**10 May 2013**

Investment Funds Team
Policy, Risk and Research Division
Financial Conduct Authority
25 The North Colonnade
Canary Wharf
London E14 5HS

**By email: cp13_09@fsa.gov.uk**

Dear Sirs,

***Re: BVCA Regulatory Committee response to the FSA Consultation Paper on the Implementation of the Alternative Investment Fund Managers Directive: Part 2 (CP 13/9)***

This response to the FSA's Consultation Paper on the Implementation of the Alternative Investment Fund Managers Directive: Part 2 (CP 13/9) (the "**Consultation Paper**") is made by the Regulatory Committee of the British Private Equity and Venture Capital Association (the "**BVCA**").

The BVCA is the industry body for the UK private equity and venture capital ("**PE/VC**") industry. With a membership of over 500 firms, the BVCA represents the vast majority of all UK-based PE/VC firms and their advisers. Its members have invested £40 billion in over 5,000 UK companies over the last five years. Companies backed by UK-based PE/VC firms employ over half a million people and 90 per. cent of UK investments in 2011 were directed at small and medium-sized businesses.

In our response, our points are generally made in reference to private equity but could equally apply to other investment strategies incorporated by BVCA members, notably venture capital and real estate investment. In order to focus our response appropriately, we have considered only those parts of the Consultation Paper which we think raise issues relevant to PE/VC firms. Given that a number of our comments and concerns are not linked to particular questions posed by the Consultation Paper ("**Consultation Questions**"), but are instead of a more general nature, we have structured our response such that a series of general comments precedes our answers to the Consultation Questions.

We appreciate the very difficult task facing the FCA, and HM Treasury (together, the "**UK Authorities**"), as regards the implementation of the Alternative Investment Fund Managers Directive (the "**Directive**") and welcome the opportunity to respond to the Consultation Paper. We stand ready to provide whatever further contribution to this work the FCA would find

helpful. In particular, we would be delighted to attend a meeting with the FCA to discuss the issues raised in our response.

Yours faithfully,

Margaret Chamberlain
Chair - BVCA Regulatory Committee

**FSA CONSULTATION PAPER – IMPLEMENTATION OF THE ALTERNATIVE INVESTMENT FUND MANAGERS DIRECTIVE: PART 2 (CP 13/9)**

## PART A: GENERAL COMMENTS AND CONCERNS

Key concerns

1. We are particularly concerned about the combined effect of: (i) the lack of guidance on the application of the restrictions in Article 6(4) of the Directive; (ii) the draft guidance on carry and co-invest schemes (which we welcome); and (iii) the interpretation suggested in the draft PERG guidance of the MiFID exemption for managers of collective investment undertakings ("**CIUs**") (with which we disagree). As we have indicated in previous submissions, we believe that the operation of carry and co-invest schemes is an AIFM activity within Annex 1, paragraph 2(c), to the Directive. Any other view, if combined with the proposed FCA guidance and interpretation of the MiFID exemption, would bring about unexpected and significant changes for PE firms, being costly in both regulatory and capital terms, at a very late stage. We believe that we have suggested in this and previous submissions a justifiable and appropriate approach to this issue. We would appreciate, at the very least, an opportunity to at least exchange views with the FCA, even if no further guidance on Article 6(4) is published.

2. We would also highlight our concerns about the proposed timing for reports; the current proposals are, for many funds, impracticable and unnecessarily costly. The reporting cycle should, as now, respect the periods within which the annual accounts are drawn up.

Applications for authorisation from prospective UK AIFMs and depositaries

3. We remain deeply concerned about the lack of certainty as regards the time at which the FCA intends to accept applications for authorisation from prospective UK AIFMs and depositaries. As explained in detail in our response to the FSA's first Consultation Paper on the Directive (the "**First Consultation Paper**"), we consider that it is vital that the FCA is in a position to accept and approve applications for authorisation from prospective UK AIFMs prior to 22 July 2013 such that those firms are authorised, and have the benefit of the marketing passport, with effect from 22 July 2013.

4. Similarly, it is important that the FCA is in a position to accept and approve applications for authorisation from prospective UK depositaries prior to 22 July 2013 given that an AIFM is under an obligation to ensure that, for each AIF it manages, a depositary is appointed (although we understand from the Treasury Q&A on the Directive (dated 29 April 2013) (the "**Treasury Q&A**") that, "*an additional transitional provision enabling depositaries to act for AIFs during the transitional period prior to obtaining the new*

*Part 4A permission*" is proposed). In any event, the BVCA's members need certainty about the Directive's requirements as they relate to PE AIF depositaries, some of whom may not yet have any form of FCA authorisation. It would be very helpful if the FCA could give the BVCA some indication as to timing – both in terms of when it intends to start accepting applications for authorisation from potential depositaries and when it intends to publish any further details on the requirements, particularly as they relate to PE AIF depositaries.

5. Whilst we understand that the FCA is having discussions with both prospective AIFMs and depositaries about the authorisation process, given that the Directive takes effect in just over ten weeks, it is imperative that information on the authorisation process is made publicly available as soon as possible and that the FCA begins to accept applications for authorisation, at least from prospective AIFMs, in the next couple of weeks (at the latest). We think it would be helpful if this could be one of the topics discussed at the UK Authorities' 'town hall event' on implementation of the Directive on 17 May 2013.

Scope of Article 6 (*Conditions for taking up activities as AIFM*) of the Directive

6. We also remain deeply concerned about how the limitations on the activities of an external AIFM (which are set out in Articles 6(2) and (4) of the Directive) are to be interpreted. Our detailed concerns about the scope of the limitations are set out in our response to the First Consultation Paper but we are concerned to note that: (i) the provisions of Articles 6(2) and (4) of the Directive have simply been copied out in draft FUND 1.4.3R; and (ii) no guidance on the limitations has been produced by the UK Authorities. We note that the FCA has sent an email to some firms asking them to indicate if they will be applying for a VoP or a new authorisation. We do not think that firms can be sure about what they will need without some guidance on the issues we have raised. Guidance in this area is urgently required and we repeat below our concerns raised previously.

7. The industry needs to understand as a matter of great urgency how the UK Authorities view the limitations set out in the Directive. Are they to be interpreted as restrictions on only the MiFID activities that an AIFM may perform, which we think is a likely interpretation given the fact that the limitation stems from a Directive, or are these limitations to be interpreted more widely so that if a Member State, under its domestic law, regulates an activity, an AIFM may not also perform it unless it is part of collective portfolio management as defined in Annex 1 to the Directive? This issue is particularly acute in relation to the operation of an unregulated collective investment scheme ("**UCIS**") (an entirely UK concept). A key issue for PE/VC firms is whether the limitations will prohibit an AIFM from managing a co-investment scheme (where such co-investment scheme is a collective investment scheme but not an AIF). We would

expect the majority of UK AIFMs to need authorisation for both managing AIFs and operating UCIS. If two authorised firms are required, this would be very serious and disruptive. We do not, however, see this as a necessary result. We suggest that either (a) the Directive restrictions are to be interpreted as we suggest and/or (b) these schemes are clearly related to the management of the AIF and within Annex 1 to the Directive. Any authorisation could be subject to limitations to make this clear. As other Member States do not currently regulate "operating unregulated schemes" the issue will not arise elsewhere and we expect their firms will naturally continue to manage co-investment schemes without the issue arising as it does in the UK.

8. We therefore believe that any approach which requires a separate authorised firm would put UK firms at a disadvantage to their counterparts in other EU jurisdictions. It was open to the UK Authorities, when implementing the Directive, to remove the existing UK regulatory regime for UCIS and replace it with the Directive regime. Instead of taking this approach, the UK has decided to retain the current regime and apply the Directive regime as an additional layer of regulation. It is only because of this policy that this issue arises in such a form. We therefore think it is vital that the FCA clarifies its approach soon to this very important issue.

9. A further issue on the limitations relates to the additional MiFID services which may be provided. It appears that even if a firm only wants to provide the additional non-core service of investment advice, it must also be authorised to provide discretionary asset management (Article 6(5)(b) of the Directive). It would be helpful if the FCA could indicate what the position will be if a firm does not wish to actually provide a discretionary asset management service – will the FCA be prepared to grant authorisation for both activities? We would also like to seek clarity in respect of the following questions:

- Can a UK authorised AIFM provide marketing services to a non-EU AIF which is managed by a sister/affiliate entity that is not an authorised AIFM?

- Can a UK authorised AIFM advise or manage discretionary accounts cross-border throughout the EEA under a MiFID passport?

- Can a UK authorised AIFM take on non-discretionary management mandates (i.e.to advise and arrange transactions)?

<u>Draft PERG Question 2.59: Does this interpretation of a CIU apply to MiFID?</u>

10. We are extremely concerned about the guidance at Question 2.59. We are concerned that the guidance is not only extremely unhelpful but also wrong as a matter of law. The

guidance suggests that the MiFID definition of "CIU" should, following the implementation of the Directive, be read as importing concepts from the Directive, thereby eliding the concept of a CIU with the concept of an AIF. This is extremely concerning given that it fundamentally changes the MiFID perimeter.

11. MiFID regulates the provision of investment services but contains a number of exemptions including, at Article 2(1)(h), an exemption for CIUs and their managers and depositaries (and Recital 15 of MiFID provides that MiFID does not apply to CIUs and their managers and depositaries, whether co-ordinated at Community level or not [our emphasis], as they are subject to specific rules directly adapted to their activities). On this basis, a UK domestic operator of a s. 235 scheme is not, at present, subject to MiFID because of this exemption. If the FCA were correct in suggesting that a CIU is only a CIU if it is a UCITs or an AIF within the meaning of the Directive, this would mean that those entities which, as at 21 July 2013 are operating a CIS, would, unless the CIS in question were an AIF, no longer be able to avail themselves of the exemption in Article 2(1)(h) of MiFID as of 22 July 2013 and would require authorisation to carry on the MiFID activity of managing investments (and would also become subject to CRD capital requirements). This would have a huge and negative impact on UK firms and is not, in our view, the correct analysis.

12. MiFID and the Directive use different language – the MiFID wording is not replicated in the Directive and it is, we think, wrong as a matter of law for the FCA to state that the two concepts are the same. An entity could be a CIU (or, in the UK, a CIS) without being an AIF either because it does not exhibit one or more of the fundamental characteristics of an AIF (e.g. it does not have a defined investment policy) or because it falls within one of the exemptions described in PERG (e.g. a staff participation scheme). The Directive applies to a specific form of CIU, namely one that raises capital and invests in accordance with a defined investment policy. These are not necessary characteristics of a CIU itself within the meaning of MiFID. We think it is vital that the guidance at Question 2.59 is deleted or at least amended.

Chapter 4 of the Consultation Paper (*Prudential requirements*) – liquid assets requirement

13. Whilst we appreciate that the FSA consulted, in the First Consultation Paper, on the liquid assets requirement as it applies to full-scope UK AIFMs, we have one further point we would like to make in this area.

14. PE arrangements often provide that if, in certain circumstances, the manager is removed from its role by the limited partners, the manager will be entitled to a compensation payment. This provision is normally relevant where the manager may be removed for 'no fault'. The provision will be a contractual term of the limited partnership agreement.

If these circumstances apply, the manager will be entitled to receive from the partnership, as a compensation payment and with no set-off or reduction, an amount calculated by reference to the annual management fee (or priority profit share) that is payable to the manager. The normal approach is that the manager will be entitled to between one to two times the management fee (or priority profit share) that was paid to the manager in the previous financial year.

15. We consider that the amount of such compensation payment can go towards satisfying the liquid assets requirement under the Directive and would encourage the FCA to confirm that this is the correct position. We understand that the policy intent underpinning the capital requirements, and particularly the liquid assets requirement, is to allow arrangements to be unwound. In other words, a manager's liquid assets only really become relevant in precisely the circumstances in which the manager would become entitled to the compensation payment. The manager's entitlement to the payment is certain and it should, therefore, be able to count such amount towards satisfying the liquid assets requirement.

Cash monitoring responsibilities of depositaries under Article 21(7) of the Directive

16. We note that, at paragraph 6.15 of the Consultation Paper, the FCA states that it intends to discuss the cash monitoring responsibilities of depositaries under Article 21(7) of the Directive with relevant stakeholders to try to clarify its interpretation. We have a number of concerns about the way in which Article 21(7) of the Directive is interpreted and would very much like to be involved in these discussions.

## PART B: RESPONSES TO CONSULTATION QUESTIONS

### Q1 Do you have any comments on the proposed PERG guidance?

17. We have a number of comments on the proposed PERG guidance.

PERG 16.2: What types of funds and businesses are caught?

*Question 2.10: You say that an undertaking needs to raise capital to be an AIF. What does capital raising involve?*

18. We have two drafting comments on the guidance at Question 2.10 and one substantive point of note. As regards our drafting comments, we would suggest that: (i) the fifth paragraph of the guidance should provide, "*... although if the AIFM and its group are the sole investors from whom capital is raised, the group exclusion described in PERG 16.6*

*(Exclusions) may be available*"; and (ii) at the end of the penultimate paragraph of the guidance, the following words are inserted: "*from the other types of investor*".

19. Some of our members have heard that there is a view in other parts of Europe that 'raising capital' means that the entity in question must actually have raised capital in the last two years (thus meaning that an entity which has not raised capital in the last two years will not satisfy one of the key elements of the definition of an "AIF" and will, therefore, fall outside the scope of the Directive). In order to ensure that there is a level playing field throughout the EEA, it is important that the FCA's approach to this issue (amongst others) is consistent with that taken by its European counterparts. If different approaches to the interpretation of the key elements of the definition of an "AIF" are taken by different Member States, this will not only lead to a lack of harmonisation throughout the EEA but will also result in significant confusion for market participants. We would urge the FCA to work through ESMA to address this issue.

*Question 2.12: Is a fund that only allows a single investor caught?*

20. We appreciate that the FCA is constrained in this area, to a certain degree, by the approach taken by ESMA in its 'Guidelines on key concepts of the AIFMD' (the "**ESMA Key Concepts Guidelines**"). We do, however, strongly consider that whether a fund is a single investor fund should be a question of fact. Given that ESMA's views in this area are fairly contentious, we think it would be helpful if, in the guidance at Question 2.12, the FCA could acknowledge that: "*If there is in fact only a single investor, there is unlikely to be pooling and therefore there may not be a CIU*".

*Question 2.13: What indicative criteria could be taken into account in determining whether or not an entity has a defined investment policy?*

21. We welcome the guidance set out at Question 2.13 on determining whether or not an entity has a defined investment policy but consider that the penultimate paragraph of the guidance is unnecessarily complicated and confusing and would, ideally, be deleted. Whilst we appreciate that the paragraph is taken from the ESMA Key Concepts Guidelines, we consider that it is wholly unclear and that, whatever the policy merits of some sections of the ESMA guidance, where the ESMA guidance is simply unclear, the FCA could consider not copying it out.

*Question 2.27: Is an investment trust an AIF?*

22. We are concerned that the guidance at Question 2.27 is fundamentally flawed. Investment trust status is simply a tax wrapper – it is incorrect to equate the concept of an "investment trust" with the concept of an "AIF". Some investment trusts will not have

a defined investment policy and would not, therefore, fall within the definition of an "AIF". Others may have a defined investment policy but are complicated entities which the term "investment trust" does nothing to explain. We think that the guidance at Question 2.27 should either be more nuanced or that the Question should be deleted. Indeed, again some of our members have heard that elsewhere in Europe at least one regulator takes the view that investment companies that have the characteristics of UK investment trusts are not AIFs. As noted at paragraph 19 above, it is vital that Member States take a similar approach to such issues to avoid the creation of an unlevel playing field and confusion for market participants.

*Question 2.35: Is a carried interest vehicle caught? / Question 2.36: Is this is the only basis on which a carried interest vehicle can be excluded?*

23. We consider that the guidance at Questions 2.35 and 2.36 should refer not only to employees but also to participants who are family members of employees (as is common), trustees for employees or family members of employees and 'friends' of the AIFM, such as professional service providers to the AIFM. We note that it is already recognised for the purposes of the current CIS promotion rules in COBS 4.12, for example at Category 4, that the scheme participant may not be the employee. Even if a carried interest vehicle is not an "employee participation scheme", it may be that it does not raise capital for the purposes of investment. Participants may make a nominal capital contribution but this should not be regarded as being capital raising for the purposes of investment or for the purposes of giving effect to a defined investment policy.

*Question 2.40: Are individual investment management agreements caught?*

24. We are concerned about the suggestion at the penultimate paragraph of the guidance at Question 2.40 that, if each investment management agreement provides that investments and sales are to be carried out in lock step, this may result in the scheme becoming a CIU. We consider that it is possible for there to be individual but 'synchronised' co-investment arrangements / managed accounts without them becoming pooled. We consider that the determinative criteria should be who is making the investment decision; if decision-making power remains with the institutional shareholders, we do not see how these arrangements could constitute an AIF (even with lock step arrangements governing an exit) because: (i) there is no raising of capital; and (ii) the manager is not investing any capital for the benefit of the investors (the investors are, essentially, investing it themselves).

*Question 2.48: What factors are relevant to whether a joint venture is excluded on the basis that it is managed by its members? / Question 2.55: Does it make a difference if there are co-investors?*

25. We broadly welcome the FCA's guidance on joint ventures but are concerned about the final paragraph of the guidance at Question 2.48 which states that, "... *a private equity acquisition company may still be excluded as a joint venture even if it has management team shareholders who are retail investors. This is because the management team may well have the practical ability to participate in joint decision making*". Whilst members of the management team will usually be shareholders in the acquisition vehicle, we do not consider that they would typically have the ability to, "*participate in joint decision making*" [emphasis added]. We consider that it may be better to treat such vehicles as administrative acquisition vehicles (and, on that basis, not AIFs). We are concerned about the guidance at Question 2.55 for a similar reason – it appears to suggest that acquisition vehicles could be AIFs.

*Question 2.52: Is a co-investment vehicle caught?*

26. We are concerned that the FCA makes reference only to one particular type of co-investment vehicle in the guidance at Question 2.52. The guidance describes an arrangement where, "*an institutional investor confers a substantial mandate on an investment manager and structures the mandate through an investment vehicle (the co-investment vehicle). The other investors are the manager itself and its employees or a vehicle taking a carried interest for the benefit of the employees of the manager*". We agree with the FCA's analysis that this type of co-investment vehicle would not normally be an AIF but would note that this is not the only type of arrangement which can constitute a 'co-investment vehicle'. Another type of co-investment vehicle may exist where the manager/its affiliates and/or investment executives working at the manager/its affiliates invest alongside the main fund. In our view, such a co-investment scheme should also be exempt from the definition of an "AIF".

27. We think it is important that the guidance is expanded to include reference to such other arrangements or at least to acknowledge that there may be other co-investment arrangements which are also not AIFs.

*BVCA suggestion for additional guidance*

28. We think it would be helpful if the FCA could include a new Question in PERG 16.2 which provides guidance to confirm that neither: (i) a limited partnership ("**LP**") in which there is a single limited partner making a substantive contribution and a general partner ("**GP**") making a nominal £1 or £10 contribution; nor (ii) a company with two shareholders, one of which is a wholly owned subsidiary of the other (the subsidiary being, "**X**"), whereby X makes a nominal capital contribution because applicable law

(i.e. overseas law, as opposed to the UK's Companies Act 2006) requires the company to have two members, constitutes an "AIF".

29. There are a number of bases for concluding that such a vehicle does not have the basic characteristics of an AIF. These are as follows: (i) there is no 'capital raising', because the nominal capital contributed by the GP is not meaningful; (ii) there is no 'pooling' of capital, which is an important characteristic of a CIU; and (iii) such nominal capital is not applied to the LP's defined investment policy.

30. Our proposition appears to be supported by the guidance at Question 2.36 which states that if, "*employees only invest a nominal amount of capital … the employees are not investors*". Whilst this guidance refers only to employee investment, we believe that the reasoning is capable of wider application, meaning that a GP which makes a merely nominal contribution is not an 'investor' for the purposes of the Directive. Furthermore, the guidance at Question 2.52, concerning third party co-investment vehicles, notes that they can, in some cases, be treated as having a 'single external investor' despite capital coming from the manager (or, by implication, an affiliate of the manager).

31. We would extend much of our reasoning outlined above to the example given at (ii) in paragraph 28 above.

PERG 16.3: Managing an AIFM

*Question 3.1: What does managing an AIF mean? / Question 3.2: If a person performs only one of the activities listed in the answer to Question 3.1 does it manage an AIF?*

32. We are concerned about the guidance at Questions 3.1 and 3.2. This guidance provides that: (i) a person manages an AIF when that person performs risk management or portfolio management for the AIF [our emphasis]; and (ii) a person manages an AIF even if it performs only one of these activities. Whilst we appreciate that this guidance reflects the current drafting of Regulation 4(1) of the draft AIFM Regulations[1], and that the issue arises because of inherent uncertainty in the Directive, we are concerned that, as currently drafted, this produces the possibility of there being two AIFMs for a single AIF.

33. This could arise in instances where an AIFM carries on the activity of portfolio management but delegates the activity of risk management to a separate entity. In such instances there could, in light of the guidance at Questions 3.1 and 3.2, be two entities

[1] For the avoidance of doubt, where we refer to the "draft AIFM Regulations", we refer to the draft of The Alternative Investment Fund Managers Regulations 2013 as it appears in the Treasury's first Consultation Paper on the Directive (January 2013).

deemed to be the AIFM. This is an issue for two reasons: (i) it is not permitted by the Directive (Article 5(1) of the Directive provides that, "*Member States shall ensure that each AIF managed within the scope of this Directive shall have a single AIFM...*") (further, draft FUND 1.4.1R provides that, "*[a] UK AIFM must ensure that for each AIF it is appointed to manage, it is the only AIFM of that AIF*"); and (ii) the FCA will be able to refuse permission to manage an AIF if the applicant would not be the only AIFM of each AIF it manages (Regulation 5(2)(b) of the draft AIFM Regulations)).

34. We have suggested, in our response to the Treasury's first Consultation Paper on the Directive, that the UK Authorities should avoid taking a literal approach to copy-out and instead provide clarification for firms in this area. We would therefore suggest that the guidance at Question 3.1 is amended to provide that, "*a person manages an AIF when the person performs (1) risk management; or (2) portfolio management for the AIF <u>but is ultimately responsible for both</u>*".

**Q2 Do you agree with the proposed reporting frequency for sub-threshold AIFMs and the proposed reporting period end dates for all AIFMs?**

35. We agree that the proposed reporting frequency for both sub-threshold AIFMs and all other AIFMs should be annually, however we do not agree that the reporting date should be fixed at 31 December. This is because many AIFMs and the AIFs they manage have different reporting dates, with a large percentage reporting on March and June year ends. In order to report at December, these entities would have to either construct an entirely new set of reports incorporating partial results from two different reporting periods or incur the expense of changing the year end dates of numerous entities.

36. Any construction of reports incorporating results from two different reporting periods will involve the AIFM in considerable disruption and expense since it will have to prepare a separate set of reports for the purpose of the Directive in addition to the reports produced for itself and its investors. In addition, since the Directive requires that accounting information given in the annual report is audited, it is likely that the AIFM will also have to incur additional audit costs to review the combined report using numbers from two different periods. As regards the alternative of changing its reporting period, there are likely to be many reasons why an AIFM cannot do so (for example, where it is part of a large group and is required to report to the same date as its parent entity). Even if it were possible to do so, the cost associated with this change and the disruption involved would be considerable.

37. Under the current regulatory regime, AIFMs report at different period end dates and we do not agree that this should be changed to 31 December, nor do we see the benefit of making such a change. On the contrary, such a requirement would involve considerable

disruption and expense for those AIFMs who currently do not report to December and these costs are unlikely to have been reflected in the FCA's cost benefit analysis. We therefore suggest that the reporting date should be set at the AIFM's existing year end reporting date with matching adjustments for quarterly and biannual reporting.

**Q6 Do you agree with our proposed approaches to amending IPRU (INV) and deleting UPRU, as explained above?**

38. We have a number of concerns about the amended Glossary definition of 'funds under management'. In short, we are concerned that the definition should encompass only AuM of in-scope AIF(s) and we consider that the definition should be amended as set out below (our amendments are underlined):

| | |
|---|---|
| ***funds under management*** | (in *IPRU(INV)* and *GENPRU*) *funds*, other than *funds* invested in:<br><br>(a) entities referred to in article 2(3) of *AIFMD*;<br><br>(b) *AIFs* of the types referred to in article 61(3) and article 61(4) of *AIFMD*; and<br><br>(c) non-*AIF collective investment schemes*,<br><br>managed by the *firm*, calculated as the sum of the absolute value of all assets of all such *funds* managed by the *firm*, including assets acquired through the use of leverage, and for such purpose derivative instruments shall be converted into their equivalent positions in the underlying assets of such instruments using the conversion methodologies set out in article 10 of *AIFMD level 2 regulation* and valued on the basis of the value of that equivalent position. This includes such *funds* where the *firm* has delegated the management function but excludes such *funds* that it is managing as a delegate. |

**Q16 Do you have any comments on our proposed marketing guidance in PERG? Are there any other issues related to AIFMD marketing that should be included in the guidance?**

39. We have a number of comments on the proposed marketing guidance.

*Paragraph 8.37.3: The meaning of markets an AIF*

40. We note that the guidance on the meaning of "markets an AIF" is based on the current approach taken by the draft AIFM Regulations, which extends the definition of "marketing" contained in the Directive such that it also includes offerings or placements which are not made at the initiative of, or on behalf of, the AIFM. We assume that the FCA will amend PERG 8.37.3 to reflect any changes made on this point in the final AIFM Regulations.

*Paragraph 8.37.4: The meaning of an offering or placement*

41. We are concerned that the current descriptions of "offering" and "placement" could catch secondary market offerings. We consider that it would be helpful if the FCA could produce clear guidance on whether only primary offerings or placements are intended to be caught or whether all offerings and placements (including those in the secondary markets) are intended to be caught (we strongly favour the former view) (any such guidance will obviously need to reflect the final AIFM Regulations). We are also concerned that the phrase "made available" (used in PERG 8.37.4G(2)) is too wide as it could catch genuine "passive marketing" (on which we have separate comments – see paragraphs 46 to 49 below).

*Paragraph 8.37.5: Communications with investors in relation to draft documentation*

42. Whilst we consider that, in some respects, the FCA's suggested approach to the issue of draft documentation is helpful, it opens up the risk, if this interpretation is adopted by other Member States, that UK PE/VC firms will face barriers to prevent preliminary communications with potential investors. Whilst the UK proposes to ensure that its financial promotion regime permits such communications, there can be no certainty that this will be the case in other Member States. If this is to be the interpretation that is adopted by the FCA then we think it is essential that the FCA works through ESMA to ensure not only that other Member States take the same approach, but that other Member States permit preliminary communications to persons who are within the class of persons to whom an AIF may be marketed. In addition, we are concerned that the proposed approach will lead to significant delays in marketing and would urge the FCA to develop a procedure which enables some preliminary clearance to be obtained so that the final documentation can be swiftly approved.

*Paragraph 8.37.6: The meaning of indirect offering or placement*

43. We think it would be helpful if the example provided at PERG 8.37.6G(2) were amended to clarify that, in order for there to be "marketing" by the third party within the meaning

of the Directive, the onward distribution by the third party must be part of the arrangements between the AIFM and the third party, rather than something done by the third party on its own initiative and without any involvement of the AIFM.

*Paragraph 8.37.8: Territorial scope of the marketing provisions*

44. We appreciate that PERG 8.37.8 reflects the draft AIFM Regulations but we consider that they contain an incorrect interpretation of the Directive. The provisions operate as a restriction which could prevent a non-EEA AIFM marketing an AIF to, say, UK nationals who are resident in the US. Article 2(1)(c) of the Directive only applies to non-EEA AIFM where their marketing is in the Union. We think it is important that this is reflected in the final AIFM Regulations and the FCA rules and guidance.

45. Separately, we think it would be helpful if the FCA could produce guidance on whether, when marketing to an intermediary, it is necessary to 'look through' the intermediary to the end investor. Where, for instance, an AIFM is marketing to a UK intermediary but for allocation to a US investor, is this marketing, "*to an investor which is domiciled or has a registered office in the United Kingdom*"? We consider that the correct approach is to take a 'look through' approach to the end investor rather than focus on the location of the intermediary if the end investor will be the subscriber. By the time subscription documents are being finalised, the AIFM will know who the end investor is (its name will be on the documents).

*Paragraph 8.37.10: Passive marketing*

46. We have a number of concerns about the guidance at PERG 8.37.10 on passive marketing. In short, our overriding concern is that the guidance is too narrow and unnecessarily restrictive. We consider that less restrictive, and clearer, guidance is necessary.

47. Sub-paragraph (3) states that, "*[o]nly communications which are solicited by the investor should be considered to have occurred at the initiative of the investor*". We consider that this is unnecessarily restrictive. In our view, the issue is how the communication chain is commenced, and we think that this sentence should be deleted. If this sentence is not deleted, it would be helpful if the FCA could at least clarify that for communications to be deemed to have been solicited by the investor, such request by the investor need only be made once in the course of dealings, such that the AIFM can then rely on that request until the investor indicates that it no longer wishes to receive further communications. Furthermore, we consider that, where the investor has an existing relationship with the AIFM (or its affiliates), there should be an exclusion for information flowing in the normal way in the context of that relationship. For example, it would be normal for an

investor in an existing fund to be notified by the fund manager when it intends to begin fundraising for a new fund, and this should not be regarded as "marketing" by the AIFM.

48. Sub-paragraph (4) provides that, "... *documentation which is available on a publically accessible website should not be considered to be sent at the initiative of the investor*". We consider that the provision of general background information about an AIFM – its existence, team and track record – should not be regarded as "marketing" by the AIFM, even if published on a website. It would be helpful if the FCA could produce guidance to this effect.

49. Lastly, the final sentence of sub-paragraph (4) provides that, "... *communications in response to an approach from a potential investor with prior knowledge of the AIF and no previous involvement with the AIFM could be at the initiative of the investor*". We think that the reference to, "*no previous involvement with the AIFM*" is extremely unhelpful and an unnecessary restriction. In many cases, the investor may have invested or considered investing in other funds or separate investment opportunities managed by the AIFM. Just because an investor has had a previous involvement with the AIFM does not mean that the investor could not make an approach of its own initiative in relation to another fund or a separate investment opportunity. We believe strongly that this wording should be deleted.