion to the European Parliament, Council and Commission whether to extend the EEA passport to third country entities (Art. 67(1) AIFMD)	
22 October 2015	Having regard to the recommendations made by EMSA, the EC decides whether to extend the EEA passport to third country entities (Art. 67(6) AIFMD)	**EEA entities** Passport available no national placement **TC entities** Passport may be available national placement available
22 July 2017	The EC starts a review of the AIFMD (Art. 69 AIFMD)	
22 October 2018	EMSA issues an opinion on the functioning of the EEA passport with regard to third country entities and the termination of the country-by-country placement regime (Art. 68 AIFMD)	
22 January 2019	The EC decides, based on ESMA's advice, whether to terminate the national placement regime (Art. 68(6) AIFMD)	**EEA entities/TC entities** National placement may be terminated Passport available

Source: Zetzsche 2012, p. 407.

10.3. *Appendix C: Number of mutual funds by country*

Table 3: Number of funds, by country

Table 3 shows the geographical distribution of mutual funds of the 1,000 largest fund companies worldwide between 1997 and 2006.

	Number of Funds	of which domiciled by foreign companies	of which domiciled by domestic companies
Austria	542	74	468
Belgium	318	6	312
Switzerland	193	62	131
Germany	529	46	483
Spain	1,580	171	1,409
Finland	32	0	32
France	1,454	386	1,068
United Kingdom	690	212	478
Ireland	325	321	4
India	376	149	227
Italy	12	0	12
Luxembourg	2,934	2,911	23
Mexico	59	25	34
Malaysia	65	27	38
Netherlands	107	0	107
Norway	19	0	19
Portugal	45	8	37
Sweden	12	2	10
Singapore	127	51	76
Thailand	141	29	112
Taiwan	191	78	113
United States	1,984	193	1,791
Total	11,735	4,751	6,984

Source: Lang & Köhler 2011, p. 35.

10.4. *Appendix D: Legal Structure of Hedge Funds by Domicile Country*

80 **Aragon, Liang, and Park:** *Onshore and Offshore Hedge Funds: Are They Twins?*
Management Science 60(1), pp. 74–91, ©2014 INFORMS

Table 1 Legal Structure of Hedge Funds by Domicile Country

			Legal structure (%)							
Domicile country	No. of funds	Average AUM ($mm)	Limited partnership	Limited liability company	Open-ended investment company	Exempted company	Exempted limited liability company	Open-ended mutual fund	International business company	Other structures[a]
Onshore funds	1,229	111.86	83.08	11.55	1.14	0.33	0.00	0.41	0.00	3.50
Offshore funds	1,710	226.10	3.51	9.88	32.98	16.14	13.86	4.74	3.39	15.50
Cayman Islands	1,161	212.58	3.70	8.79	26.61	23.17	19.38	3.10	0.00	15.25
British Virgin Islands	262	324.38	3.44	7.25	53.05	0.76	0.38	5.34	17.56	12.21
Others	287	183.33	2.79	16.72	40.42	1.74	3.83	10.80	4.18	19.51

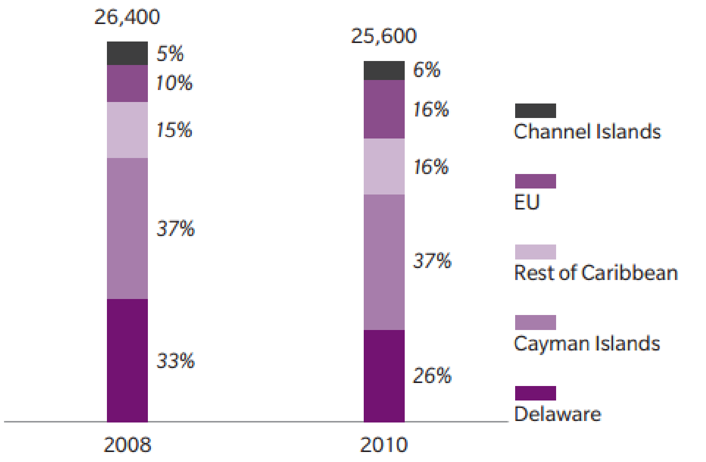
Notes. This table compares offshore hedge funds with onshore funds in terms of fund size (measured by the average value of assets under management (AUM) during the fund life) and legal structure (form of organization). Onshore funds are registered in the United States. Offshore funds are registered in low-tax jurisdictions such as the Cayman Islands, British Virgin Islands, Bermuda, Bahamas, Netherlands Antilles, Mauritius, St. Kitts and Nevis, Saint Lucia, Anguilla, and Barbados. The data is from the TASS database, and the sample period is from January 1994 to December 2010.

[a]Other structures are closed-ended investment company, exempted unit trust, individual managed account, limited corporation, protected cell company, segregated portfolio company, and unit trust.

Source: Aragon, Liang & Park 2014, p. 74-91.

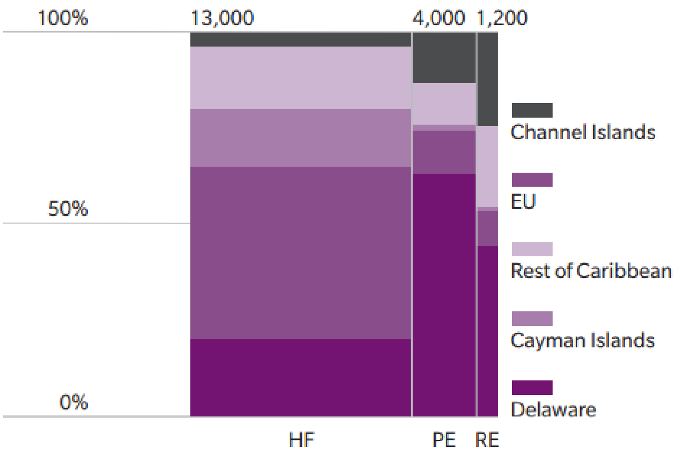
10.5. *Appendix E: AIFs in major fund jurisdictions*

EXHIBIT 2: NUMBER AND PROPORTION OF AIFS IN MAJOR FUND JURISDICTIONS



Source: Oliver Wyman analysis
Notes: Rest of Caribbean is Bermuda and British Virgin Islands; EU consist of Ireland, Luxembourg and Malta

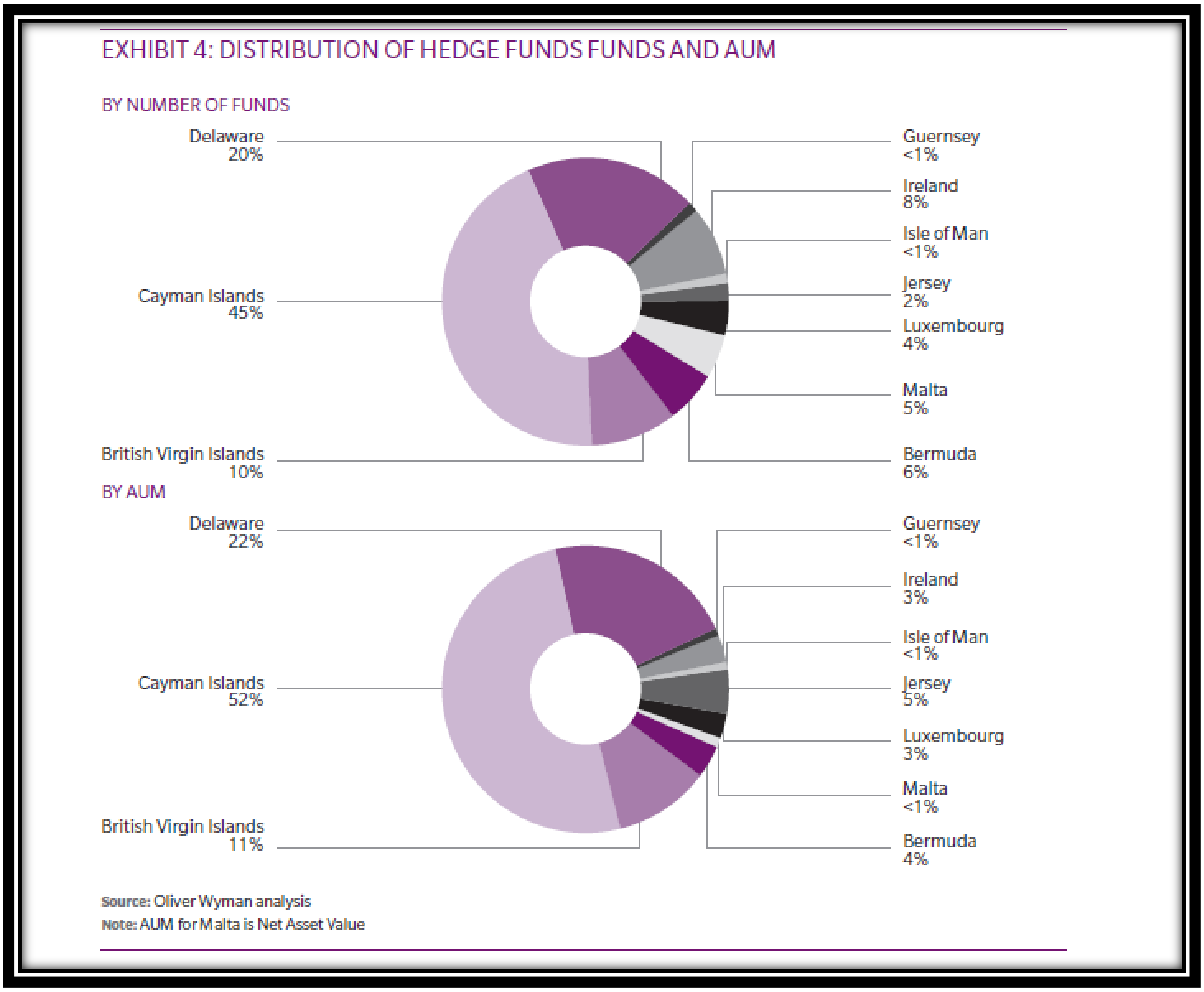
EXHIBIT 3: ESTIMATED DISTRIBUTION OF NUMBER OF AIF IN MAJOR FUND CENTRES



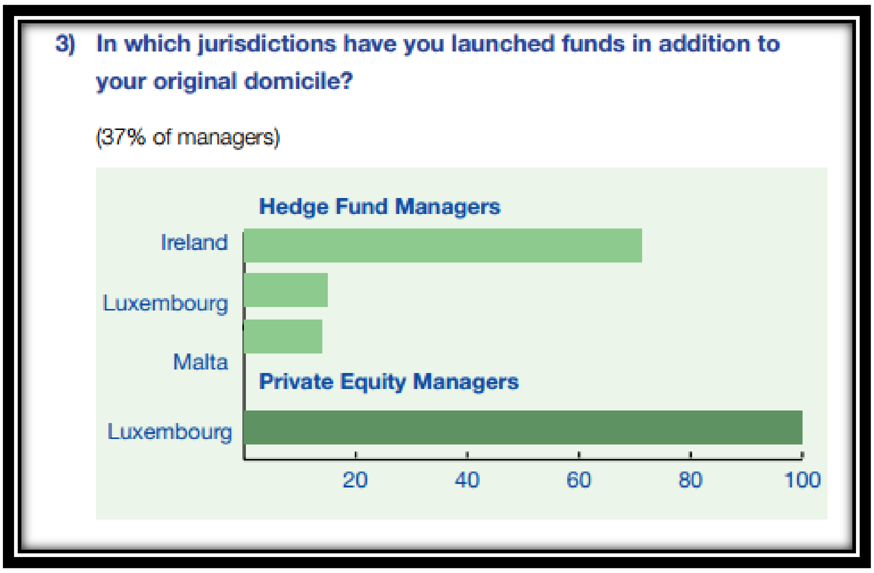
Source: Oliver Wyman analysis
Notes: Figures do not include fund of funds; Rest of Caribbean is Bermuda and British Virgin Islands; EU consist of Ireland, Luxembourg and Malta

Source: ALFI 2011, p. 2.

10.6. *Appendix F: Distribution of hedge funds*

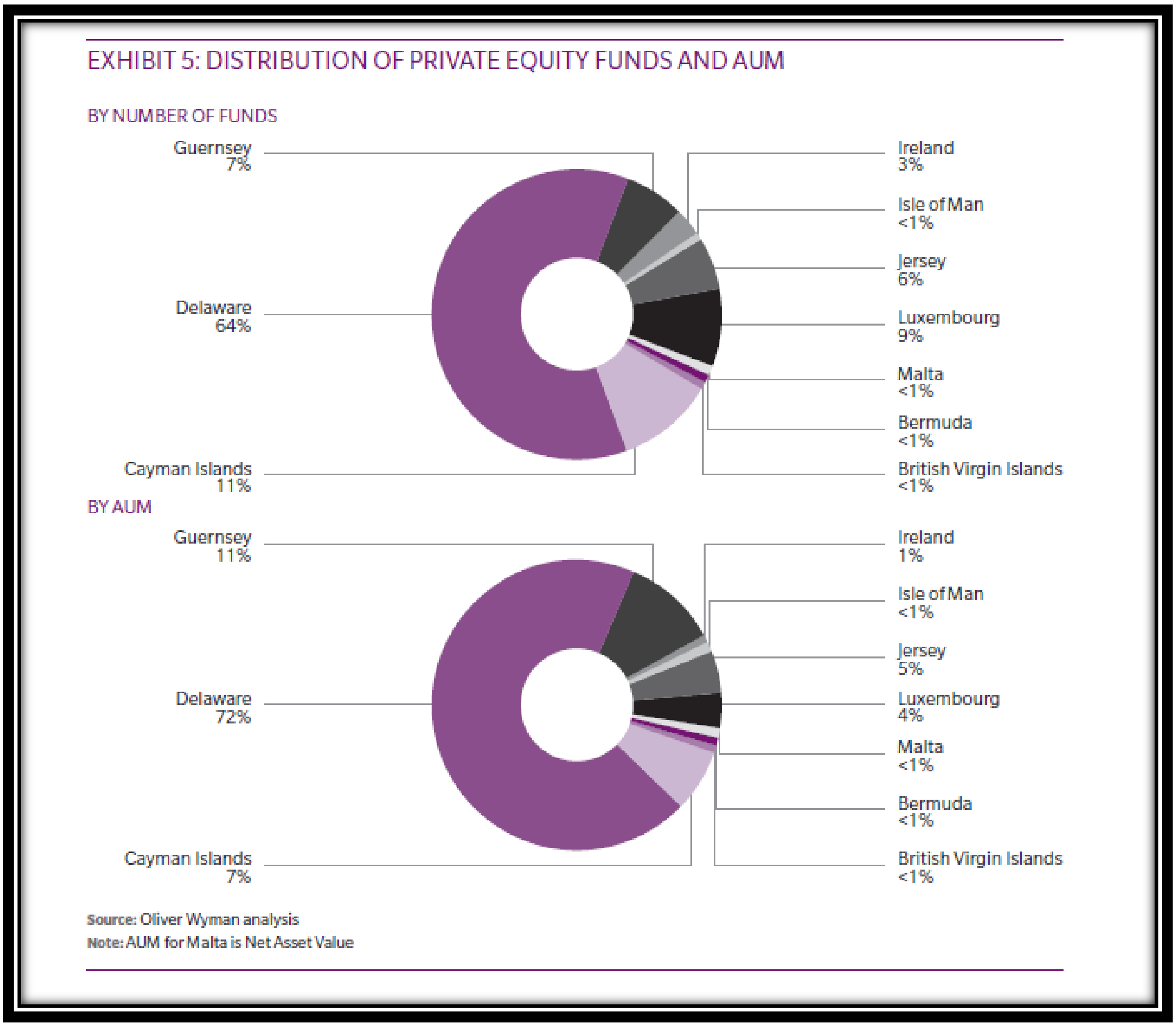


Source: ALFI 2011, p. 3.

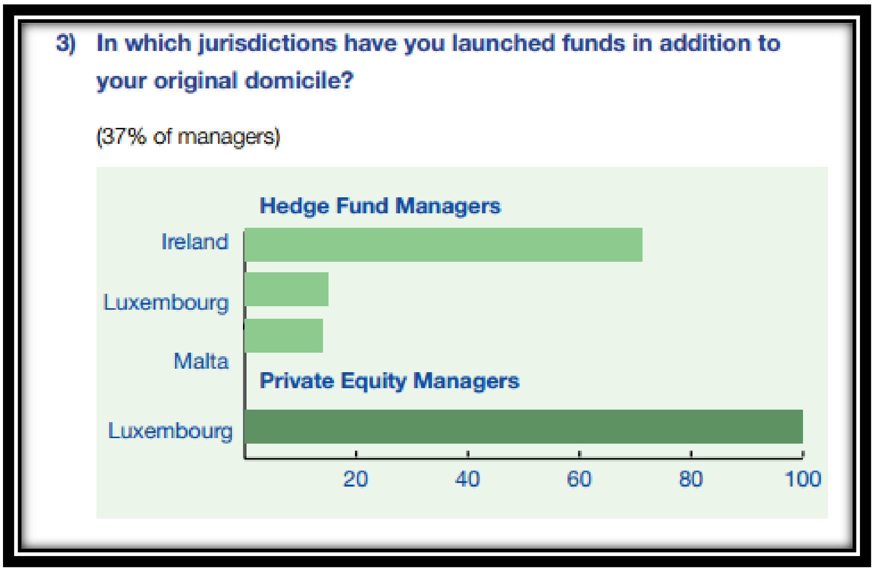


Source: APEX 2011, p. 4.

10.7. Appendix G: Distribution of private equity

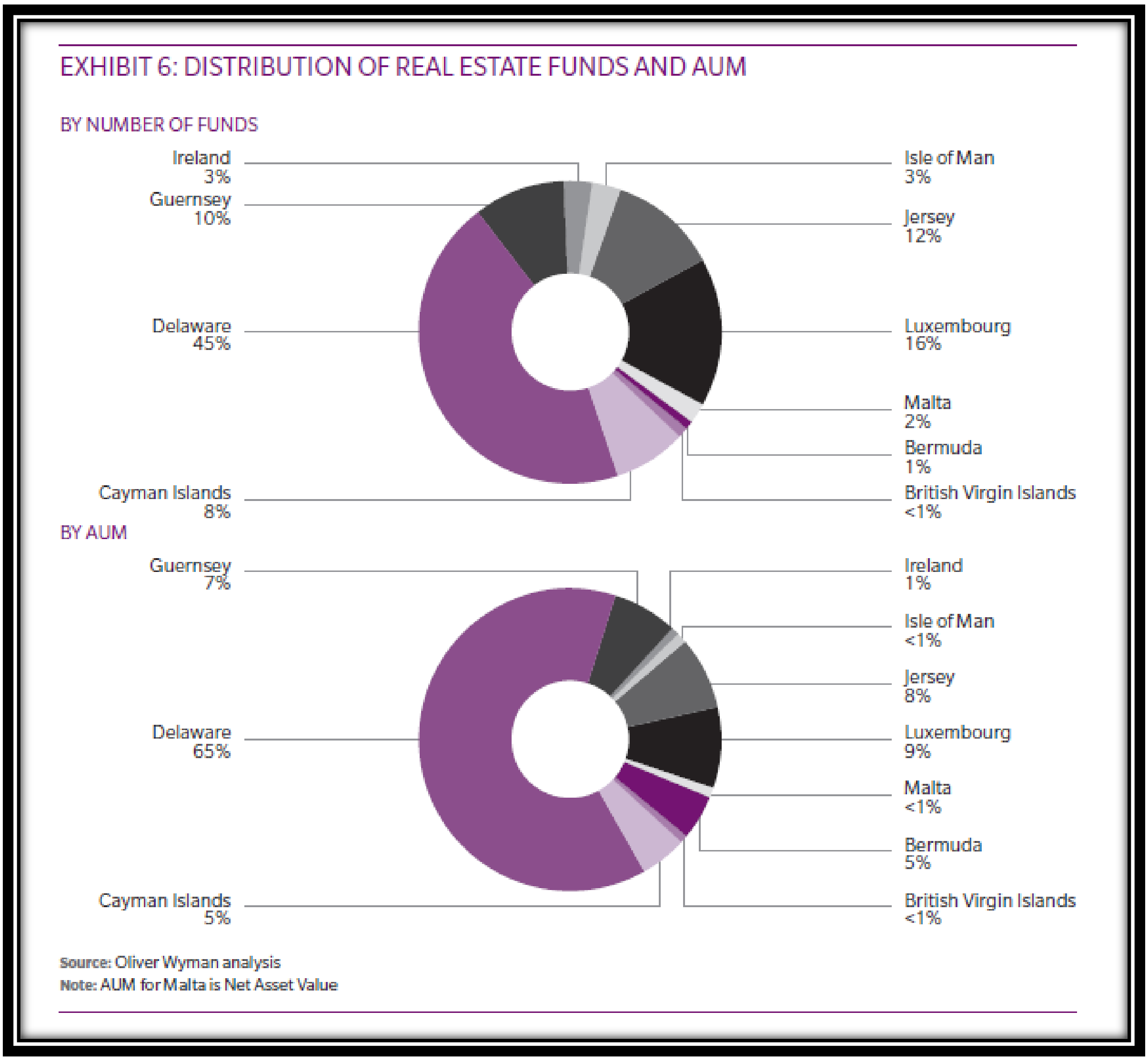


Source: ALFI 2011, p. 4.



Source: APEX 2011, p. 4.

10.8. <u>Appendix H: Distribution of real estate funds</u>



Source: ALFI 2011, p. 5.

10.9. *Appendix I: Key factors for asset managers in their choice for a EU fund domicile*

Which of the following are the most important legal and regulatory factors when choosing a European domicile for your range of funds? Please rank-order the top three.

Ranking	Legal and regulatory factors	Total score	% of number one votes
1	Approach to the AIFMD	214	21.5
2	The sophistication of the national regulator	213	24
3	Approach to the UCITS Directive	192	19
4	The ease of re-domiciling funds	180	11.5
5	Accessibility and responsiveness of the national regulator	134	10
6	The legal system and legal certainty	107	3.5
7	Range of fund vehicles	81	6.5
8	Presence of a stock exchange	75	4

Source: The Economist Intelligence Unit.

Which of the following are the most important financial and business factors when choosing a European domicile for your range of funds? Please rank-order the top three.

Ranking	Financial and business factors	Total score	% of number one votes
1	Cost of doing business	418	52
2	Tax treatment of fund vehicles	235	11
3	Double tax treaties	207	8
4	Professional services cluster	146	11.5
5	Local expertise	102	9.5
6	Having existing fund ranges/business relationships	88	8

Source: The Economist Intelligence Unit.

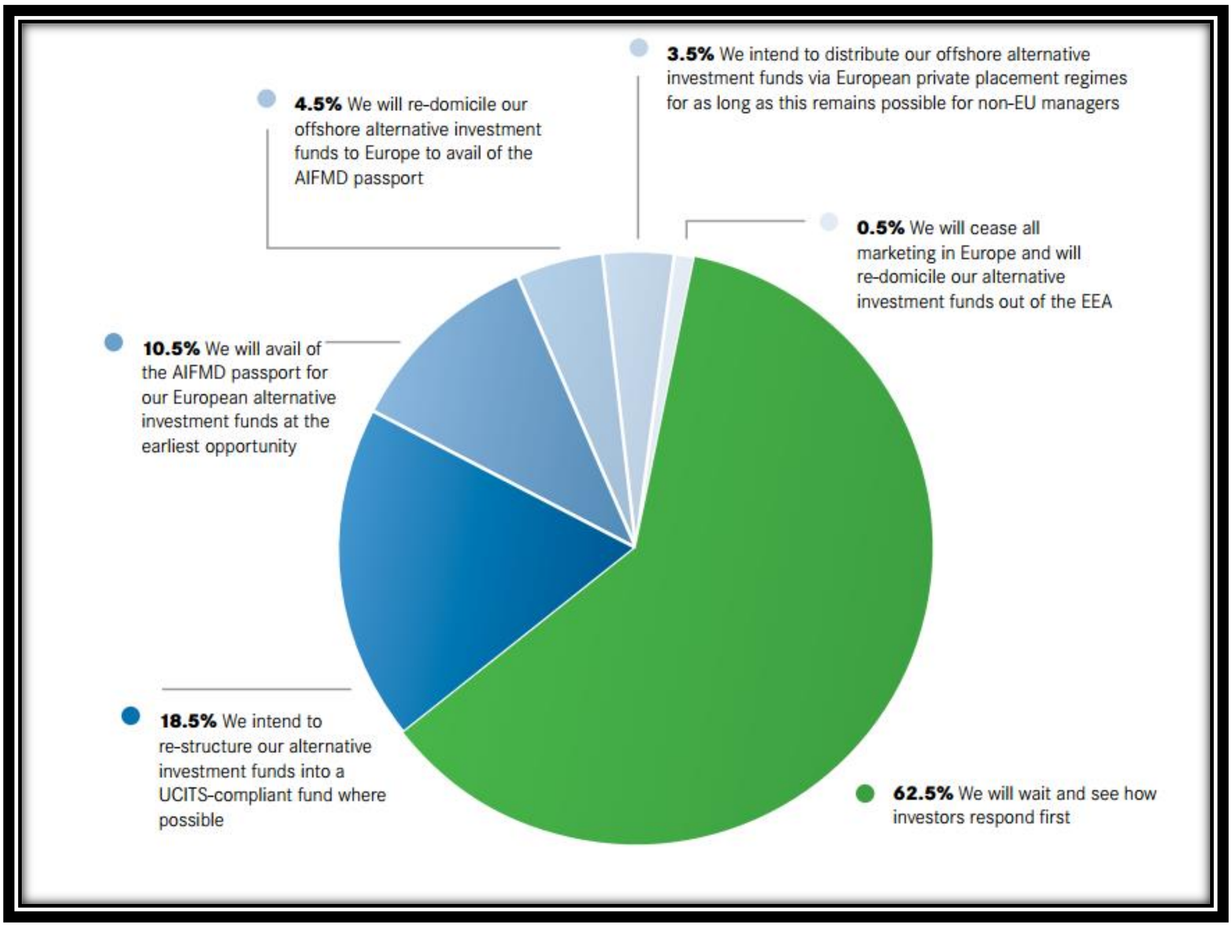
Which of the following are the most important market and distribution factors when choosing a European domicile for your range of funds? Please rank-order the top three.

Ranking	Market and distribution factors	Total score	% of number one votes
1	Speed to market	228	25.5
2	Investors' perceptions	216	20
3	Reputation and longevity as a funds centre	192	11.5
4	Service culture	171	7.5
5	Pro-business Government	149	10.5
6	Access to a large domestic (national) market	139	15.5
7	Status as a global distribution hub	101	9.5

Source: The Economist Intelligence Unit.

Source: Matheson 2013, p. 14.

10.10. *Appendix J: How asset managers expect to react on the implementation of the AIFMD*



Source: Matheson 2013, p. 32.

10.11. *Appendix K: Number of UCITS and non-UCITS funds in the EU*

	End december 2011						End december 2012						End december 2013					
	UCITS Market			Non-UCITS Market			UCITS Market			Non-UCITS Market			UCITS Market			Non-UCITS Market		
	Number of funds	Net assets in mio euro	Average net asset per fund in mio EUR	Number of funds	Net assets in mio EUR	Average net asset per fund in mio EUR	Number of funds	Net assets in mio EUR	Average net asset per fund in mio EUR	Number of funds	Net assets in mio EUR	Average net asset per fund in mio EUR	Number of funds	Net assets in mio EUR	Average net asset per fund in mio EUR	Number of funds	Net assets in mio EUR	Average net asset per fund in mio EUR
Austria	1,371	74,329	54.22	796	63,157	79.34	1,349	79,585	59.00	819	68,233	83.31	1,300	78,053	60.04	861	71,354	82.87
Belgium	1,866	78,643	42.15	32	6,028	188.38	1,673	80,339	48.02	31	6,958	224.45	1,583	86,874	54.88	33	8,145	246.82
Bulgaria	93	226	2.43	1	2	2.00	96	247	2.57	1	2	2.00	99	367	3.71	1	2	2.00
C.R.	113	4,119	36.45	3	78	26.00	109	4,498	41.27	3	92	30.67	114	4,596	40.32	3	124	41.33
Denmark	509	65,856	129.38	340	73,151	215.15	503	78,653	156.37	356	85,782	240.96	520	86,317	165.99	352	99,337	282.21
Finland	368	48,066	130.61	129	7,321	56.75	375	56,075	149.53	132	10,260	77.73	369	64,145	173.83	123	10,978	89.25
France	7,744	1,068,141	137.93	4,086	312,812	76.56	7,392	1,116,481	151.04	4,300	389,250	90.52	7,154	1,110,507	155.23	4,238	414,600	97.83
Germany	2,051	226,456	110.41	3,826	907,418	237.17	2,059	248,325	120.60	3,869	1,037,202	268.08	2,012	277,700	138.02	3,940	1,126,654	285.95
Greece	225	4,417	19.63	6	1,887	314.50	206	4,927	23.92	6	1,776	296.00	192	5,256	27.38	6	1,803	300.50
Hungary	231	6,337	27.43	121	2,700	22.31	245	7,394	30.18	278	4,281	15.40	255	10,262	40.24	289	5,284	18.28
Ireland	3,085	820,041	265.82	1,984	235,227	118.56	3,167	967,562	305.51	2,138	259,864	121.55	3,345	1,044,063	312.13	2,254	299,819	133.02
Italy	659	139,697	211.98	347	53,598	154.46	600	137,729	229.55	340	52,763	155.19	661	156,300	236.46	355	52,792	148.71
Liechtenstein	476	25,467	53.50	252	4,512	17.90	557	24,316	43.66	270	3,397	12.58	697	26,510	38.03	311	4,602	14.80
Luxembourg	9,462	1,760,155	186.02	3,832	336,357	87.78	9,435	2,002,398	212.23	3,985	381,428	95.72	9,500	2,197,567	231.32	4,185	417,796	99.83
Malta	59	1,648	27.93	473	6,517	13.78	54	2,299	42.57	510	7,421	14.55	70	2,293	32.76	530	7,118	13.43
Netherlands	495	53,448	107.98	132	11,067	83.84	497	57,712	116.12	108	10,865	100.60	501	61,855	123.46	113	10,617	93.96
Norway	507	61,828	121.95	0	0		404	74,836	185.24	0	0		573	79,273	138.35	0	0	
Poland	240	14,414	60.06	336	10,912	32.48	279	19,816	71.03	425	15,979	37.60	285	20,318	71.29	418	25,174	60.22
Portugal	190	6,018	31.67	370	16,085	43.47	174	6,001	34.49	353	17,739	50.25	169	7,406	43.82	329	17,284	52.53
Romania	106	1,846	17.42	25	1,536	61.44	63	1,983	31.48	26	1,450	55.77	64	2,905	45.39	31	1,604	51.74
Slovakia	73	2,656	36.38	8	545	68.13	65	2,392	36.80	15	1,358	90.53	64	2,681	41.89	19	1,890	99.47
Slovenia	140	1,790	12.79	0	0		134	1,828	13.64	0	0		116	1,850	15.95	0	0	
Spain	2,474	150,877	60.99	62	5,535	89.27	2,349	144,978	61.72	56	5,388	96.21	2,267	179,997	79.40	53	4,881	92.09
Sweden	553	147,042	265.90	23	3,392	147.48	527	168,300	319.35	19	4,171	219.53	543	198,117	364.86	9	2,135	237.22
Switzerland	664	211,037	317.83	200	61,504	307.52	667	235,476	353.04	186	61,794	332.23	765	287,927	376.38	185	68,904	372.45
Turkey	342	10,866	31.77	53	8,202	154.75	356	12,495	35.10	47	10,168	216.34	378	10,217	27.03	49	11,310	230.82
U.K.	2,079	648,406	311.88	782	156,704	200.39	2,037	758,663	372.44	822	210,973	256.66	2,022	862,506	426.56	837	258,255	308.55
Europe	**36,175**	**5,633,825**	**155.74**	**18,219**	**2,286,249**	**125.49**	**35,372**	**6,295,307**	**177.97**	**19,095**	**2,648,593**	**138.71**	**35,618**	**6,865,860**	**192.76**	**19,524**	**2,922,460**	**149.69**

Source: EFAMA.

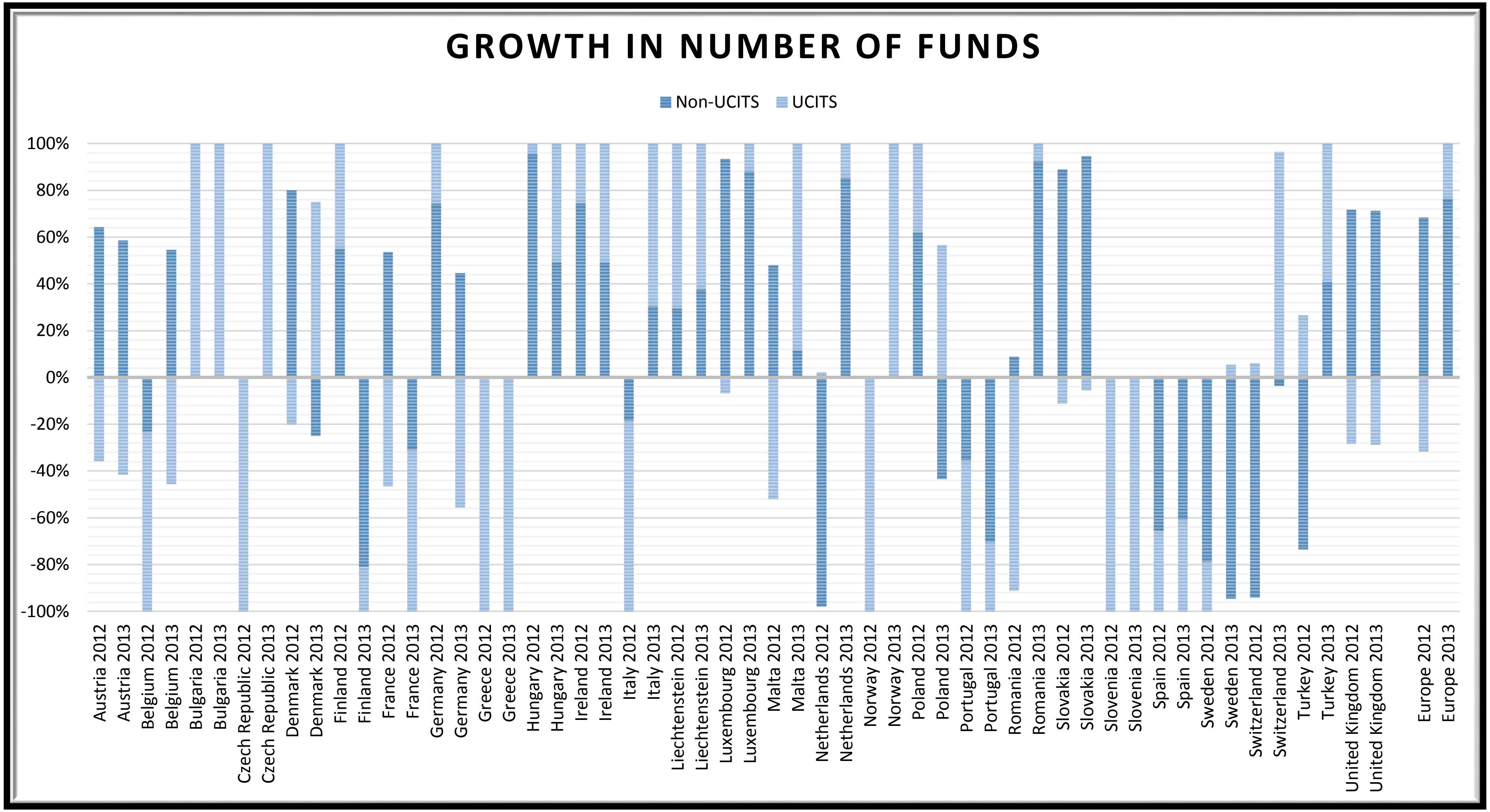
10.12. *Appendix L: Growth in 2012 and 2013 of funds in the EU*

	Growth number in 2012 (as to 2011)						Growth number in 2013 (as to 2012)					
	UCITS Market			Non-UCITS Market			UCITS Market			Non-UCITS Market		
	Number of funds	Net assets	Average net asset per fund	Number of funds	Net assets	Average net asset per fund	Number of funds	Net assets	Average net asset per fund	Number of funds	Net assets	Average net asset per fund
Austria	-1.60%	7.07%	8.82%	2.89%	8.04%	5.00%	-3.63%	-1.92%	1.77%	5.13%	4.57%	-0.53%
Belgium	-10.34%	2.16%	13.94%	-3.13%	15.43%	19.15%	-5.38%	8.13%	14.28%	6.45%	17.06%	9.96%
Bulgaria	3.23%	9.29%	5.88%	0.00%	0.00%	0.00%	3.13%	48.58%	44.08%	0.00%	0.00%	0.00%
C.R.	-3.54%	9.20%	13.21%	0.00%	17.95%	17.95%	4.59%	2.18%	-2.30%	0.00%	34.78%	34.78%
Denmark	-1.18%	19.43%	20.86%	4.71%	17.27%	12.00%	3.38%	9.74%	6.16%	-1.12%	15.80%	17.12%
Finland	1.90%	16.66%	14.48%	2.33%	40.14%	36.96%	-1.60%	14.39%	16.25%	-6.82%	7.00%	14.83%
France	-4.55%	4.53%	9.50%	5.24%	24.44%	18.24%	-3.22%	-0.54%	2.77%	-1.44%	6.51%	8.07%
Germany	0.39%	9.66%	9.23%	1.12%	14.30%	13.03%	-2.28%	11.83%	14.44%	1.84%	8.62%	6.67%
Greece	-8.44%	11.55%	21.83%	0.00%	-5.88%	-5.88%	-6.80%	6.68%	14.46%	0.00%	1.52%	1.52%
Hungary	6.06%	16.68%	10.01%	129.75%	58.56%	-30.99%	4.08%	38.79%	33.35%	3.96%	23.43%	18.73%
Ireland	2.66%	17.99%	14.93%	7.76%	10.47%	2.52%	5.62%	7.91%	2.16%	5.43%	15.38%	9.44%
Italy	-8.95%	-1.41%	8.29%	-2.02%	-1.56%	0.47%	10.17%	13.48%	3.01%	4.41%	0.05%	-4.17%
Liechtenstein	17.02%	-4.52%	-18.40%	7.14%	-24.71%	-29.73%	25.13%	9.02%	-12.88%	15.19%	35.47%	17.61%
Luxembourg	-0.29%	13.76%	14.09%	3.99%	13.40%	9.05%	0.69%	9.75%	9.00%	5.02%	9.53%	4.30%
Malta	-8.47%	39.50%	52.42%	7.82%	13.87%	5.61%	29.63%	-0.26%	-23.06%	3.92%	-4.08%	-7.70%
Netherlands	0.40%	7.98%	7.54%	-18.18%	-1.83%	19.99%	0.80%	7.18%	6.32%	4.63%	-2.28%	-6.61%
Norway	-20.32%	21.04%	51.90%				41.83%	5.93%	-25.31%			
Poland	16.25%	37.48%	18.26%	26.49%	46.44%	15.77%	2.15%	2.53%	0.37%	-1.65%	57.54%	60.18%
Portugal	-8.42%	-0.28%	8.89%	-4.59%	10.28%	15.59%	-2.87%	23.41%	27.06%	-6.80%	-2.56%	4.54%
Romania	-40.57%	7.42%	80.74%	4.00%	-5.60%	-9.23%	1.59%	46.50%	44.21%	19.23%	10.62%	-7.22%
Slovakia	-10.96%	-9.94%	1.14%	87.50%	149.17%	32.89%	-1.54%	12.08%	13.83%	26.67%	39.18%	9.88%
Slovenia	-4.29%	2.12%	6.70%				-13.43%	1.20%	16.91%			
Spain	-5.05%	-3.91%	1.20%	-9.68%	-2.66%	7.77%	-3.49%	24.15%	28.65%	-5.36%	-9.41%	-4.28%
Sweden	-4.70%	14.46%	20.10%	-17.39%	22.97%	48.85%	3.04%	17.72%	14.25%	-52.63%	-48.81%	8.06%
Switzerland	0.45%	11.58%	11.08%	-7.00%	0.47%	8.03%	14.69%	22.27%	6.61%	-0.54%	11.51%	12.11%
Turkey	4.09%	14.99%	10.47%	-11.32%	23.97%	39.80%	6.18%	-18.23%	-22.99%	4.26%	11.23%	6.69%
U.K.	-2.02%	17.00%	19.42%	5.12%	34.63%	28.08%	-0.74%	13.69%	14.53%	1.82%	22.41%	20.22%
Europe	-2.22%	11.74%	14.28%	4.81%	15.85%	10.53%	0.70%	9.06%	8.31%	2.25%	10.34%	7.92%

Source: own analysis on data of EFAMA.

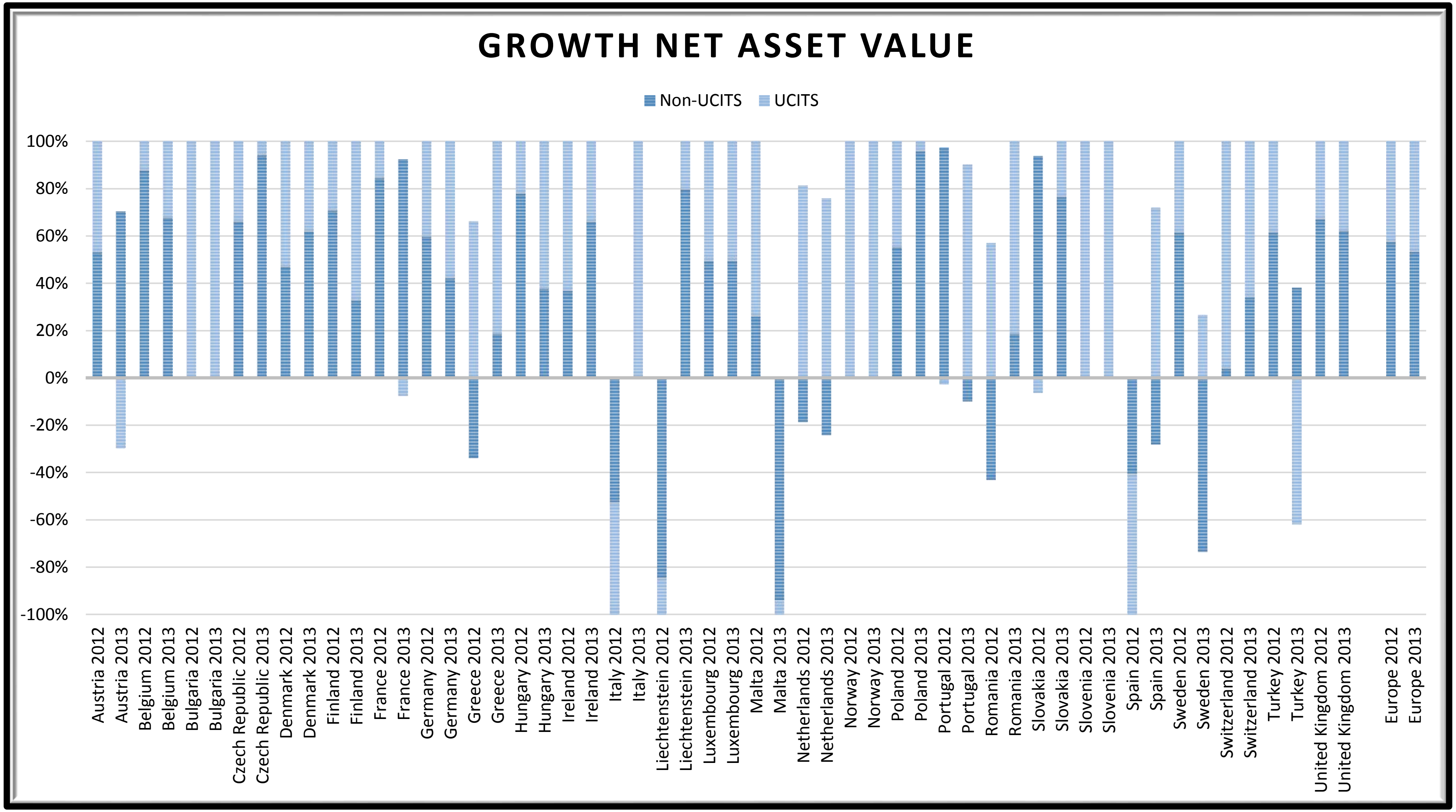
Significant levels of an increase in growth
Levels of an increase in growth
Significant levels of an decrease in growth
Levels of an decrease in growth

10.13. <u>*Appendix M: Growth in number of funds*</u>



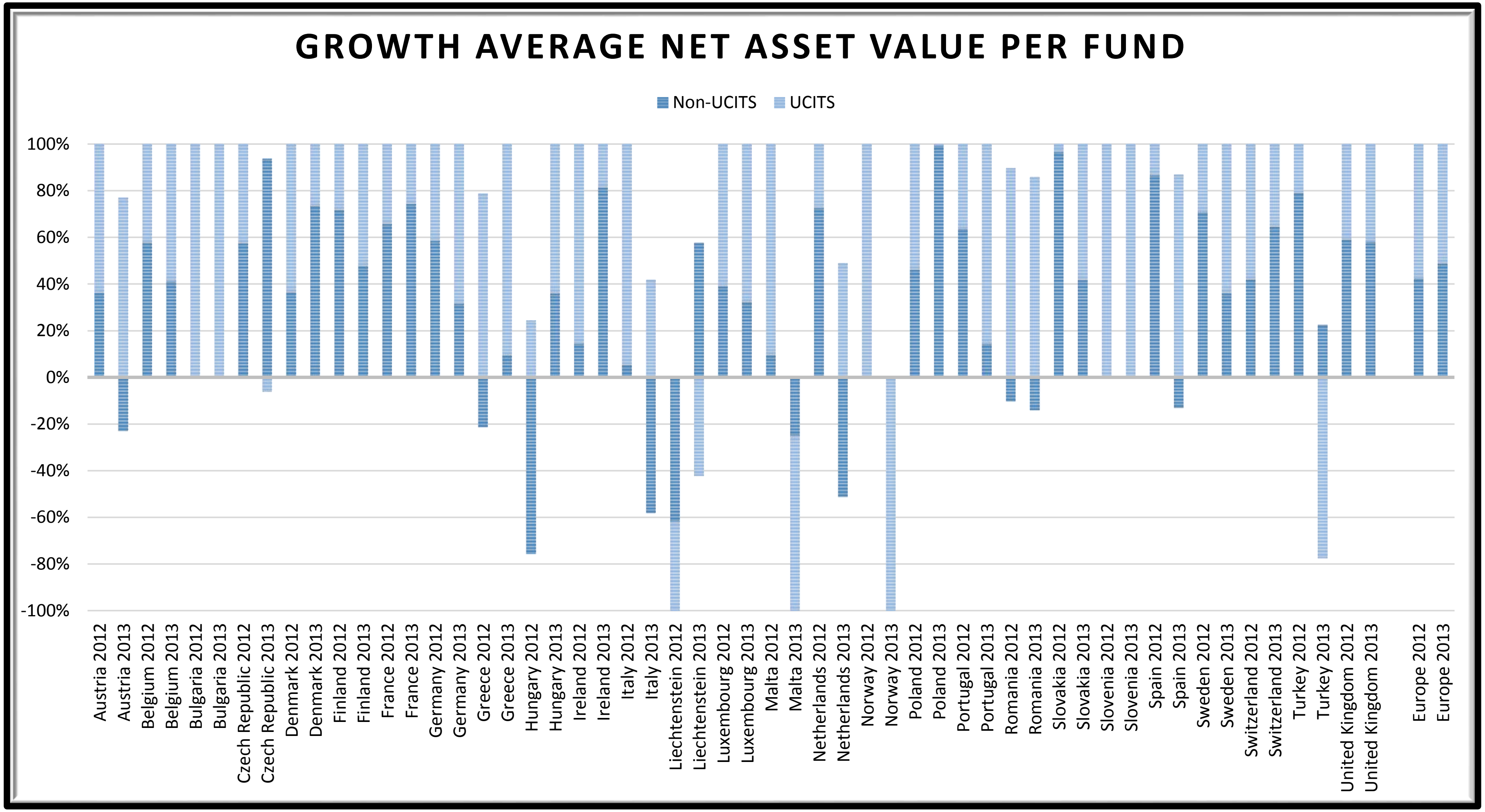
Source: own analysis on data of EFAMA.

10.14. <u>*Appendix N: Growth in net asset value*</u>



Source: own analysis on data of EFAMA.

10.15. <u>*Appendix O: Growth in average net asset value per fund*</u>



Source: own analysis on data of EFAMA.

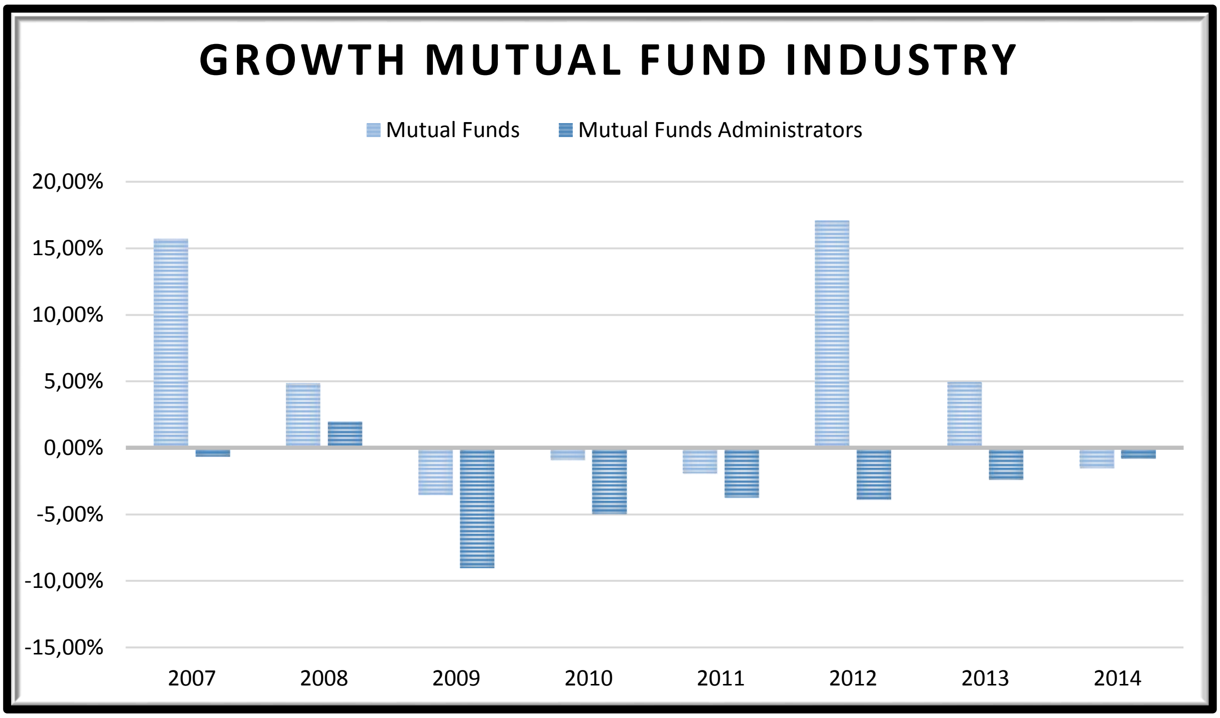
10.16. *Appendix P: Mutual Funds on the Cayman Islands*

	Mutual Funds					Mutual Funds Administrators			
Period	Registered	Master	Administered	Licensed	**Total**	Full	Restricted	Exempted	**Total**
2006 - Q4	7,481	0	548	105	**8,134**	91	57	5	**153**
2007 - Q4	8,751	0	543	119	**9,413**	95	52	5	**152**
2008 - Q4	9,231	0	510	129	**9,870**	102	49	4	**155**
2009 - Q4	8,944	0	448	131	**9,523**	97	42	2	**141**
2010 - Q4	8,870	0	435	133	**9,438**	94	38	2	**134**
2011 - Q4	8,714	0	424	120	**9,258**	92	35	2	**129**
2012 - Q4	8,421	1,891	408	121	**10,841**	90	32	2	**124**
2013 - Q4	8,235	2,635	398	111	**11,379**	88	31	2	**121**
2014 - Q1	8,064	2,637	394	110	**11,205**	88	30	2	**120**

Source: Cayman Islands Monetary Authority.

	Growth	
	Mutual Funds	Mutual Funds Administrators
2007	15.72%	-0.65%
2008	4.85%	1.97%
2009	-3.52%	-9.03%
2010	-0.89%	-4.96%
2011	-1.91%	-3.73%
2012	17.10%	-3.88%
2013	4.96%	-2.42%
2014	-1.53%	-0.83%

Significant levels of an increase in growth
Levels of an increase in growth
Significant levels of an decrease in growth
Levels of an decrease in growth



Source: own analysis on data of Cayman Islands Monetary Authority.