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Watered down AIFMD is lesson to protectionist Eurocrats

Added 27 April 2011 by Geoff Cook, Chief Executive, Jersey Finance

In early April we held our Jersey Funds Conference in London where, as usual, we discussed and debated the various issues and opportunities currently affecting the market generally, and Jersey specifically.

The Alternative Investment Fund Managers Directive (AIFMD) was on the agenda, (as it has been for some time,) although thankfully in a much less dramatic way than in previous years.

The rocky progression of the AIFMD has finally led us to a situation where we believe we can move forward as a funds industry. For those based within and without the EU, Jersey's Private Placement regime will continue to facilitate business and for those requiring AIFMD compliant access to EU markets, we plan to achieve the criteria to participate in the passporting scheme by 2013, well ahead of the expected launch of the passport.

In the early period of the Directive it was not easy to see clearly the way forward for any of the stakeholders. Our preferred strategy in terms of international relations has been to engage constructively and we did this to good effect with the European Parliament and the EU Commission.

Ultimately, it was the US response and the big pension players pointing out the full extent of the potential damage that made the EU reconsider the directive; which would have impeded international capital and made Europe a less attractive destination for investment.

Geoff Cook
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However, in extremis, advice received indicates had we been disadvantaged in a discriminatory manner there were a number of quite powerful options available to us. The EU Competition Directive and the Internal Market Directive could both have provided support for jurisdictions such as Jersey and much more powerful countries such as the United States.

Now that things are more positive and certain, I have been reflecting on how we got into a situation where something like AIFMD could be proposed in the first place.

The US, EU and Developing market trading blocs are constantly shifting and changing, and when dramatic events occur, such as the global credit crisis, they do not always fit neatly together.

The EU saw the crisis as an Anglo Saxon induced event, and reacted accordingly, by introducing new regulation in an attempt to exert significant control on shaping and managing events within its geography. The EU's instinct was to build a regulatory wall around Europe, and one of the outcomes was the proposed AIFMD, complete with three year exclusion zone.

In response, the US became engaged, realising that this sort of measure would damage

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world trade. The US Treasury Secretary, Timothy Geithner, wrote to the EU, warning it that:

"...proposals for more restrictive regulation of alternative fund managers could affect cross-border investment, demonstrating how the controversial European Union directive could have transatlantic ramifications."

Ultimately, it was this US response and the big pension players pointing out the full extent of the potential damage that made the EU reconsider the directive; which would have impeded international capital and made Europe a less attractive destination for investment.

Meanwhile, developing countries have continued to beaver away furiously trying to create and distribute wealth fast enough to satisfy the aspirations of hundreds of millions of people, while curbing inflation and economic overheating. Their immediate priority is to build infrastructure, and they are hungry for foreign capital.

This global appetite for capital has certainly intensified, given that many banking institutions are still trying to unwind the excesses of the financial crisis. The moral of this particular tale is that if the EU does things to make itself less attractive to international capital, then investors will simply invest elsewhere.

In the end the economic arguments won through, but the unintended consequences of the AIFMD directive in its original form would have hurt everyone.

Reason enough now to focus on level two measures with a view to developing appropriate and effective rules while encouraging enhanced market access through passporting, a move which is likely to bring more investment, more trade and more jobs.

The credit crisis, unlike the Great Depression, has seen better policy responses with co-ordinated action by central banks and governments. An unwillingness, though, to grasp the austerity nettle in the post crisis aftermath, coupled with regulation threaded with protectionist tendencies continues to pose real risks to a sustained recovery.

The consensus forged in the heat of the crisis is abating and a strong recovery could be impeded if political leaders give in to the temptation to try to tax out of existence banks, offshore companies, property holders or indeed any party that looks like it might have a bit of cash and doesn't have significant influence at the ballot box.

The easy option would in fact be the most damaging to economic recovery, where structural deficits driven by excessive government borrowing and unrealistic welfare provision, are simply spirited away on the 'someone else can pay' platform. A strategy which would surely consign several generations to a debt burden of Atlas proportions.

That said, the IMF will likely be asked to sort the Sovereign debt issues of Southern Europe and Ireland, and given a pretty decent track record in debt restructuring, it is likely to be significantly more effective than the Europeans themselves.

The G20 looks tricky, with currency 'imbalances' or 'flows'- depending on whether you take an Atlantic or Asian view, continuing to be rather testy subject matter. With Sarkozy, Merkel, Zapatero and Berlusconi all in some difficulty at home, it seems unlikely that a European led G20 will make much impression on the economic superpowers of the US, China and India, who are more focused on their own challenges than the machinations of the Eurozone. Mon Sarkozy's grand Bretton Woods II doesn't seem all that likely to fly given the divergence of

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views amongst the major players.

What of the future then for Jersey and its funds industry? A curious outcome of the crisis has been for Jersey to become more engaged, a la Brussels office, the appointment of a Minister for Internal relations and a realisation that leading global standards on transparency, regulation and governance has put Jersey in a very safe place.

A place from which it can compete fairly based on classical features common to all successful economies; expertise, access, and competitiveness. While undoubtedly there is still a lot of work to do, Jersey is in good shape. With a stable tax system and a top rate of 20%, high quality but affordable office space, (sub £30 per square foot), outstanding education, health, and premium housing opportunities, coupled with one of the most beautiful natural environments anywhere in the world, we believe we have an unbeatable offer for booking and locating funds business, and businesses.

The global economy and Jersey's Finance industry are both growing again, and while we may encounter some headwinds, in Jersey at least, we have learnt how to adjust our sails and to navigate successfully through troubled waters.

We face the future with renewed optimism and confidence.

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