Technical Bulletin

Keeping you at the forefront of private equity
and venture capital in the UK

November 2019 ////

Contents

Legal & Accounting

Regulatory

Taxation

Terminology

Introduction

Welcome to the BVCA Technical Bulletin, a collection of in-depth articles by members of the BVCA and our three technical committees: Regulatory; Legal & Accounting; and Taxation. Our goal is to keep BVCA members informed of the key topics on the committees' agendas, how they impact the private equity and venture capital industry, and how the BVCA and committee members are engaging with policymakers. The Bulletin is published twice a year.

Amy Mahon
Chair, Legal & Accounting Committee

Mark Baldwin
Chair, Taxation Committee

Tim Lewis
Chair, Regulatory Committee

Gurpreet Manku
Deputy Director General, BVCA

Earlier this year, the Legal & Accounting Committee established a working group to address ongoing issues around replacement of LIBOR rates. Angel Quek examines current market developments for risk-free rates in different currency jurisdictions and considers the potential impact on legacy contracts that do not envisage alternative rates. Victoria Sigeti covers the BVCA's response to the BEIS consultation on Corporate Transparency and Register Reform, which could see an enhanced role for Companies House and measures that could disproportionality impact private equity and venture capital, as well as overall UK competitiveness. Tom Alabaster provides our regular case law update. Please note that the Legal & Accounting Committee also publishes monthly accounting and legal updates which are available on the BVCA website.

The Regulatory Committee has been considering the potential impact on BVCA members of UK regulation, such as the practicalities of implementing the Senior Managers and Certification Regime ("SMCR"). Paul Ellison's article provides an update on the final amendments to the FCA's SMCR before the new rules come into force in December 2019. The article covers the lessons learned from the adoption of SMCR by banks and the key steps private equity firms should be taking to prepare for implementation. Tim Lewis and Stephanie Biggs summarise the other ongoing activities of the Regulatory Committee in their article.

The Taxation Committee has been continuing to work on both domestic and international taxation issues. One of these was HMRC's implementation of EU's Mandatory Disclosure Regime (DAC6) for cross-border transactions. Jenny Wheater's article provide an update on HMRC's DAC6 consultation, which covers the BVCA's response, our discussions with HMRC, and the potential implications for private equity and venture capital firms. Russell Warren's article provides an update on the failure to prevent the facilitation of tax evasion offence.

Brexit update

The Brexit deadline has now been extended until 31 January 2020 to give time for Parliament to ratify the revised EU (Withdrawal Agreement) Bill. If Parliament is able to ratify the agreement before the end of January, the UK will be able to enter a transitional period until the end of 2020. A General Election was voted through by Parliament to break the current deadlock in the Commons. It is set for the 12 December, the first December election since 1923.

The BVCA's workload, continues to be dominated by the ongoing uncertainty around Brexit. We are continuing to provide monthly updates via the Brexit Bulletin[1] and in September we published an updated no-deal Brexit Briefing[2]. Our work is summarised below.

- The UK Government has published statutory instruments to "prevent, remedy or mitigate any failure of EU law to operate effectively" in the event of a no-deal Brexit. The BVCA was in discussions with HMT and the FCA throughout this process and provided feedback. The Government stated that there are no changes to existing policy. The FCA published final instruments, directions and guidance in response to consultation feedback.

---

[1] Available on the BVCA website at https://www.bvca.co.uk/Policy/Political-Engagement/Brexit-and-the-BVCA/Brexit-Bulletin/
[2] https://www.bvca.co.uk/policy/political-engagement/brexit-and-the-bvca/brexit-bulletin/details/BVCA-Brexit-Update---September-2019

- Our Brexit Briefings have covered our regulatory work with the FCA including the "on-shoring" of EU rules to allow the UK regime to function independently of EU law, the UK's Temporary Permissions Regime for EEA firms, and how the FCA intends to use its Temporary Transitional Power. We also commented on transitional regimes being introduced in EU Member States and the discussions with the FCA on the regulatory co-operation agreements needed for members' no-deal Brexit planning.
- The Brexit Briefings summarise the outcome of meetings held with HMRC, HM Treasury and organisations representing the financial services industry, including the BVCA, regarding the tax implications of business restructuring and Brexit. We recommend that members contemplating a business restructuring (whether or not in response to Brexit) review the BVCA's published example then refer to the broader HMRC document which was also published. As always, we recommend you seek professional advice where needed.
- The Brexit Briefings also covers no-deal considerations for portfolio companies and links to relevant Government guidance on topics, including transactions, employment and immigration, supply chain and commercial arrangements, licensing, data protection and intellectual property. The BVCA attended the EU Exit Business Readiness Forum, which was run by the EU Exit Business Intelligence & Readiness Directorate at BEIS. These regular meetings were chaired by senior civil servants from a range of government departments and aimed to keep business intermediaries up-to-date on the latest no-deal guidance for business.

Our committee members

The BVCA is immensely grateful for the time, enthusiasm and expertise of members of the technical committees as their work is crucial to our political engagement and advocacy activities.

We would like to thank all members that have served on the technical committees, including those who have recently stepped down, for their considerable contributions. We would also like to welcome new members to our committees.

	New members on our committees	Members who stepped down
Legal & Accounting Committee	**Jonny Myers** (Clifford Chance) **Steven Smith** (Macquarie)	**Daniel Parker** (Synova)
Regulatory Committee	---	---
Taxation Committee	**José Maria Palicio** (Permira)	**Dominic Spiri**

We would also like to extend our thanks to the excellent secretariat at the BVCA who support the work of our three committees so well.

If you have any questions, or would like to get more involved in the work of the committees and their working groups, please feel free to get in touch with any of us.

With best wishes,

Amy Mahon
Chair, Legal & Accounting Committee

Mark Baldwin
Chair, Taxation Committee

Tim Lewis
Chair, Regulatory Committee

Gurpreet Manku
Deputy Director General, BVCA

Legal & Accounting Committee

Amy Mahon (Chair)	Simpson Thacher & Bartlett
Alastair Richardson (vice-Chair)	3i
Angel Quek	Latham & Watkins
Ashley Coups	EY
Babett Carrier	Cinven
Chris Bulger	Vitruvian Partners
Ed Hall	Goodwin
Elizabeth Judd	STAR Capital
Garrath Marshall	Deloitte
Geoff Kittredge	Debevoise
John Atherton	Ares Management
John Heard	Abingworth
Jonathan Martin	KPMG
Jonny Myers	Clifford Chance
Karen Sands	Hermes GPE
Nick Reid	Carlyle
Richard Mcguire	PwC
Stephanie Biggs	Travers Smith
Steven Smith	Macquarie
Tom Alabaster	Linklaters
Victoria Sigeti	Freshfields Bruckhaus Deringer

Regulatory Committee

Tim Lewis (Chair)	Travers Smith
Rachel Thompson (vice-Chair)	Bridgepoint
Andrew Lewis	ICG
Christopher Crozier	Permira
Ed Kingsbury	CMS
James Smethurst	Freshfields Bruckhaus Deringer
John Decesare	3i
John Morgan	Pantheon
Lindsay Hamilton	Livingbridge
Mark Howard	KKR
Matthew Cottrell	Carlyle
Neel Mehta	DWS Private Equity
Owen Lysak	Clifford Chance
Paul Cook	YFM Equity Partners
Paul Ellison	Macfarlanes
Peter Moore	Cinven
Simon Powell	Advent International
Alfred Fabian (secondee)	Travers Smith

Taxation Committee

Mark Baldwin (Chair)	Macfarlanes
Abigayil Chandra	Deloitte
Alexander Conway	Livingbridge
Alexander Cox	Ashurst
Alexandra Hone	ICG
Anthony Stewart	Clifford Chance
Caroline Conder	LDC
Clare Copeland	Carlyle
Craig Vickery	Exponent
Dan Kennedy	Permira
Eli Hillman	Grant Thornton
Gareth Miles	Slaughter & May
Garry O'Neill	3i
Graham Iversen	Greenberg Traurig Maher
James Pratt	BDO
James Sanderson	Vitruvian Partners
Jenny Wheater	Linklaters

Jill Hardie	Aberdeen Standard Investments
Jonathan Page	PwC
Jose Maria Palicio	Permira
Maria Carradice	Mayfair Equity Partners
Matthew Saronson	Debevoise
Michael McCotter	Charterhouse Capital Partners
Paul McCartney	EY
Richard Vitou	Deloitte
Russell Gibson	KPMG
Russell Warren	Travers Smith
Stephen Pevsner	Proskauer
Tim Hughes	PwC
Tim Lowe	Kirkland & Ellis
Tony Mancini	KPMG
Rhiannon Kinghall Were (secondee)	Macfarlanes

01.

LIBOR Transition

Angel Quek (Latham & Watkins)

01. LIBOR Transition

Angel Quek
Latham & Watkins

In July 2017, the FCA announced that it will no longer compel panel banks to contribute to LIBOR submissions after the end of 2021. It is unclear at this stage whether LIBOR will cease to exist from that date or continue to be published (with reduced submissions).

Whilst the potential discontinuation may seem like a while away, it is prudent for BVCA members to consider the various contexts in which LIBOR may apply to their businesses, in preparation for a smooth transition away from LIBOR. The FCA has stated that asset managers need to prepare for the possible end of LIBOR at the end of 2021 and to transition out of LIBOR instruments before LIBOR disappears.

How might LIBOR be relevant?

The contexts in which LIBOR is used within a firm's business could potentially be wide-ranging, whether from a fund or portfolio level perspective. Most commonly, it is used for the purposes of financing and treasury activities, such as:

- syndicated or bilateral loan agreements;
- floating rate notes; and
- derivative transactions.

However, it may not be limited to such purposes and it is worthwhile considering how else it may be relevant to the business – for example, in commercial contracts (whether in late payment provisions or purchase price adjustment mechanics), in intra-group arrangements, from an accounting perspective (e.g. fair value calculations, hedge accounting) from a regulatory perspective or in pricing and valuation models.

It is recommended that parties conduct, if not already conducted, a diligence exercise to review and identify the instances where LIBOR may be relevant. An understanding of these uses will help drive next steps including consideration of what replacements may be appropriate, what contracts and/or processes need updating and/or re-negotiation and whether any fall-backs apply in the interim.

Current market developments

LIBOR is currently available in a number of tenors and across five currencies. Working groups in each currency jurisdiction have identified near-risk free rates ("RFRs"), as set out in the table, as potential replacement benchmarks to LIBOR. This is an ongoing process and work is being conducted to evaluate and tailor the use of such benchmarks across different market and products. In particular, it is worth noting that there are various differences between the rates, which means that RFRs are not an exact substitute and it is not a simple matter of replacing references to LIBOR in a document with references to SONIA.

GBP	**SONIA** (Reformed Sterling Overnight Index Average)
EUR	**€STR** (Euro Short-Term Rate)
USD	**SOFR** (Secured Overnight Financing Rate)
CHF	**SARON** (Swiss Average Overnight Rate)
JPY	**TONA** (Tokyo Overnight Average rate)

For example, for the loan markets, there are operational issues and yield differences between the use of LIBOR and RFRs – in particular:

- LIBOR is a forward-looking term rate and RFRs are backward-looking overnight rates,
- LIBOR is available in a number of tenors whereas RFRs are overnight rates; and
- LIBOR includes term bank credit risk and term liquidity premia (reflective of the risk inherent in longer dated funding), whereas RFRs do not include a credit premium or liquidity premium.

There are practical issues to consider, such as when rates are published, calculation methodologies to reflect the use of an overnight rate, and what rate is to be used (and over what period), so that interest calculations can be made in advance of payment to allow advance notice of payment and cashflow certainty. Working groups have been exploring the use of average and/or compounded rates and in this respect, there has been growing traction with the FRN market convention of compounding in arrears with a lag mechanism. Ultimately, there is also a need to ensure alignment and consistency across relevant products such as loans and interest rate hedging. Given the yield differentials between LIBOR and RFRs, there may also be potential pricing adjustments which need to be reflected if RFRs are ultimately adopted. Note that financial markets have also been looking at developing a "credit spread adjustment" in this regard.

In light of the above, parties have yet to widely adopt an approach of hard-wiring a replacement benchmark into documents. Instead, provisions such as the LMA "Replacement of Screen Rate" provisions, are being incorporated into loan documents to allow for amendment flexibility (usually with majority lender consent) to update documents at a later stage. This "amendment approach" aims to provide greater flexibility to adapt as financial markets evolve on this topic.

Legacy contracts

For legacy contracts that are already in existence and are expected to continue beyond 2021, consideration should be given to:

- what fall-back position applies under the contract in the event of a discontinuation of LIBOR;
- whether an amendment is required and should be sought;
- whose consent is required for the amendment (e.g. is it a majority decision or is unanimous approval required?);
- timing of any amendment;
- the potential for mismatch with any hedging contract; and
- amendment costs, legal fees and other costs may be relevant (for amending documents as well as updating any internal systems and processes (if necessary)).

There is significant work being carried out by trade associations and other market participants in the derivatives, bonds and loans market to settle on standard conventions and wording for the replacement rates. Due to this ongoing work, parties are generally not proactively amending their legacy documents at this stage. However, if documents are being amended for other reasons (e.g. in a repricing or other consent request scenario), that may also be an opportunity to update the documents to introduce amendment flexibility.

Conclusion

Whilst financial markets are adapting and it may not be up to individual borrowers or firms to dictate what the alternative solution should be in all cases, BVCA member firms should be assessing their exposure to LIBOR and planning for the transition.

02.

Corporate Transparency and Register Reform

Victoria Sigeti (Freshfields Bruckhaus Deringer)

02. Corporate Transparency and Register Reform

Victoria Sigeti
Freshfields Bruckhaus Deringer

Against a backdrop of growing concern over the misuse of UK corporate entities in recent years, the Government launched its Corporate Transparency and Register Reform consultation ("the Consultation") in May 2019. The Consultation covered a range of proposals designed to enhance the role of Companies House, increase the transparency of UK corporate entities and help combat economic crime. If implemented, the proposals would be the most significant changes to the UK regime for setting up and operating companies since the UK companies register was created in 1844. Many of the proposals would require primary legislation, most likely to be achieved by amending the Companies Act 2006.

The Consultation sought views on a wide range of proposals. Certain of these are likely to be of more relevance than others to the private equity and venture capital industry. These include:

- verification of the identity of directors before they are validly appointed;
- collection of more detailed information about shareholders;
- Companies House having more discretion to query information on the register; and
- capping the number of directorships that can be held by an individual.

The BVCA provided a detailed written response to the Consultation (available on the BVCA website) and attended a stakeholder roundtable with representatives from the Department for Business, Energy and Industrial Strategy ("BEIS").

We have summarised below the key aspects of the BVCA's response on the four proposals identified above. More generally, in our response, we focused on the need to ensure that the UK remains an attractive place to do business for the vast majority of companies that are pursuing legitimate corporate objectives. This is particularly vital given the current political and economic climate and in light of the fact that a number of the proposals go beyond what is required in other jurisdictions. In the BVCA's view, certain of the proposals seem disproportionate to the perceived risks and if those proposals are implemented in the form suggested (which potentially involves increased process and uncertainty as well as delay), there is a risk that investors may favour other jurisdictions.

Verification of the identity of directors

The Consultation proposed that a person should not be able to act as a director until his/her identity has been verified.

The BVCA response expressed concern that there would be a number of complexities in the practical implementation of this proposal. In our view, it should be relatively straightforward to require such verification on new incorporations, although we do not think that an incorporation should be held up if directors are not able to verify their identities, rather there should simply be an obligation to provide the requisite information within a certain period.

It would, however, be much more difficult to implement this in relation to new appointments to existing companies, since directors are typically appointed by the board or shareholders and registration is not a pre-requisite to being appointed. We envisage a number of difficulties with changing the law to provide that a director is only validly appointed once registered and verified (such a change would be necessary if verification was required to take place as a pre-requisite to a valid appointment). In particular, the precise timing of appointment and resignation of directors is critical to ensure a proper allocation of responsibility and liability, so any such change would require both identity verification and online registration of appointments / resignations to be able to occur instantaneously (24 hours a day, seven days a week, including for non-UK passport holders).

We also believe that changing the law in this way could have the unintended consequence of an increase in the number of de facto directors who rely on common law ostensible authority rather than being registered at Companies House. This would have the opposite effect to the one intended and would increase uncertainty for third parties.

If identity verification was made a pre-requisite to valid appointment without a change in law to provide that directors are only validly appointed once registered, there would be a grey area in respect of acts undertaken prior to verification and, in particular, whether a company is bound by the acts of an unverified director.

Collection of more detailed information about shareholders

The Consultation proposed that individuals who have a key role in companies, such as “persons with significant influence or control” (“PSCs”), should also have their identities verified. It also considered whether more information should be disclosed about shareholders, including possible identity verification.

The BVCA response explained our strong view that identity verification for PSCs should be voluntary, as we do not see how mandatory verification furthers the stated objective of preventing the use of companies for illicit purposes. In any event, we do not see how this can take place prior to a PSC becoming a PSC, since this would have far reaching consequences for M&A and capital markets transactions (such as increasing the leak risk and creating uncertainty through the need for conditionality in transactions). As regards shareholders more generally, our view is that additional information could be included in the annual confirmation statement (so long as sensitive personal data is protected on the public register). However, we consider the introduction of more regular filings of shareholder information would be disproportionately burdensome and that it would not assist with genuine transparency, since such filings could only ever relate to legal ownership and so could be avoided by those wishing to avoid transparency via nominee structures. In relation to identity verification for shareholders, we explained that we were not in favour as we did not think that it would materially improve transparency for third parties.

Companies House having more discretion to query information on the register

The Consultation proposed an extension of the powers of Companies House to query and seek corroboration of information before it is entered on the register and to make it easier to remove inaccurate information from the register. This is intended to deliver better quality information on the register.

The BVCA response explained that a general discretion to query information before it is entered on to the register (beyond the discretion Companies House already has to reject an incomplete filing) seems excessive and likely to create material uncertainty for companies. This is particularly of concern where it could cause delay on a new incorporation, or in circumstances in which there are either legal consequences of a failure to file on time (such as accounts) or for filings which are effective upon registration (such as reductions of capital). This approach would also require significant skilled resource at Companies House.

Capping the number of directorships that can be held by an individual

The Consultation sought views on whether imposing a limit on the number of directorships to be held by one individual might deter abuse of UK legal entities.

In the BVCA response noted that it is sufficient to identify and report the number of directorships held by an individual. We disagree with the introduction of a cap as we do not believe there is a specific number of directorships that would render a director no longer able to perform their duties adequately. The appropriate number for a particular individual will vary and, as such, any cap imposed would be arbitrary. The introduction of a cap could lead to less experienced individuals being required to take on directorships. In the context of the drive towards high quality corporate governance, that would be an unfortunate outcome.

Next steps

We anticipate a further consultation once BEIS has digested the responses it has received to the Consultation. The BVCA will continue to engage with BEIS as these proposals develop.

03.

Case Law Update

Tom Alabaster (Linklaters)

03. Case Law Update

Courts shifting away from implied duties of good faith?

Tom Alabaster
Linklaters

It has long been established that English law recognises certain implied duties of "good faith" in particular contexts (such as in the performance of a partnership contract). However, the law is still in flux when it comes to finding that a contract is subject to an implied duty of good faith. There was a spate of cases in 2018 and early 2019 finding that this duty arises in a "relational" contract such as a joint venture, including *Bates v Post Office [2019] EWHC 606 (QB)*[3], where Fraser J set out a (non-exhaustive) list of characteristics that are relevant to determine whether a contract is "relational". However, recent cases suggest a more critical approach. This includes returning to the strict tests for the implication of terms so that an implied duty of good faith will only apply where needed to give the contract commercial or practical coherence (*UTB LLC v Sheffield United Ltd [2019] EWHC 2322*)[4] or seizing upon boilerplate provisions containing references to good faith as an indication that the parties have exhaustively defined the extent of any good faith obligations, so that no wider duty of good faith should be implied (*Teesside Gas Transportation v CATS North Sea [2019] EWHC 1220*)[5].

Good faith and commercially unacceptable behaviour

New Balance Athletics, Inc v The Liverpool Football Club and Athletic Grounds Limited [2019] EWHC 2837 (Comm).

In *New Balance Athletics, Inc v The Liverpool Football Club and Athletic Grounds Limited*[6], the Court did not have to decide whether the parties' contract contained an implied obligation of good faith, as they agreed that it did. However, they disagreed as to what that obligation meant.

Teare J stated that, ultimately, the question for the Court is whether reasonable and honest people would regard the conduct alleged to be in breach of a good faith obligation as "commercially unacceptable". It was clear, he said, that the duty of good faith can be breached not only by dishonesty but also by conduct which lacks fidelity to the parties' bargain. In judging whether a party has not been faithful to the bargain it is necessary to bear in mind the nature of that bargain, the terms of the contract and the context in which the matter arises.

Directors did not owe fiduciary duties to shareholders on an MBO

Vald. Nielsen Holding A/S Newwatch Ltd v Baldorino & Ors [2019] EWHC 1926 (Comm)

In *Vald. Nielsen Holding A/S Newwatch Ltd v Baldorino & Ors*[7], the High Court considered various claims by selling shareholders arising out of a private equity-backed management buy-out. It found that the managers did not owe any fiduciary duties to the selling shareholders merely by virtue of the fact that they have better access to information about the target and a personal interest in the transaction. However, directors do still owe duties to the target company itself and these need to be carefully considered in the context of any MBO transaction.

---

[3] Bates v Post Office [2019] EWHC 606 (QB) (https://www.bailii.org/ew/cases/EWHC/QB/2019/606.html)
[4] UTB LLC v Sheffield United Ltd [2019] EWHC 2322. (https://www.bailii.org/ew/cases/EWHC/Ch/2019/2322.html)
[5] Teesside Gas Transportation v CATS North Sea [2019] EWHC 1220. (https://www.bailii.org/ew/cases/EWHC/Comm/2019/1220.html)
[6] New Balance Athletics, Inc v The Liverpool Football Club and Athletic Grounds Limited [2019] EWHC 2837 (Comm). (https://www.bailii.org/ew/cases/EWHC/Comm/2019/2837.html)
[7] Vald. Nielsen Holding A/S Newwatch Ltd v Baldorino & Ors [2019] EWHC 1926 (Comm). (https://www.bailii.org/ew/cases/EWHC/Comm/2019/1926.html)

The executive management team of the target company pursued an MBO alongside a private equity house. The selling shareholders argued that the management had misled them as to the state of the business in that it was more successful than the managers had represented. As such, the sellers had sold their shares for a lesser sum than if they had known the true value. The sellers brought a claim in the tort of deceit and a claim for breach of fiduciary duty. The sellers claimed that a fiduciary relationship existed at common law between the managers on the one hand and the shareholders on the other, for reasons including the close relationship between them all, the fact of the managers' involvement in the transaction and the disparity of information regarding the affairs of the target.

The Court ruled that the claim for deceit arising from representations made in certain emails was successful and awarded damages. The default position is that directors do not owe fiduciary duties to shareholders absent exceptional circumstances. The Court considered the law on fiduciary duties at length and referred to the judgement of *Nugee J in Sharp v Blank [2015] EWHC 3220 (Ch)*[8], concluding that directors will only owe fiduciary duties to shareholders in limited circumstances. Such circumstances mostly involve companies which are small and closely-held, where there is often a family or other personal relationship between the parties and where there is a particular transaction involved in which directors are dealing with the shareholders. The Court found that no fiduciary relationship arises merely from the fact that the managers' actions could affect the shareholders or that they had more knowledge and information about the target than the shareholders. This was a normal feature of the shareholder/director dynamic.

On the facts of this case, the special circumstances needed to establish a fiduciary relationship were not present and so there was no such relationship between the managers and the shareholders.

High Court considers distribution formalities and revisits directors' liability

Burnden Holdings (UK) Limited (in liquidation) v Fielding [2019] EWHC 1566 (Ch)

In *Burnden Holdings (UK) Limited (in liquidation) v Fielding*[9], the High Court dismissed claims in respect of a distribution in specie in a case that considers a number of practicalities relating to dividends. In particular it considers that two-page interim accounts may be sufficient to justify a dividend by a non-trading holding company, and that directors' liability for unlawful distributions is fault-based rather than strict.

Mr and Mrs Fielding were the majority owners of the BHUK group of companies and directors of BHUK at the relevant time. BHUK granted security to Mr and Mrs Fielding in relation to loans they made to the BHUK group. BHUK later made a distribution in specie of its shareholding in its wholly-owned subsidiary, Vital Energi Utilities Ltd, as part of a restructuring involving the demerger of Vital from the BHUK group. BHUK went into liquidation and the liquidator brought claims in respect of these transactions.

The High Court dismissed the liquidator's claims that:

- the grant of security was a dishonest breach of fiduciary duty and a transaction defrauding creditor under Section 423 Insolvency Act 1986; and
- the distribution was unlawful under the Companies Act 1985, a breach of fiduciary duty under Section 172(3) Companies Act 2006 and a transaction defrauding creditor under Section 423 IA 1986.

[8] Sharp v Blank [2015] EWHC 3220 (Ch). (https://www.bailii.org/ew/cases/EWHC/Ch/2015/3220.html)
[9] Burnden Holdings (UK) Limited (in liquidation) v Fielding [2019] EWHC 1566 (Ch). (https://www.bailii.org/ew/cases/EWHC/Ch/2019/1566.html)

The case straddled the period in which CA 1985 was repealed and replaced by CA 2006. Both statutes are referenced in the judgment.

The ruling that a director's liability for an unlawful dividend is fault-based resolves a conflict in the authorities which had been noted in several recent Supreme Court decisions and represents a more director-friendly environment in respect of this area of liability.

Privy Council considers directors' authority

East Asia Company Ltd v PT Satria Tirtatama Energindo (Bermuda) [2019] UKPC 30

In *East Asia Company Ltd v PT Satria Tirtatama Energindo*[10], the Privy Council considered the validity of a 'Heads of Agreement on the Sale and Purchase of Bali Energy Ltd' (HoA) and a share transfer form, transferring shares from East Asia Company Ltd (EACL) to PT Satria Tirtatama Energindo (PT Satria) of EACL's sole asset. The HoA was executed by one of EACL's three directors, and by PT Satria's sole director. PT Satria conceded that although EACL's director did not have the actual authority to transfer the shares on behalf of EACL, it argued he had ostensible authority to do so and therefore the HoA was validly executed.

The Privy Council upheld the Bermuda Court of Appeal's decision that the director of EACL did not have the ostensible authority to sign the transfer, that PT Satria was put on inquiry as to the lack of authority, and therefore the share sale agreement and transfer was not binding. In reaching their conclusion, the Privy Council considered that EACL had not held the director out as having any authority to enter into the transaction, nor had PT Satria relied on any representation by EACL as to the director's authority.

Although the decision in *East Asia Company Ltd v PT Satria Tirtatama Energindo* is not binding on the Courts of England and Wales, it provides persuasive guidance on issues around ostensible authority.

High Court considers level of care required when warranting forecasts

Triumph Controls UK Ltd v Primus International Holding Company [2019] EWHC 565 (TCC)

In *Triumph Controls UK Ltd v Primus International Holding Company*[11], the High Court considered multiple warranty claims under a share purchase agreement (SPA) arising as result of a significant shortfall in the target business's projected revenue following completion. While the judge dismissed some of the warranty claims, she upheld those which related to the "careful preparation" of forward-looking projections.

Pursuant to an SPA, Triumph Controls UK Ltd acquired three companies, one based in the UK and two in Thailand. The companies were loss-making but expected to become profitable within a few years. The SPA provided that the seller would not be liable for breach of warranty where the matter had been fairly and clearly disclosed in writing in or under the disclosure letter (with sufficient detail to identify the nature of the matter disclosed). The disclosures revealed significant and persistent operational issues which had led to customer complaints.

---

[10] East Asia Company Ltd v PT Satria Tirtatama Energindo (Bermuda) [2019] UKPC 30. (https://www.bailii.org/uk/cases/UKPC/2019/30.html)

[11] Triumph Controls UK Ltd v Primus International Holding Company [2019] EWHC 565 (TCC). (https://www.bailii.org/ew/cases/EWHC/TCC/2019/565.html)

One of the warranties in the SPA provided that the forward-looking projections had been honestly and carefully prepared by the seller so far as it was aware. Six months after completion, the financial performance of the companies was significantly worse than forecast due to operational issues and a delay in transferring work from the UK to Thailand. The UK company also lost an industry accreditation, which it required to carry out its business. Around 17 months after completion, the buyer gave notice to the seller of claims for breaches of warranties in the SPA.

The term “carefully prepared” was not a defined term nor a recognised accounting term but rather a matter of judgement based on professional experience. Taking account of the view of the experts of both sides, the judge held that the forecasts had not been carefully prepared, on the grounds that the seller had not taken into account key assumptions, which meant that the operational and financial position of the target had not been adequately modelled. Had the forecasts been carefully prepared, they would have included adjustments to the long-range plan of the business, which would have delayed profitability for the target companies. On that basis, the buyer would have lowered the price.

The judge held that the measure of damages was to be based on the general contractual principle of putting the buyer in the position it would have been in had there been no breach of warranty. Therefore, the buyer was entitled to damages based on the difference between the price agreed on the basis of the assumption of the long-range plan and what the price would have been had the plan been appropriately adjusted, subject to the contractual cap on liability.

The value of the target following the adjustment of the long-range plan was to be done on a discounted cash flow basis. The judge favoured this approach because the companies were sold as a going concern and remained in active business, with their value derived from revenues driven by production. The discounted cash flow basis anticipated future economic benefits or cash flow from the assets whereas the net asset approach put forward by the seller would only take into account the current market value of the underlying assets of the business less its outstanding liabilities.

The time limit for bringing warranty claims under the SPA was held to apply not only to claims for breaches of warranty but also to a claim by the buyer that the seller had breached its obligation to notify the buyer of breaches of warranty at the time of completion.

This constituted fair and clear disclosure to defeat a claim for breach of warranty as to no potential claims. The SPA did not require disclosure of the extent and scope of the relevant matter, simply sufficient detail to identify its nature.

Notice of warranty claims under an SPA

Stobart Group Ltd v Stobart [2019] EWCA Civ 1376

In *Stobart Group Ltd v Stobart*[12], the Court of Appeal considered whether a unilateral notice served by Stobart Group Ltd (SGL) and Stobart Rail Ltd (SRL) was valid for the purpose of giving notice of a tax claim under a share purchase agreement (SPA). Simon LJ set out the Court’s approach to the construction of notices, reiterating principles from *Mannai Investment Co Ltd v. Eagle Star Life Assurance Co Ltd [1997] AC 749*[13] and *Wood v. Capita Insurance Services Ltd [2017] UKSC 24*[14], that notices must be approached objectively, taking into account the relevant objective contextual scene. In this case, the Court of Appeal unanimously dismissed the appeal, holding that it was not an effective notice drafted in compliance with the terms of the SPA, therefore no notice of a tax claim had been made within the SPA’s prescribed seven years of the completion date, and as such a claim was barred. This case reminds us of the importance of drafting notices fully in compliance with any prescribed terms in an SPA.

Implying terms into SPAs

Zedra Trust Company (Jersey) Ltd v The Hut Group Ltd [2019] EWHC 2191 (Comm)

In *Zedra Trust Company (Jersey) Ltd v The Hut Group Ltd*[15], a dispute arose in the context of the sale of the entire share capital of the target company. A share purchase agreement (SPA) relating to the sale provided for the buyer to require the target's auditor to determine whether there had been any tax over-provisions at the seller's request. The buyer provided an executive summary of the auditor's report to the seller. The seller sought disclosure of the full report, submitting that it was an implied term that the full report was to be provided to them.

The High Court referred to the test set out by Lord Neuberger in *Marks & Spencer plc v BNP Paribas Securities Services Trust Co (Jersey) Ltd [2015] UKSC 72, [2016] AC 742*[16] that the Court will apply when deciding whether to imply a term into a contract, namely is it (a) necessary in the sense of being necessary for the contract to have business efficacy such that the contract lacks commercial or practical coherence without it; or (b) sufficiently obvious to go without saying? In this case, the Court implied a term into the SPA that the seller was entitled to see the full report on tax over-provisions as it was both necessary and obvious to imply such a term. This case demonstrates that parties should state the level of disclosure in SPAs to avoid the possibility of terms being implied.

What constitutes good consideration?

Simantob v Shavleyan [2019] EWCA Civ 1105

In *Simantob v Shavleyan*[17], the Court of Appeal considered one of the elements of a valid contract under English law, that of "consideration". The issue of consideration, as acknowledged by Lord Sumption in the Supreme Court case of *MWB Business Exchange Centres [2018] UKSC 24*[18], is "a difficult one", and is "probably ripe for re-examination". Contracts rarely fail for lack of consideration, particularly where it is clear parties intended to be bound, but there can be issues where a contract is varied, not using a deed, where the variation appears to be one-sided.

In this case, Shavleyan was in debt to his business partner, Simantob. The parties entered into a settlement agreement which included a large daily interest payment. Shavleyan made some payments to Simantob but did not pay the entirety of what was owed. At trial, the judge found that a later oral agreement between the parties had capped Shavleyan's liability. In deciding the validity of this variation to the settlement agreement, there had to have been "consideration" by Shavleyan in order for him to pay a lesser sum.

---

12 Stobart Group Ltd v Stobart [2019] EWCA Civ 1376. (https://www.bailii.org/ew/cases/EWCA/Civ/2019/1376.html)
13 Mannai Investment Co Ltd v. Eagle Star Life Assurance Co Ltd [1997] AC 749. (https://www.bailii.org/uk/cases/UKHL/1997/19.html)
14 Wood v. Capita Insurance Services Ltd [2017] UKSC 24. (https://www.bailii.org/uk/cases/UKSC/2017/24.html)
15 Zedra Trust Company (Jersey) Ltd v The Hut Group Ltd [2019] EWHC 2191 (Comm). (https://www.bailii.org/ew/cases/EWHC/Comm/2019/2191.html)
16 Marks & Spencer plc v BNP Paribas Securities Services Trust Co (Jersey) Ltd [2015] UKSC 72. (https://www.bailii.org/uk/cases/UKSC/2015/72.html)
17 Simantob v Shavleyan [2019] EWCA Civ 1105. (https://www.bailii.org/ew/cases/EWCA/Civ/2019/1105.html)
18 MWB Business Exchange Centres [2018] UKSC 24. (https://www.bailii.org/uk/cases/UKSC/2018/24.html)

The Court of Appeal held that a debtor who promised to give up any claim to a defence (in this case, whether the interest amounted to a penalty clause), which was later found to be unmeritorious, was good consideration for the variation of a settlement agreement. The key issue was whether the debtor believed that he could raise the defence, not whether the defence had any real prospect of success; and this was in furtherance of "the public policy in favour of holding people to their commercial bargains". The validity of the consideration must be judged at the time the agreement was made, and an agreement to not pursue a claim or defence can be good consideration.

Automatic email footer constitutes a valid signature

Neocleous & Anor v Rees [2019] EWHC 2462 (Ch)

In *Neocleous & Anor v Rees*[19], the County Court held that an automatically generated email footer constituted a valid signature.

A dispute arose about a right of way over some land near Lake Windermere. To settle the dispute, Ms Rees proposed to sell part of her land to Mr and Mrs Neocleous. The terms of the settlement were set out in a series of emails exchanged by the parties' solicitors. Ms Rees later claimed that there was no enforceable contract because her solicitor's purported signature was by automatic generation of his name, occupation, role and contact details on a footer at the bottom of the relevant email. Mr and Mrs Neocleous brought a claim for specific performance of the settlement agreement. They contended that an email footer is capable of rendering a document "signed" (regardless of whether that footer is inserted automatically or entered manually).

The County Court held that the test of a valid signature is whether the name was applied with authenticating intent (as identified in *Mehta v J Pereira Fernandes SA [2006] EWHC 813 (Ch)*[20] and adopted by the Law Commission). The Court was satisfied that Ms Rees' solicitor had signed the relevant email on behalf of Ms Rees and held that Mr and Mrs Neocleous were entitled to an order for specific performance.

The Court noted that the recipient of an email has no way of knowing whether the details at the bottom of an email are added automatically or manually by the sender. Objectively "the presence of a name at the end of an email indicates a clear intention to associate oneself with the email – to authenticate or sign it".

Key reasons for the decision were:

- An email footer only exists where there has been an initial conscious decision to set up the automatic signature. The recipient of an email with such a footer would naturally conclude that the sender's details had been included as a means of identifying the sender with the contents of the email.
- The sender of an email is aware that their name is being applied as a footer. The recipient has no reason to think that the sender is unaware of the presence of the email signature.
- The use of the words "Many thanks" by Ms Rees' solicitor before the footer shows an intention to connect his name with the contents of the email.
- The presence of a name and contact details is the usual style of signature at the end of a document.

[19] Neocleous & Anor v Rees [2019] EWHC 2462 (Ch). (https://www.bailii.org/ew/cases/EWHC/Ch/2019/2462.html)
[20] Mehta v J Pereira Fernandes SA [2006] EWHC 813 (Ch). (https://www.bailii.org/ew/cases/EWHC/Ch/2006/813.html)

Supreme Court rules that the “blue pencil” test can be used to remove words which would make a non-compete unenforceable

Tillman v Egon Zehnder Limited [2019] UKSC 32

The Supreme Court has handed down judgment in the case of *Tillman v Egon Zehnder Limited*[21]; the first case on restrictive covenants to be heard by it in over 100 years. The decision resolves two competing lines of authority on the “blue pencil” test, establishing that the liberal approach, which gives the employer more flexibility, is the correct one. However, the Court hinted strongly that the need to give clarity to the employer’s drafting could result in the employer bearing the cost of the litigation, underlining the need to ensure that covenants are drafted in clear and unambiguous terms.

Ms Tillman worked as a consultant with the executive search firm, Egon Zehnder Limited (EZL), for over 13 years. Following her resignation, Ms Tillman wanted to take up employment with a US competitor. Her contract of employment with EZL contained restrictive covenants, including a non-compete clause. EZL sought to enforce the covenants and obtained an injunction in the High Court preventing her from breaching the non-compete clause.

The non-compete clause stated: “*You shall not … directly or indirectly engage or be concerned or interested in any business carried on in competition with any of the businesses of the Company or any Group Company …”* The case turned on the words “or interested in”. Ms Tillman argued that they prevented her from having any shareholding, no matter how small, in a competitor.

Before the Supreme Court, EZL appealed the Court of Appeal’s finding that the non-compete was unenforceable, raising three arguments.

EZL argued that owning shares was not an activity that was capable of being prevented by a restrictive covenant. Holding shares was not a trade or occupation which could be subject to restraint. This was rejected by the Supreme Court. It outlined three scenarios in which a former employer’s business could be threatened by a former employee holding shares in a competitor:

- where the individual had a controlling shareholding, allowing the former employee to direct a competitor’s operations;
- where the individual had a minority shareholding giving the former employee influence over a competitor’s activities; and
- the individual being appointed to a senior position in a competitor and being remunerated in part by shares or share options.

The Supreme Court held that the restraint on shareholding was part of the restraint on Ms Tillman’s work. It did fall within the restraint of trade doctrine and must be reasonable to be enforceable.
EZL also argued that the words “interested in” did not prohibit Ms Tillman from holding shares in a competitor. The Supreme Court rejected this approach on two grounds: first it held that the natural meaning of the words included holding shares, and second, the formulation “engaged, concerned or interested in” has been consistently interpreted by the Courts as including owning shares.

Having lost on the first two arguments, EZL’s case hinged on the issue of whether the words “or interested in” could be severed from the covenant. Can parts of a restrictive covenant be severed to make the covenant enforceable? There are two competing lines of authority on how to approach

---

[21] Tillman v Egon Zehnder Limited [2019] UKSC 32. (https://www.bailii.org/uk/cases/UKSC/2019/32.html)

severing words from restrictive covenants. Under the “strict” approach, parts of a single promise or obligation cannot be severed. The Supreme Court rejected this approach. Instead, it held that the three-stage “Beckett” test should be applied. Under this test, words may be deleted if:

- no additional words need to be added;
- there is adequate consideration for the remaining terms; and
- the character of the restriction is not changed so that it becomes “not the sort of contract that the parties entered into at all”.

Applying this test, the Supreme Court held that the words “or interested in” could be removed from the non-compete covenant, leaving it enforceable.

04.

Senior Managers & Certification Regime

Paul Ellison (Macfarlanes)

04. Senior Managers & Certification Regime

Paul Ellison
Macfarlanes

This article addresses the key developments concerning the rules on the extended Senior Managers and Certification Regime ("SMCR") since the May 2019 Technical Bulletin, as applicable to the private equity and venture capital industry. In particular, this article:

- provides a reminder of the key dates for SMCR implementation;
- contains an update on the finalisation of the Directory;
- summarises feedback on the adoption of the SMCR by banks; and
- provides five key practical steps which private equity and venture capital fund managers should be taking in advance of the introduction of the SMCR.

SMCR implementation – key dates

There are a number of key dates leading up to the extension of the SMCR on 9 December 2019 and beyond. These dates are as follows:

- 9 June 2019: Since this date, firms have been able to file a Form O to opt-up from Core to Enhanced, or from Limited Scope to Core.
- 9 September 2019: On this date, Form K (used to provide notification in relation to a non-approved non-executive director becoming Chair (SMF9)) and Form A (used for applying for a Senior Manager to be approved) were made available.
- 24 November 2019: Deadline for submitting Form K and Form O.
- 9 December 2019: SMCR for solo regulated firms begins. Senior Managers and Certification Staff must have received training by this date (as detailed further below) and the firm must be ready to implement the regime.
- 9 December 2020: All other staff to whom the Conduct Rules apply must have received training. Initial certifications must be completed in respect of Certification Staff. Firms must submit data to the Directory.

Finalisation of the Directory – an update

As explained in the BVCA's May 2019 Technical Bulletin, the FCA has set out the final rules on establishing a directory of individuals who will no longer be included on the Financial Services Register ("FS Register") following the extension of the SMCR (the "Directory"). The Directory will be separate from the FS Register, which will contain only Senior Managers. The Directory will include individuals performing roles that will no longer be made public on the FS Register.

Three broad categories of individuals will be included, collectively referred to as "Directory Persons":

- all Certified Staff (i.e. those holding a certification function under the SMCR);
- directors who are not performing SMFs (both executive and non-executive); and
- other individuals who are sole traders or appointed representatives ("ARs") (including those within ARs) where they are undertaking business with clients and require a qualification to do so.

FCA solo-regulated firms can start to upload their data from 9 December 2019 in line with the SMCR extension date. The information in relation to these solo-regulated firms will then go live in December 2020.

As was set out in May's Technical Bulletin, the following information will have to be provided by firms:

- Directory Persons' details including full name, date of birth and IRN (if the individual has no IRN this will be automatically assigned by the Directory);
- relevant roles(s) held (i.e. certification function or non-SMF Director);
- different customer engagement method(s) offered by an individual (for customer facing roles requiring certification only) (for example, face-to-face, telephone and/or online);
- membership of professional bodies (for customer facing roles requiring certification only);
- start and end dates of each role;
- type of business the individual is qualified to undertake (if requiring certification);
- workplace location(s) (for customer facing roles requiring certification only); and
- unique identifiers (for example, national insurance number or passport number if the individual is not the holder of a national insurance number).

This will require firms to provide a large amount of information to the FCA. On 6 September 2019, the FCA published a user guide on submitting multiple entries to the Directory. The user guide sets out instructions on how to access and fill in a template spreadsheet which can be uploaded to the system in order to provide full details of all relevant individuals. It should be noted that the spreadsheet is to be used for initial submissions only, and that subsequent amendments to the data provided must be made separately.

Lessons learned from the adoption of the SMCR by banks

On 5 August 2019, the FCA published its findings of its review into the embedding of the SMCR in the banking sector. BVCA member firms may find some of the lessons learned instructive in their own approach to implementation.

Overall, the FCA found that the banking industry has made a concerted effort to implement the regime. Most firms are taking actions to move away from basic rule-based compliance, towards embedding the regime in the organisation. The review covered a wide range of themes, and their findings were as follows:

- Senior Manager accountability: Stakeholders expressed concern that the line between non-executive and executive could become blurred. The FCA clarified that it is not seeking to redefine the roles of non-executives. The FCA sees the oversight role of non-executive directors and their ability to challenge management as a key safeguard for the interests of firms' stakeholders. However, the FCA stated that, especially in larger firms, the responsibilities of SMF non-executive directors will often be considerable.
- Senior Managers also expressed concern about understanding the meaning of 'reasonable steps' in the context of their business. The FCA explained that it expects that Senior Managers should be doing what they reasonably can to prevent misconduct, an important part of which is to think more broadly and to create an environment where the risk of misconduct is minimised, for example through nurturing a healthy culture.
- Certification: The FCA reported that evidence indicates that firms have implemented processes to oversee the certification population, which include a broadened approach to assessment of staff beyond solely technical skills. However, the FCA expressed concern that most firms are not able to demonstrate the effectiveness of their assessment approach. There is no evidence that firms have made significant changes to their performance assessment processes other than incorporating expected behaviours.

- Regulatory references: Stakeholders felt that the industry had some way to go to improve the quality and timeliness of references, which is important in ensuring that those with poor conduct records are not simply able to move from one job to the next. There is also concern that firms are not always consistent in recording breaches of the Conduct Rules.
- Conduct Rules: The FCA flagged that firms have not always sufficiently tailored their conduct rules training to individuals' roles. Notably firms are often unable to explain what a conduct breach looks like in the context of their business. The FCA emphasised that the Conduct Rules are a critical foundation for firms' culture and the conduct of individuals. It is essential that staff understand the rules and their application. Firms must provide suitable training.
- Impact on culture: Firms described a stronger tone and ownership from the top, and that there was a change in the level of detail, clarity and quality of conversations on culture and expected behaviours. The view is that the regime is having an impact on the mind-set of Senior Managers.
- Unintended consequences: For most firms, SMCR has not led to significant unintended consequences. Some firms stated that there was a culture of fear during the early days of implementation that has now largely dissipated. There is some indication that firms are being more risk averse and considered around innovation initiatives. The FCA thinks that, if firms get the balance right, this is not a negative outcome. Firms also highlighted the additional staff and work required to administer the regime. However, this was seen by many as part of creating a robust governance environment within their firm.

Key next steps for private equity and venture capital firms

With just under a month to go until the application of the SMCR (which applies from 9 December 2019), there are a number of key steps that firms should be taking to ensure that they are ready.

In particular, it is important that firms:

1. appropriately categorise their staff;
2. allocate prescribed responsibilities and produce statements of responsibilities;
3. complete any necessary FCA filings;
4. provide training to staff; and
5. update compliance documents and other relevant documents.

These actions are discussed in more detail below. For these purposes, we have assumed that most private equity firms will be "core firms" under the SMCR.

Categorisation of staff

The SMCR splits staff into three broad categories (Senior Managers, Certification Staff and Conduct Rules Staff). The categories of staff are ordered from those subject to the most significant regulatory requirements, Senior Managers, to those subject to the least, Conduct Rules Staff. The level of accompanying regulatory requirements is intended to be proportionate to the amount of harm the individuals could cause in their respective roles. As the regulatory requirements for each category of staff are different, it is important to categorise staff as a first step.

Prescribed Responsibilities and statements of responsibilities

Every Senior Manager must have a statement of responsibilities setting out their role and responsibilities. The FCA has explained that these statements should be brief and clear. The document is intended to provide transparency regarding the areas of the firm for which each Senior Manager has responsibility.

It is important that statements of responsibilities are accurate because each Senior Manager is subject to a “duty of responsibility”. This is the overarching responsibility of each Senior Manager for their individual area(s) of responsibility. The relevant Senior Manager could be held accountable for any breaches in their area, if they did not take “reasonable steps” to prevent or stop the breach. Prescribed Responsibilities are specific responsibilities set out by the FCA, which must be allocated to a Senior Manager. There are six Prescribed Responsibilities applicable to core firms. To the extent that a Senior Manager is allocated one or more of the Prescribed Responsibilities, this should be made clear in their statement of responsibilities.

FCA filings

Firms are not generally required to apply for re-approval for individuals who are currently approved under the Approved Persons Regime.

If an individual is not currently approved, or is to carry out additional functions following the introduction of the SMCR, the firm needs to submit a Form A in respect of the individual. This is likely to be of particular relevance in relation to the Chair function, as this was not a Certified Function under the Approved Persons Regime. Where a Form A is required, the individual’s statement of responsibilities should be filed alongside the form.

Additionally, where individuals currently carry out controlled functions under the Approved Persons Regime, but will not carry out corresponding Senior Management Functions under the SMCR, a Form C should be filed.

Training

Firms are required to have trained their Senior Managers and Certification Staff in relation to their responsibilities under the Conduct Rules by 9 December 2019. Firms will also be required to train Conduct Rules staff in relation to their obligations, but this does not need to be completed until 9 December 2020.

Updates to documentation

Firms will almost certainly need to make changes to their documentation to reflect the significant changes introduced by the SMCR, in particular, compliance manuals. Other documents which may require updating include the firm’s staff handbook and other policies allocating responsibilities or dealing with oversight within the firm.

05.

Regulatory Roundup

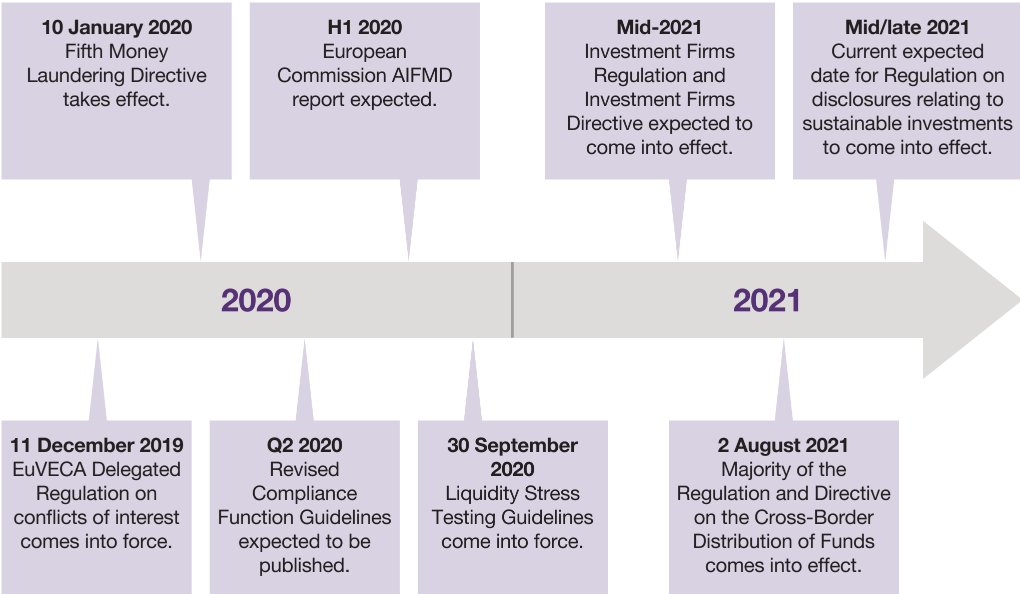
Tim Lewis and Stephanie Biggs (Travers Smith)

05. Regulatory Roundup

Tim Lewis
Travers Smith

Stephanie Biggs
Travers Smith

This note provides an overview of some of the main regulatory changes which will be relevant for BVCA members in 2020 and beyond.



Investment Firms Regulation/Directive

The new EU Regulation on prudential requirements for MiFID investment firms and the accompanying Directive (IFR/IFD) will introduce a bespoke regulatory capital, liquidity and pay regime for many MiFID investment firms, including portfolio managers and adviser/arrangers. This will replace, for those firms, the current regime under the Capital Requirements Directive and the Capital Requirements Regulation. IFR/IFD could also affect the own funds requirements for some EU alternative investment fund managers (AIFMs).

Regardless of Brexit, it is expected that IFR/IFD will be implemented in some form in the UK. The FCA will need to make implementing rules which will affect how these measures apply to UK firms. The BVCA is discussing this with the FCA on behalf of its members. Affected firms will need to start planning for implementation during 2020.

For some MiFID investment firms, IFR/IFD will mean higher regulatory capital requirements (subject to some transitional phasing-in). In addition, IFR/IFD will introduce a range of internal governance and disclosure and reporting requirements as well as new, more onerous remuneration rules based on those applicable to banks.

MiFID investment firms subject to IFR/IFD will generally need to comply with the following:

- Subject to transitional phasing-in, more onerous capital requirements (with portfolio managers and adviser/arrangers being required to hold own funds of a minimum of EUR 75,000 and liquid assets equal to at least one month's fixed overheads).

- Remuneration requirements in respect of persons having a material impact on the risk profile of the firm or the assets it manages or on which it advises, including requirements for a remuneration policy, the setting of appropriate ratios of variable remuneration to fixed remuneration and the application of mandatory deferral and malus and clawback arrangements for variable remuneration. Some of these requirements will not apply to firms meeting certain size criteria but it is not clear how useful this derogation will be in practice.
- A wide range of disclosure and reporting requirements including public disclosures about their capital, capital requirements, risk management objectives and policies, internal governance arrangements and remuneration policies and practices.

Depending on the application of transitional rules, some or all of these provisions may apply to adviser/arrangers from summer 2021.

Regulatory capital requirements as well as disclosure and reporting will apply on a solo (individual firm) basis and, unless a derogation can be used, parent undertakings will also need to apply those requirements to the group on a group-wide basis. This will be a particular change for adviser/arrangers.

MiFID investment firms which meet the requirements to be a "small and non-interconnected investment firm'" will only be subject to a more limited application of IFR/IFD.

For AIFMs and UCITS management companies, own funds will not be able to be less than the IFR's fixed overheads requirement – i.e. one quarter of the firm's fixed overheads for the previous year. It is not yet clear how this will apply to AIFMs or UCITS management companies with "top-up" MiFID permissions.

Finally, the new regime will also introduce a stricter framework for third-country (non-EU) firms seeking to rely on the equivalence provisions in the Markets in Financial Instruments Regulation.

Cross-border distribution of investment funds

The regime under the Regulation and Directive on the cross-border distribution of funds will introduce new standardised requirements for cross-border fund distribution in the EU as from 2 August 2021. The new regime will apply to certain fund managers including AIFMs and UCITS management companies. We focus on its application to AIFMs below.

New definition of "pre-marketing"

The new rules seek to harmonise the approach taken by different member states to pre-marketing activities by introducing a new definition of "pre-marketing". "Pre-marketing" is broadly information or communication by an AIFM (or on its behalf) relating to investment strategies or investment ideas to potential professional investors in order to test interest in an alternative investment fund (AIF) (or a compartment) which is not yet established or which is established but not yet notified for marketing.

Information is likely to be considered "marketing" rather than "pre-marketing" where it is sufficient to allow investors to commit to the AIFs; amounts to subscription documents in draft or final form, or amounts to final form constitutional or offering documents of a yet-to-be established AIF.

The AIFM will be required to send, within two weeks of the start of its pre-marketing, an "informal letter" with details of the pre-marketing to its home member state regulator.

Any third parties which the AIFM uses to pre-market on its behalf will have to be licensed as MiFID investment firms, EU credit institutions, AIFMs or UCITS management companies and will be subject to the same conditions which apply to the AIFM itself.

Any subscription by investors in units or shares of an AIF that takes place within 18 months of the pre-marketing will be considered to be the result of marketing and the applicable marketing notification procedures under the Alternative Investment Fund Managers Directive (AIFMD) will apply. This means that AIFMs will be unable to claim that subsequent investments can be considered to result from reverse solicitation.

Marketing to retail investors

AIFMs will be required, when marketing an AIF to retail investors, to put in place certain “facilities” in the relevant member state, e.g. paying agents.

Regulators may also require prior notification of marketing communications where an AIFM proposes to market to retail investors in a particular member state. Although this particular requirement is already in force, the FCA has not indicated to date that it intends to do so.

“De-notification” of Marketing

An AIFM may only discontinue the marketing of units or shares of an EU AIF in a jurisdiction in which it has exercised the marketing passport if certain conditions are met, including publicising its intention to cease its marketing activities and modification or termination of contracts with financial intermediaries or delegates with effect from de-notification.

For 36 months after de-notification, the AIFM will not be able to engage in any further pre-marketing of the relevant units or shares or of any “similar investment strategies or investment ideas” in the relevant member state. We expect market views to formulate on how to comply with this obligation in practice.

In addition, except for closed-ended AIFs or European Long-term Investment Funds, the AIFM must make a public offer to repurchase all the units or shares held by the investors in the relevant member state. Private equity AIFs are normally closed-ended AIFs so should not be impacted by this measure.

Even after de-notification, the AIFM must continue to provide investor transparency information (e.g. periodic reports) to investors on an ongoing basis.

Marketing communications

Additional requirements will also apply in respect of the content and presentation of fund marketing communications.

Sustainability initiatives

The next few years will see an increased focus on the integration of sustainability and environmental factors into financial services, both at EU and UK level.

As part of this, the EU authorities have been working on a range of measures including a Regulation on disclosures relating to sustainable investments and sustainability risks and also the integration of sustainability risks and factors. The UK government has also announced its own green initiative.

Regulation on disclosures relating to sustainable investments

The draft Regulation on disclosures relating to sustainable investments and sustainability risks is currently going through the EU legislative process. This Regulation applies to portfolio managers, AIFMs and UCITS management companies as well as investment advisers and introduces transparency requirements for those persons including:

- Disclosures (on the relevant website) regarding:
  - Policies for the integration of sustainability risks in decision-making and advisory processes.
  - How any remuneration policies are consistent with the integration of sustainability risks.
  - Whether the firm considers the principal adverse impacts of investment decisions on sustainability factors.
  - Whether the firm considers the principal adverse impacts on sustainability factors in its advice.
- Pre-contractual disclosures of how sustainability risks are integrated into decisions or advice and the likely impact of sustainability risks on investment returns.
- Where a product seeks to promote environmental or social characteristics or has certain sustainability objectives, disclosure of how these are met.

Although most of the Regulation is expressed to come into force in mid to late 2021, industry associations have requested that this be pushed back to at least one year after the implementing legislation is adopted.

Integration of sustainability risks and factors

The European Securities and Markets Authority (ESMA) has issued technical advice in respect of potential legislation on the integration of sustainability risks and factors (including, in certain cases, environmental, social and governance considerations) (Sustainability) into firms' policies and procedures.

The proposals apply to MiFID investment firms (including portfolio managers and adviser/arrangers) and AIFMs and UCITS management companies. In some cases, the proposed requirements would also apply indirectly to the manufacturers of funds (including non-EEA funds), particularly where making use of an EU distributor subject to MIFID.

Under the proposals, such firms would be required to take Sustainability into account in their organisational measures including (where relevant) risk management, conflicts of interest and product governance requirements.

AIFMs and UCITS management companies would also need to integrate Sustainability into the responsibilities of senior management and consider Sustainability when selecting and monitoring investments.

It is anticipated that the European Commission will take further action on this leading ultimately to amendments to MiFID II, AIFMD and the UCITS Directive.

UK Green Finance Strategy

In July 2019, the UK Government launched its "Green Finance Strategy" which aims to create a greener financial system which supports cleaner and more environmentally sustainable investment and growth. The Government intends that climate and environmental factors be fully integrated into mainstream financial decision-making across all sectors and asset classes.

As part of this, the Government has announced a number of measures including the establishment of the Green Finance Institute to collaborate between the private and public sectors with respect to green finance.

The government has also committed at least to match the ambition of the three key objectives of the EU's Sustainable Action Plan:

- To reorient capital flows towards sustainable investment.
- To manage financial risks from climate change by considering environmental and social goals in financial decision-making.
- To increase transparency in financial products so customers can make informed decisions about their investments.

Finally, the government also stated that it intends to require the PRA and FCA to have regard to the COP21 Paris Agreement when considering their objectives and discharge of their functions and would seek to establish a joint taskforce with UK regulators to ensure a co-ordinated approach on climate-related financial issues (including disclosures).

Money Laundering Directive V

The fifth Money Laundering Directive (MLD5) is due to take effect from 10 January 2020. It will be implemented in the UK by way of changes to the Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017 and HM Treasury has consulted on its proposed amendments.

The main change for most BVCA member firms will be the stricter requirements when carrying out customer due diligence. Many firms will already carry out the necessary steps as part of their current processes.

This includes a requirement for firms subject to MLD5, when carrying out customer due diligence on a body corporate, to identify and verify the relevant governing law, its constitution and the full names of directors and senior management. Firms will also be required to understand the business, ownership and control structure of their customers and to collect proof of registration on any beneficial ownership register. Firms will be required to report any discrepancies they discover between the information they hold and the information on the Register for People with Significant Control which has the potential to be a disproportionately onerous obligation.

In addition, firms will be subject to a requirement to refresh customer due diligence on existing customers in certain cases and apply enhanced due diligence to business relationships or transactions "involving" high risk third countries (rather than just in cases where persons are "established" in high risk third countries).

Firms subject to MLD5 which are part of a group will have to have policies requiring customer, account and transaction information to be provided to them from their branches and subsidiaries. Finally, additional requirements also apply in respect of express trusts.

EuVECA Delegated Regulation on conflicts of interest

Delegated Regulation (2019/820) on conflicts of interest applicable to European venture capital funds (EuVECA) comes into force on 11 December 2019.

This Delegated Regulation includes guidance on what constitutes a conflict of interest; a requirement for managers of EuVECA to establish, implement and maintain a written conflicts of interest policy, and a requirement to take steps to prevent and manage conflicts of interest.

Managers of EuVECA must also develop strategies for determining when and how to exercise voting rights held in the portfolio for the benefit of both the EuVECA and its investors. These must include the monitoring of corporate actions; ensuring that the exercise of voting rights is in accordance with the investment objectives and policy of the fund, and prevention and management of any conflicts of interest arising from the exercise of those voting rights. Investors must also be provided with a summary description of those strategies and the details of any resulting actions taken.

Liquidity stress testing

ESMA published its final guidelines on liquidity stress testing (Liquidity Guidelines). These principally apply to AIFMs and UCITS management companies but they do also impose a verification obligation on depositaries.

Liquidity stress testing (LST) is a risk management tool which simulates a range of conditions, including normal and stressed conditions, to assess their potential impact on the funding, assets and overall liquidity of a fund and any necessary follow-up actions.

The Liquidity Guidelines include obligations to design and build LST models and to produce an LST policy. They also impose governance principles which require LST to be properly integrated and embedded into a fund's risk management framework and subject to appropriate governance and oversight. LST should employ historical scenarios, hypothetical scenarios and, where appropriate, reverse stress testing.

Under the Liquidity Guidelines, LST should occur at least annually but quarterly or more frequent LST is recommended.

Depositaries must have appropriate verification procedures to check that fund managers have documented LST procedures in place.

The Liquidity Guidelines will apply from 30 September 2020.

Compliance Function Guidelines

ESMA issued a consultation paper on an update to its guidelines on the MiFID II compliance function (Compliance Guidelines). The final Guidelines are expected to be issued in the second quarter of 2020.

These apply to MiFID firms and to AIFMs when providing MiFID investment services. They are also now expressed to apply to product governance arrangements.

Under the proposed Compliance Guidelines, all compliance staff should have appropriate skills, knowledge and expertise and the compliance officer must demonstrate high professional ethical standards and personal integrity. The firm's compliance culture should also be supported by senior management. If appropriate and subject to proportionality, firms should consider having a core team focussing solely on MiFID II compliance.

The proposed Compliance Guidelines also state that firms should put in place arrangements for an effective exchange of information between the compliance function and other functions e.g. auditors or risk management.

Review of AIFMD

The European Commission commissioned a review, by KPMG, of AIFMD and its original objectives which was published in December 2018. The review concluded that, for the most part, the EU's objectives had been achieved and remained relevant.

The review, however, also highlighted some areas of AIFMD where some issues potentially remain including the reporting regime, the calculation of leverage, disclosures to investors and the marketing passport.

The European Commission is therefore carrying out further work on this. Current indications are that a consultation paper will be issued in early 2020 with a view to publishing a report during the first half of 2020. In due course, this may result in further AIFMD legislation and possibly even AIFMD II.

06.

DAC6: An Update for the Investment Fund Industry

Jenny Wheater (Linklaters)

06. DAC6: An Update for the Investment Fund Industry

Jenny Wheater
Linklaters

Introduction

On May 25, 2018, Council Directive (EU) 2018/822 ("DAC6") was published and caused some understandable disquiet within many industries, including that of investment funds. Although, in the UK, common parlance initially referred to DAC6 as "EU DOTAS" with the implication that, as is the case with the UK's Disclosure of Tax Avoidance Schemes ("DOTAS") regime, it was drafted so as to target tax avoidance arrangements only, it quickly became apparent that this was a misleading moniker and that compliance with DAC6 would involve a much wider set of considerations and reporting obligations than is the case under DOTAS. The most recent development in this area is the publication by HMRC, on 22 July 2019, of a consultation document and draft regulations implementing DAC6 in the UK. The BVCA has responded to these and has been involved in additional discussions with HMRC and HM Treasury, with our concerns currently being considered. However, it will remain the case that DAC6 demands the ongoing attention of BVCA members as matters develop and that, even with favourable changes, its implementation in the UK will result in further obligations on in-house professionals and external advisers alike.

DAC6 Recap

DAC6 entered into force on 25 June 2018, and will require "intermediaries" (see below) and, in some cases, taxpayers to report details of certain "cross-border arrangements" (see below) to HMRC and other EU tax authorities. Member States must implement DAC6 by 31 December 2019 and first reports, due in July/August 2020, will need to include all reportable arrangements implemented from 25 June 2018.

A cross-border arrangement is an arrangement that concerns more than one Member State, or that concerns a Member State and a third country. These arrangements are reportable only if they have certain "hallmarks." The hallmarks are grouped under five broad categories, A – E. A "main benefit" test must be satisfied for any arrangement for hallmarks under categories A, B and subcategories 1(b)(i), 1(c) and 1(d) of category C to apply. It does not have to be satisfied for arrangements under any of the other hallmarks. This is a key distinction from the UK's DOTAS regime in which a similar test is of universal application.

The main benefit test will be satisfied if it can be established that the main benefit or one of the main benefits which, having regard to all relevant facts and circumstances, a person may reasonably expect to derive from an arrangement is the obtaining of a tax advantage. The term "tax advantage" is defined in Regulation 12 and it should be noted that:

- the main benefit of an arrangement will not include the obtaining of a tax advantage if the tax consequences of the arrangement are entirely in line with the policy intent of the legislation upon which the arrangement relies; and
- tax does not only include taxes levied by EU member states, but also equivalent taxes levied in other jurisdictions. This means that the regulations can apply to a tax advantage realised in a non-EU member state.

The hallmarks are as follows:

- Category A (1)-(3): the "generic hallmarks" (confidentiality, remuneration related to a tax advantage and standardised documentation);
- Category B (1)-(3): loss buying, income into capital and circular transactions;

- Category C (1)-(4): deductible cross border payments, depreciation, relief from double taxation and transfer of assets;
- Category D (1)-(2): undermining reporting obligations and obscuring beneficial ownership (including under FATCA or CRS); and
- Category E (1)-(3): unilateral safe harbours, hard-to-value intangibles and cross-border transfers.

Typically, it is anticipated that "intermediaries" will undertake most of the reporting obligations since the primary reporting obligation falls on such parties. An intermediary is defined in DAC6 as including any person that designs, markets, organises, makes available for implementation or manages the implementation of a reportable cross-border arrangement. An intermediary also includes any person who provides (directly or indirectly) services in relation to a reportable cross-border arrangement if it is, in all the circumstances, reasonable for the service provider to know that the arrangement is reportable. Evident examples of intermediaries include tax advisers, accountants and lawyers advising clients on reportable cross-border arrangements. Additionally, since there is no exclusion for in-house advisers, an entity within a fund structure which is not the actual taxpayer could well be regarded as an intermediary in certain circumstances.

There are some limitations on the scope of the term "intermediary" in the context of certain service providers, given the requirement for knowledge that an arrangement is reportable. DAC6 states that this test depends upon the circumstances, information available and expertise of the person in question. It may be unreasonable to expect certain providers of administrative or compliance services to know that the arrangement is reportable.

Jurisdiction is another factor in identifying intermediaries. For an intermediary to have a reporting obligation, they must be resident for tax purposes or provide the relevant services in a Member State. This means that a non-EU advisory firm would be within the scope of the DAC6 regime if it were providing advisory services in an EU Member State.

Where there is more than one intermediary, the obligation to report lies with all the intermediaries involved in the arrangements. An intermediary may, however, be exempt from filing information to the extent that it has proof that this information has already been filed by another intermediary. Where there is no EU intermediary (or the EU intermediary is a lawyer whose advice benefits from legal professional privilege), the obligation to report the cross-border arrangement then passes to the taxpayer, if resident in the EU.

HMRC consultation process, BVCA representations and remaining issues

As stated above, HMRC published its proposed implementation of DAC6 together with consultation in July 2019. Clearly, it needs to be acknowledged that DAC6 must be implemented in accordance with its drafting and purpose so that there are certain areas where HMRC has little flexibility. However, the BVCA has noted that there is still scope for the UK proposals to operate in a more appropriate and targeted way than is currently suggested in the consultation and draft regulations and guidance.

Multiple reporting

A typical cross border fund transaction or fund establishment will involve a number of potential intermediaries in the form of legal, accounting and other specialists and, potentially, a number of entities within the fund in question. When the implementation of DAC6 in the various EU jurisdictions is taken into account, the likelihood of same subject matter being reported on more than one occasion is significant. HMRC acknowledge the undesirability of this in their consultation. However, there remains scope for a more helpful position in what they have thus far suggested.

HMRC proposals require intermediaries to have a scheme reference number from another intermediary to avoid the need to make a further report on substantially the same subject matter. Since there is flexibility in DAC6 on the timing of reports, it may be that the most appropriate intermediary to make the report does not, under their domestic law, need to make it until a later point in time. This would mean that a reference number would be unavailable and a further report would also be required in the UK. In addition, the HMRC consultation requires intermediaries to ensure that all information is captured in any report made by another intermediary, effectively meaning that all intermediaries are required to review the reports of others to ensure all information has been properly reported. This is, at best, significantly burdensome and, at worst, will mean that additional reports are automatically necessary on the basis that one intermediary may not even be given access to the report of another, leaving them with no choice but to file an additional report. Since DAC6 does offer flexibility in this area, requiring only proof in accordance with national law that a report has been filed, a different approach in this area is possible and it is hoped that HMRC can be persuaded to amend their proposals so that intermediaries need merely obtain written confirmation that another intermediary has or intends to file a report relating to the same subject matter. This would be a helpful move to reduce the compliance burden.

The BVCA has raised the foregoing issues with HMRC. It is especially noteworthy that in-house professionals in funds, already burdened with increasing technical obligations, will, potentially, be required to spend time reviewing the reports of all intermediaries on a transaction in which they are involved. It would be preferable if this could be avoided.

Penalties

DAC6 gives discretion to Member States in the area of penalties and the penalty regime proposed by HMRC would appear to be disproportionately punitive and not effectively targeted, especially given the inherent ambiguity within DAC6 as to whether a hallmark is met and a report is even required. The penalty regime is not only significant in terms of amounts but is applied on a strict “failure to comply” basis which will, inevitably, result in absurdly conservative approaches to the reporting process. HMRC are, understandably, concerned to ensure that any penalty regime operates as a suitable deterrent, but the BVCA has made it clear that they consider the current proposals to be excessive and not properly directed at those who carelessly or deliberately flout the rules.

The BVCA has recommended a clear exemption or “reasonable excuse” from penalties for those able to demonstrate that they had in place appropriate procedures to address reporting compliance In addition, we have suggested that penalties should not be based on strict “day counting” with reference to the number of unreported transactions. This approach could easily lead to disproportionate penalties being imposed if a reasonable “judgment call” is erroneous, especially if technically multiple, but very similar, transactions are affected. Further, we have asked that HMRC review the provisions relating to the obtaining of legal advice. Currently, reliance cannot be placed on legal advice provided by an intermediary involved in the arrangement. There is no reason to suppose that legal professionals are subject to lower standards of care as result of their involvement and there are ample professional safeguards in relation to e.g. conflict of interest to ensure that such professionals remain impartial. In addition, those receiving legal advice should not, as is proposed by HMRC, be responsible for determining whether conclusions in relation to such advice are "unreasonable" or not. Accordingly, we have asked that this reference should be deleted.

Concept of made available

The obligation to report an arrangement arises when it is "made available" for implementation. The issues with the interpretation of this as set out in the HMRC proposals are twofold. First, the notion is too broadly drafted; second, it is focused on "promoted" schemes, unlikely to be of much relevance to the investment fund industry, where the regime is more likely to apply in the context of an initial fund establishment, subsequent acquisitions or exits and, technically, the day to day running of a fund itself in the form of e.g. cross border payments to investors.

In this area, it is useful to make a comparison between the HMRC proposals in implementing DAC6 and those in the DOTAS legislation. While the wording of "made available" is the same, the interpretation suggested in the DAC6 consultation differs from that in the DOTAS guidance. Under DOTAS, for a scheme to be made available, such scheme needs to be fully designed and capable of being implemented. This is materially different to consultation which states that, for DAC6 "the full details do not need to be finalised, as long as the essence of the arrangement is identifiable." This difference is not necessary for the proper implementation of DAC6 and could result in several issues, to which the BVCA have alerted HMRC.

Arrangements which involve discussions between e.g. a UK fund house and their advisers may, given the proposed DAC6 interpretation, give rise to the need for a report at a very early stage. Early discussions of potential structuring options could need to be disclosed in a report identifying the relevant fund and the cross-border arrangement. This would potentially need to be made ahead of any action being taken by a fund to proceed with an arrangement so that a report naming a fund might be made despite such fund actively declining to engage in the arrangement. Funds might be legitimately concerned about being associated with arrangements they have no intention of implementing. Given these potential consequences and the existing interpretation of the same concept in the DOTAS rules, we have suggested that the DAC6 guidance mirrors that of DOTAS so that the obligation to disclose does not arise at an inappropriately early time.

In addition, there should, it seems, be greater clarity on when non-promoted arrangements are considered "made available" for implementation. In terms of common fund situations, this would most likely involve examples in any HMRC guidance, although, obviously, it is generally preferable not to need to rely on non-binding guidance. For example, a new fund structure might involve a cross border arrangement and it would be helpful to receive confirmation of whether this might become reportable at the point of establishment or when investors make their initial investments. Equally, in relation to an acquisition transaction, would this be "made available" when structure papers are circulated or when the agreements are signed? We have requested that HMRC consider these suggestions.

Jurisdictional scope of tax advantage

We consider that the proposed extra-territoriality of the HMRC proposals applying to non-EU tax advantages is disproportionate and could have an adverse impact on the competitiveness of the UK as a place to do business, with non-EU businesses being brought within the scope of the rules by virtue of doing business with a UK entity. This kind of competitive disadvantage is not something which the UK can afford to introduce at this point in time.

From the introductory text of DAC6, it is clear that its purpose is to protect the national tax bases of Members States from erosion. This point is elaborated upon stating that it is "critical that Member States' tax authorities obtain comprehensive and relevant information about potentially aggressive tax arrangements". Bearing in mind the nature of DAC6, this purpose envisages a "tax advantage" (which falls within one of the hallmarks) should only be considered if it relates to a "tax advantage" arising in an EU Member State. We have, accordingly, urged HMRC to review its position on this.

Other

There are additional elements of HMRC's proposals which we consider could benefit from further review and we have also raised these. Examples include the desirability of including as much as possible in actual legislation as opposed to guidance. Already, the investment fund industry is required, given the breadth of legislation in other areas, to focus too much on HMRC guidance, which can be changed at any time and which does not have statutory footing and thus cannot, technically, be relied upon. It would be preferable if, in this area at least, the industry can look to actual legislation. Additionally, specific areas such as the confidentiality hallmark warrant further review, since the current proposals do not focus sufficiently on the rationale behind any confidentiality. Furthermore, there is some lack of clarity as to the obligations of individual LLP members in LLP structures and some equal lack of clarity on what might constitute "knowledge", especially in larger entities where information might be known or available to some, but not others. We have requested that HMRC look into these points.

Brexit

It is difficult to consider implementation of EU measures without correspondingly considering the impact of Brexit. Currently, the consultation states that the UK will remain committed to international tax transparency, notwithstanding its intention to leave the EU. This is neither unexpected nor controversial. However, no information is given as to how exchanges of information between HMRC and other EU tax authorities under DAC6 will operate in a post-Brexit world. This is somewhat unsatisfactory, given the amount of preparation necessary to comply with these new measures, but, in all fairness, it is unlikely that HMRC has sufficient information to assist on this point.

Next steps

It would be prudent to assume that DAC6 will be implemented in some form, notwithstanding Brexit and preparations should be made on that basis. Industry professionals need to ensure that all relevant departments within their organisation are aware of what might be reportable so that analysis can be made on what to include in initial reports. It might also be worth working with potential service provider intermediaries to try and ensure, as far as possible under the current rules, that multiple reports are not filed. There may be reason for optimism in that many of the issued identified above have been raised by other industries as well as by the BVCA and HMRC will, accordingly, be reviewing their position. Equally, Brexit could alter the landscape significantly. However, it is wise to be cautious.

07.

The "Failure to Prevent the Facilitation of Tax Evasion Offence": time for a refresh of prevention procedures

Russell Warren (Travers Smith)

07. The “Failure to Prevent the Facilitation of Tax Evasion Offence”: time for a refresh of prevention procedures

Overview

Russell Warren
Travers Smith

Two years on from the enactment of the Criminal Finances Act 2017 and the “failure to prevent the facilitation of tax evasion” offence (the “FTP Offence”), HMRC has confirmed that it has begun its first investigations into potential offences under these provisions. The number of investigations so far is surprisingly low, perhaps due to resourcing constraints and the time-consuming nature of such enquiries, nevertheless this is a timely reminder for businesses to refresh their policies and procedures.

The FTP Offence makes body corporates or partnerships (“relevant bodies”) criminally liable if they fail to prevent the criminal facilitation of tax evasion by their associates. This is a strict liability offence and the only defence is to demonstrate that either (a) they had in place “reasonable prevention procedures” or (b) it was reasonable to have no such prevention procedures in place.

The offence is similar in structure to offences under the Bribery Act 2010 and many relevant bodies have tied their prevention of the facilitation of tax evasion procedures into their existing compliance regime. It may be desirable to coordinate updates to risk assessments, policies and procedures across both offences, however it is important that firms are able to demonstrate how policies and procedures have been tailored to address tax facilitation risks.

Maintaining “Reasonable Prevention Procedures”

When the FTP Offence was first enacted, relevant bodies were expected to undertake a risk assessment of their business and to use this to inform policies and procedures designed to prevent their associates from criminally facilitating tax evasion.

HMRC’s guidance is clear that risk assessment cannot be a “one-off” event. Instead relevant bodies are expected to regularly review the risks faced by their business and update their policies to mitigate those risks.

The HMRC guidance does not specify how frequently businesses should update their risk assessments, instead noting that this should be informed by the level and nature of risks faced by the business. Firms with higher risk profiles, and particularly those operating in areas where the business model or the nature of risks faced by the business are swiftly changing, are expected to update their risk assessments more frequently than low risk firms with a consistent risk profile.

Two years on from the enactment of the FTP Offence, BVCA members may wish to consider updating their risk assessments to the extent that a review has not already been completed.

Factors relevant bodies may wish to consider when updating their risk assessments include:

- Changes to their business model including:
  - new products or services;
  - new jurisdictions targeted by the business either directly or through local agents;
  - newly created roles for employees – consider whether these roles provide employees with the means, motive and opportunity to facilitate tax evasion; and
  - newly formed or acquired portfolio companies and subsidiaries.
- Changes to the business of associates, such as agents and contractors. Consider whether any due diligence should be refreshed, particularly for associates identified as higher risk.

- Any whistleblowing reports received since the implementation of prevention policies or any breaches of policies and procedures that have been identified since the last review.
- Changes to published guidance. HMRC’s guidance has not been updated since 2018 however relevant bodies should ensure that they have considered any guidance issued by relevant industry bodies.

To evidence the existence of reasonable prevention procedures, the process of updating the risk assessment should be clearly documented. Changes to the risk assessment should then inform amendments to policies and procedures to address any new or increased risks identified.

Examples

“Marketing Co.” acquired a new bolt-on subsidiary “Survey Co.”, which runs surveys on behalf of Marketing Co.. At the time of the acquisition Marketing Co. required Survey Co. to adopt Marketing Co.’s existing group-wide FTP policy. Without Marketing Co.’s knowledge, Survey Co. agrees to attribute an incorrect level of profit to a connected company “Data Co.” in relation to work on behalf of Marketing Co. so that they can evade paying corporation tax.

In this example Data Co. deliberately evaded corporation tax and Survey Co. knowingly facilitated that tax evasion. Survey Co. is likely to be an associate of Marketing Co. and so Marketing Co. may need to rely on the reasonable prevention procedures defence. Whether or not their prevention procedures were reasonable may depend on a number of factors including whether Marketing Co. updated the group’s risk assessment to include specific consideration of Survey Co.’s business and risk profile, rather than simply applying a generic set of group-wide policies to the new subsidiary.

“PE House” engaged with a third-party contractor to provide cleaning services two years ago. Due diligence at the time of the engagement flagged that this was a higher risk area due to the use of “cash-in-hand” workers. Six months ago, a news report was published highlighting that the contractor was under investigation for tax evasion. Cleaners working for PE House were paid in cash to allow them to evade tax.

Again, the PE House may well need to rely on the reasonable procedures defence. To give the best possible arguments that prevention procedures were reasonable, the PE House will want to be able to demonstrate not only that it had undertaken initial due diligence in relation to the contractor but also that due diligence was refreshed within an appropriate timescale given the risk level identified. There is no requirement for due diligence to be refreshed after a particular interval, and so it may be reasonable for the PE House not to have identified the news report, however the PE House should have documentation evidencing an appropriate review schedule, influenced by its assessment of the risks.

“Food Group” has recently brought its payroll function back in-house. A member of the new accounts team agrees to pay a senior employee via a UK subsidiary rather than the US trading subsidiary to assist the senior employee to evade US taxes on his income.

A member of the accounts team has knowingly assisted another employee to evade US taxes. To give the best possible argument for a reasonable prevention procedures defence, Food Group will want to be able to demonstrate that it performed a risk assessment of the new roles within the accounts department (considering the means, motive and opportunity the new employees had to facilitate tax evasion), and that it put in place appropriate, risk driven procedures to mitigate the risks identified.

Additional points to consider

Relevant bodies were expected to provide training to employees on the FTP Offence, appropriate to the level of risk associated with the employee’s role within the business. Relevant bodies may wish to consider how often employees, particularly those in high risk areas, should be given refresher training. Relevant bodies should also ensure that new employees have received appropriate training as part of the onboarding process.

The HMRC guidance emphasised that HMRC expected relevant bodies to demonstrate top level engagement with the new policies and procedures, with relevant bodies expected to give a “zero tolerance” message to their associates. BVCA members may wish to consider asking a senior employee or board member to circulate a reminder about the offence and the relevant body’s zero tolerance approach.

For an in-depth summary of the legislation and an overview of the guidance received by the BVCA from HMRC please see the BVCA website[22].

[22] https://www.bvca.co.uk/Policy/Tax-Legal-and-Regulatory/Matters-on-our-agenda/Taxation/Failure-to-prevent-the-facilitation-of-tax-evasion-offence

08.

Jargon Buster

Amber-Leigh Furnell (BVCA)

08. Jargon Buster

The BVCA's technical committees and policy team work on a wide range of regulatory, taxation, reporting, accounting and legal issues. We are conscious that in some policy areas many acronyms are used and for the benefit of our members, some of these are defined below. We have also included various organisations and stakeholders we work with regularly.

Amber-Leigh Furnell
BVCA

Key topics	
Regulation	
AIFMD	**Alternative Investment Fund Managers Directive** AIFMD is an EU directive that regulates a wide range of areas such as the operation, reporting and marketing of alternative investment funds. It took effect in July 2013 and remains the primary piece of regulation effecting the private equity and venture capital industry. It mainly applies to Alternative Investment Fund Managers (AIFMs) with total assets under management that do not exceed €500 million (for unleveraged and closed-ended funds) and allows authorised AIFMs to use a European Economic Area (EEA) passport to market and manage funds in other EEA countries. The European Commission recently agreed an amendment, through a new regulation on marketing, which will impact pre-marketing of funds for EU AIFMs in 2021. The AIFMD is currently under review by the European Commission.
AMLD V	**Fifth Anti-Money Laundering Directive** This is an EU directive for financial institutions and regulated firms to prevent, detect and report money laundering activities. The fifth directive extended the requirement to virtual currencies, such as cryptocurrencies, requires self-regulated bodies to publish an annual report about compliance monitoring, and public bodies are required to publish information on risks identified and their response. It is expected to be written into UK legislation in early 2020.
CRD	**Capital Requirements Directive** The CRD is an EU Directive that introduced a supervisory framework establishing rules on capital measurements and standards, in response to concerns about financial stability following the latest banking crisis. It has also made changes to rules on corporate governance and introduces standardised EU regulatory reporting.
ESG	**Environmental, Social and Governance** ESG is an area that is high on regulators agendas due to increasing expectations on fund managers to consider and report on ESG matters as part of their management activities during the life of the fund. The includes looking at policies, processes and systems in place.

LIBOR	**The London Interbank Offered Rate** LIBOR is a benchmark interest rate at which major global banks lend to one another for short-term loans. It is based on five currencies including the US Dollar, the Euro, the British Pound, the Japanese Yen, and the Swiss Franc and serves seven different maturities—overnight/spot next, one week, and one, two, three, six, and 12 months. LIBOR is also the basis for consumer loans in countries around the world, so it impacts consumers just as much as it does financial institutions. LIBOR is being replaced in 2021 as part of reforms to reference rates.
MiFID II	**The Markets in Financial Instruments Directive II** This is an EU directive that governs: the provision of investment services in financial instruments by banks and investment firms; and operation of traditional stock exchanges and alternative trading venues. MiFID II applies to UK private equity and venture capital managers who are regulated as investment firms or advisers and use passports to provide their services in the EU.
PRIIPs	**The Packaged Retail Investment and Insurance Products Regulation** This is an EU regulation that impacts private equity and venture capital funds when they are marketed to retail investors. The product must include a Key Information Document (KID) and this should provide clear information for retail investors to better understand the risks associated with an investment.
SII	**Solvency II** Solvency II is an EU directive that sets out regulatory requirements for insurance firms and groups, covering financial resources, governance and accountability, risk assessment and management, supervision, reporting and public disclosure.

Tax	
ATAD I & II	**Anti-Tax Avoidance Directive I and II** ATAD I is an EU directive that implements the Organisation for Economic Co-operation and Development’s BEPS project. It sets the minimum standards for EU countries and requires them to change corporate tax law. It introduced five measures including, hybrid mismatch provisions between EU jurisdictions. Most of the rules applied from January 2019 and ATAD II aims to extend the scope of to include hybrid mismatches involving non-EU countries, from January 2020. It is likely to impact how alternative investment funds, and their investments, will be structured.

BEPS	**Base Erosion and Profit Shifting Project** BEPS is an international tax initiative launched in 2013 by the Organisation for Economic Co-operation and Development (OECD) to combat tax avoidance by enterprises due to non-universal tax systems in different jurisdictions. The actions of interest to private equity funds cover limiting base erosion involving interest deductions and preventing abuse of treaty benefits.
CRS	**Common Reporting Standard** CRS is an international standard approved by the OECD for the purpose of combatting tax avoidance. It requires jurisdictions to obtain information from financial institutions in the country and automatically exchange the data with other jurisdictions, annually. The CRS sets out the type of information to be exchanged, the institutions required to report, the taxpayers it affects and the due diligence procedures to be followed. The United States does not participate in the CRS, but has it's own similar rules under FATCA, see page 52.
DAC6	**Directive on Administrative Cooperation 6** DAC6 is the most recent amendment to the EU Directive on Administrative Cooperation directing all EU member states to share certain information on residents of other member states including employment income, directors' fees and pensions, for taxable periods starting after 1 January 2014. DAC6 introduces an obligation on intermediaries to disclose information on cross-border arrangements that have certain "hallmarks" to their domestic tax authorities and the subsequent exchange of this information between tax jurisdictions. This must be implemented before 31 December 2019 to be applied from 1 July 2020.
DOTAS	**Disclosure of Tax Avoidance Schemes** DOTAS is a procedure introduced by HMRC in 2004 to reduce tax avoidance. It requires companies to disclose the schemes they use to avoid tax. The types of tax covered by the DOTAS requirements include income and capital gains tax, corporate tax, stamp duty land tax, inheritance tax, value-added tax (VAT), and national insurance contributions.
DIMF	**Disguised Investment Management Fees** DIMF is a UK tax law, introduced in 2015, that seeks to tax any amounts arising to fund managers from the collective investment scheme funds they manage as fee income. This does not affect carried interest or returns on amounts invested as investors, through co-investment or GP commitment.

EIS	**Enterprise Investment Scheme** EIS is a tax relief scheme created by the UK Government to encourage investment into start-ups and early-stage businesses. It can offer significant income and capital gains tax reliefs and makes smaller companies for more attractive as an investment opportunity.
GAAR	**General Anti-Abuse Rule** The GAAR took effect from 17 July 2013 and is intended to deter tax advantages arising from tax arrangements that are abusive. The rules apply to a number of taxes. In addition to the legislation, HMRC published guidance in April 2013 that stated the GAAR's purpose was to improve the previous situation where court decisions allowing abusive tax advantages are now rejected. HMRC also created an advisory board, whose role is to determine if a tax arrangement is abusive by considering factors, such as whether the arrangement was intended to exploit shortcomings in the relevant tax provisions.
FATCA	**Foreign Account Tax Compliance Act** FACTA is a United States federal law endorsed in 2010 to promote transparency in global financial services. It requires all non-US financial institutions to search their records for customers with a connection to the US and reports the assets and identities of the individual to the US Department of the Treasury. It also requires US citizens to file annual reports on any foreign account holdings, as the US taxes all income and assets of citizens on a global scale.
IBCI	**Income-based Carried Interest rule** Like DIMF (above), IBCI applies to individuals who provide investment management services in relation to collective investment schemes or investment trusts. If any part of carried interest is deemed to be "income-based" it is then taxed as income under the DIMF regime. Carried interest is usually taxed as Capital Gains at 28%. Whether carried interest is "income based" depends on the average holding period of an investment scheme at the time the carried interest is paid. If the average holding period is 40 months or more, then the carried interest will not be "incomised" under these rules. If the holding period is less than 36 months, then it will all be included and if the holding period is between 36 and 40 months, then part of it will be.
JSOP	**Joint Share Ownership Plan** A JSOP involves the acquisition of joint shares and is a flexible employee incentive arrangement that can be used by listed and privately held companies, and tailored to meet specific requirements. The employee jointly acquires shares with a third party, usually an employee benefit trust (EBT). The ownership of the shares is structured such that the employee pays a small upfront payment and is entitled to the subsequent growth in share value which will be subject to capital gains tax.

Non-CIV	**BEPS: Non-Collective Investment Vehicle** Non-CIV is the term used by the OECD BEPS Project to refer to the wide variety of private equity and other alternative investment fund products, pension funds, and similar institutional funds that do not meet the OECD's strict criteria for "collective investment vehicles" - funds that are widely held, own a diversified portfolio of securities, and are themselves subject to investor-protection regulation i.e. UCITS.
SEIS	**Seed Enterprise Investment Scheme** SEIS is a tax relief scheme created by the UK Government to encourage investment in seed-stage start-ups that meet certain eligibility criteria. It allows investors to claim back investment through income and capital gains tax reductions. The main difference between the Enterprise Investment Scheme (EIS) and the SEIS is that SEIS is more focused on earlier-stage (seed stage) companies than EIS.
SITR	**Social Investment Tax Relief** A tax relief implemented by the Government which encourages investment to support specific social enterprises, such as charities, community interest companies or community benefit societies, to help them to access new sources of finance.
VCT	**Venture Capital Trust** A VCT is a type of publicity listed fund in the UK. It is designed as a way for individual investors to access venture capital investments through capital markets. It is managed by a fund manager and invests in small unlisted firms to generate higher, risk adjusted returns. It is popular with investors seeking to invest in a diversified portfolio. They carry tax relief to encourage investment in smaller, higher risk companies, but the risk can be spread across a number of smaller companies.

Legal	
CTI	**Corporate Transparency Initiative** The CTI is a new industry standard for institutional investment cost data. It consists of an advisory board, of which the BVCA is a member, aiming to promote understanding, raise awareness and encourage transparency and standardisation of costs and charges information for investors.
ESOS	**Energy Savings Opportunity Scheme** ESOS is a regulation that came into in 2014, and implements a requirement in the UK that large enterprises carry out an energy audit, a minimum of every four years. The aim is to assess where potential energy savings could be made.

MSA	**Modern Slavery Act** The Modern Slavery Act was introduced in 2015 and is designed to combat modern slavery in the UK. It contains a number of provisions, including consolidation of existing slavery and trafficking offences, and established an independent anti-slavery commissioner to encourage good practice on prevention. For PE/VC, section 54 about transparency in supply chains has the most impact. All obligated businesses (those with global turnover of £36m+, or carrying on a business in the UK) must publish a slavery and human trafficking statement each financial year and should outline steps taken to ensure these activities are not taking place in the relevant operations or supply chain.
PSC	**People with Significant Control** PSCs are indviduals within a company with either significant shareholdings or other means of control over the company. UK companies are required to keep a register of PSCs (PSC Register) in addition to a register of their executive and/or membership, and this must be shared with Companies House. The reason for the PSC register is to aid investors with analysing company structures, and also to aid law enforcement.

UK Government Bodies	
HMT	**HM Treasury** HMT is the government's economic and finance ministry. It is responsible for a number of policy areas that impact the private equity and venture capital industry, including financial regulation and taxation.
HMRC	**HM Revenue & Customs** HMRC is a non-ministerial department of the UK Government responsible for the collection of taxes, the payment of some forms of state support, and the administration of other regulatory regimes.
BEIS	**Department for Business, Energy and Industrial Strategy** BEIS is the government ministry responsible for business, industrial strategy, science, innovation, energy and climate change policy. The BVCA has worked with BEIS and its predecessor, BIS, on a number of areas, including company law, corporate governance, cutting red tape and the register of people with significant control.

BBB	**British Business Bank** The BBB is a government-owned bank, but independently managed, aimed at developing smaller businesses in the UK. It brings expertise and Government money to the smaller business finance markets. It does not lend or invest directly but works with partners such as banks, leasing companies and venture capital funds to enable small businesses to grow. Its investment subsidiaries include British Business Investments and British Patient Capital.
DExEU	**Department for Exiting the European Union** DExEU is responsible for coordinating and overseeing the UK's negotiations for leaving the European Union.
FCA	**Financial Conduct Authority** The FCA is the conduct regulator for the financial services industry in the UK, and the prudential regulator for those parts of the sector that are not regulated by the Prudential Regulation Authority, including private equity and venture capital.
PRA	**Prudential Regulation Authority** The PRA is part of the Bank of England. It is the prudential regulator for banks, building societies, credit unions, insurers and major investment firms.
FPC	**Financial Policy Committee** The FPC is part of the Bank of England responsible for identifying and monitoring systemic risks to the UK financial system, including levels of leverage and debt. It can make recommendations to the FCA and PRA to introduce changes to mitigate risks to the financial system.
FRC	**Financial Reporting Council** The FRC is the UK's independent regulator for promoting high quality corporate governance and reporting. The FRC sets standards for corporate reporting and audit practice, and it monitors and enforces accounting and auditing standards. It also oversees the regulatory activities of the professional accountancy bodies.

The European Union	
European Council	The European Council consists of the heads of government of the 28 EU Member States. It sets the general political direction of the EU and establishes its priorities by adopting "conclusions" following quarterly summits. It is not one of the EU's legislating bodies, and should not be confused with the Council of the European Union (see p56).

European Commission	The European Commission is the executive branch of the European Union. It has the sole power to initiate legislative proposals, which must be approved by both the European Parliament and the Council of the European Union (see below). While the Commission does not have the power to introduce or veto amendments to legislation, if it objects to amendments unanimity is required in the Council for the amendments to be adopted. This, along with the Commission's agenda setting power, makes it a key player in negotiations over EU laws.
Council of the European Union	The Council of the European Union is one of the European Union's two 'co-legislators', along with the European Parliament (see below). It consists of government Ministers from the EU Member States who meet to discuss, amend and adopt laws proposed by the European Commission (see above).
European Parliament	The European Parliament is, along with the Council of the European Union, one the EU's co-legislators. It is composed of 751 elected MEPs organised into 8 recognised political groupings. The Parliament can approve and amend proposals made by the Commission but must agree a final text with the Council in order for a proposal to become law.
Trialogue	Trialogues are informal meetings of representatives from the European Parliament, the Council of the European Union and the European Commission. They are used to agree amendments to legislation that are acceptable to all three parties.
ESAs	**European Supervisory Authorities** The European Banking Authority ("EBA"), the European Insurance and Occupational Pensions Authority ("EIOPA"), and the European Securities and Markets Authority ("ESMA") are the three European Supervisory Authorities. While national supervisory authorities remain in charge of supervising individual financial institutions, the ESAs aim to improve the functioning of the internal market by promoting harmonised European regulation and supervision by developing Level 2 regulation (secondary legislation) and guidance. They are accountable to the European Parliament and the Council of the European Union.
ESMA	**European Securities and Markets Authority** ESMA, based in Paris, is the ESA (see above) responsible for promoting stable and orderly financial markets. ESMA's remit includes markets and securities regulation, asset management and investor protection.
EIOPA	**European Insurance and Occupational Pensions Authority** EIOPA, based in Frankfurt, is the ESA (see above) responsible for the supervision of the insurance and pension sectors, and ensuing that policyholders are sufficiently protected.

EBA	**European Banking Authority** The EBA, based in London, is the ESA (see p56) responsible for the banking sector. Its overall objectives are to maintain the EU's financial stability and to safeguard the integrity, efficiency and orderly functioning of the banking sector.
RTS	**Regulatory Technical Standards** Level 1 (primary) legislation may empower the Commission to adopt technical standards in the form of RTS. The RTS are prepared by the relevant ESAs, and submitted to the Commission, which has 3 months to adopt the RTS or send them back to the ESAs for amendment. Once adopted by the Commission, there is a 1-month window (which may be extended to 3 months) for the European Parliament and the Council to object to the proposals.
ITS	**Implementing Technical Standards** Level 1 (primary) legislation may empower the Commission to adopt technical standards in the form of ITS. The ITS are prepared by the relevant ESAs, and submitted to the Commission, which has 3 months to adopt the RTS or send them back to the ESAs for amendment. Unlike RTS (see above), ITS are not scrutinised by the Parliament or the Council.
ECB	**European Central Bank** The ECB is the central bank for the Eurozone. It is responsible for monetary policy in the Eurozone, as well as identifying and monitoring systemic threats to financial stability such as excessive levels of leverage and debt.
EIB	**European Investment Bank** The EIB is the EU's development bank, owned by the Member States. It uses its creditworthiness to borrow at low rates on international capital markets and works closely with other EU institutions to finance projects that contribute to EU policy objectives.
EIF	**European Investment Fund** The EIF is a specialist provider of risk finance to SMEs across Europe. Between 2011 and 2015 the EIF invested €2.3bn into UK venture capital and growth funds. It is majority owned by the EIB (see above).

The European Private Equity and Venture Capital Industry	
BVK	**Bundesverband Deutscher** The BVK is the German private equity and venture capital trade association
France Invest	**France Invest** France Invest, formerly AFIC is the French private equity and venture capital trade association.
Invest Europe	**Invest Europe** Invest Europe, formerly EVCA, is the pan-European trade body for private equity and venture capital.
EPER	**European Private Equity Roundtable** EPER is the Invest Europe committee that represents large buyout houses. It feeds into the policy work of Invest Europe and the PAE (see below).
PAE	**Public Affairs Executive** The PAE is the industry's strategic decision-making body for EU-level public affairs. It consists of representatives from the venture capital, mid-market and large buyout parts of the private equity industry, as well as institutional investors and representatives of national private equity associations, including the BVCA. The PAE makes policy submissions on behalf of the European private equity and venture capital industry to the European Institutions and international bodies.
Rep Group	**European Representative Group** The Rep Group consists of Invest Europe and the private equity and venture capital associations from individual EU Member States, including the BVCA. It provides a forum for coordinating action at a Member State level and feeds into the work of the PAE (see above).

International	
IOSCO	**International Organization of Securities Commissions** IOSCO the international body that brings together national securities regulators, and develops, implements and promotes adherence to international standards for securities regulation. The FCA (see p56) is the UK member. It works closely with the G20 and the FSB (see p59) on the international regulatory agenda.

FSB	**Financial Stability Board** The FSB is the international body responsible for promoting financial stability. It identifies and monitors global systemic risks, and works with national authorities and international standard setting bodies to respond to threats as they arise. The FSB is chaired by Bank of England Governor, Mark Carney.
OECD	**Organisation for Economic Co-operation and Development** The OECD is an intergovernmental economic organisation designed to promote policies that will improve economic and social well-being. It has a wide-ranging remit including trade and investment, economic growth, employment, health, education and tax. The OECD is responsible for the Base Erosion and Profit Shifting (BEPS) initiative which looks to tackle tax avoidance strategies that exploit gaps and mismatches in tax rules to artificially shift profits to low or no-tax locations.
G20	The G20 is the central forum for international cooperation on financial and economic issues made up of 19 countries and the European Union. Much of the global tax transparency agenda and post-financial crisis regulatory framework originated in discussions between finance ministers, central bankers and heads of government at a G20 level.
FATF	**Financial Action Task Force** FATF is an inter-governmental body established to set global standards for combating money laundering, terrorist financing and related threats to the integrity of the international financial system. FATF also monitors the progress of its members in implementing the measures it recommends.

Other Trade Associations and Industry Bodies	
ABI	**Association of British Insurers** The ABI is the trade body for the insurance industry and providers of savings products and services.
AIC	**Association of Investment Companies** The AIC represents the mutual funds industry as well as some venture capital trusts.
AIMA	**Alternative Investment Management Association** AIMA is the global trade associations for the hedge fund and private debt fund industry.

AFME	**Association for Financial Markets in Europe** AFME is the trade body for participants in wholesale financial markets. Primarily leading European and global investment banks as well as other significant capital market players.
EFAMA	**European Fund and Asset Management Association** EFAMA is the trade association for the traditional European investment management industry.
IA	**The Investment Association** The Investment Association is the trade body that represents the UK's traditional investment management industry.
ILPA	**Institutional Limited Partners Association** ILPA is the global industry association for private equity Limited Partners. It aims to promote best practice in the private equity industry and publishes standardised industry documents and reporting templates.
JMLSG	**Joint Money Laundering Steering Group** The Joint Money Laundering Steering Group is made up of the leading UK trade associations in the financial services Industry. Its aim is to promulgate good practice in countering money laundering and to give practical assistance in interpreting the UK Money Laundering Regulations. This is primarily achieved by the publication of industry-specific guidance.
OTS	**Office for Tax Simplification** The OTS is an independent office of HM Treasury and gives independent advice to the government on simplifying the UK tax system.
PERG	**Private Equity Reporting Group** The PERG is the independent body that monitors conformity with the Walker Guidelines on transparency and disclosure within UK private equity industry. PERG also makes recommendations to the BVCA on improvements in the levels of openness and communication amongst the largest private equity houses in the UK.
UK Finance	**UK Finance** UK Finance is the trade association for the UK banking sector.

US regulation	
Investment Adviser	**Investment Adviser** Any person who, for compensation, engages in the business of advising others, either directly or through publications or writings, as to the value of securities or as to the advisability of investing in, purchasing, or selling securities or who, for compensation and as part of a regular business, issues or promulgates analyses or reports concerning securities (Section 202(a)(11), Investment Advisers Act of 1940).
RIA	**Registered Investment Adviser** An investment adviser that is registered under the Investment Advisers Act with the SEC (see below) and/or state securities authorities, as applicable.
ERA	**Exempt Reporting Advisor** An investment adviser exempt from registration with the SEC due to falling within the Venture Capital Fund, Foreign Private Adviser or Private Fund Adviser exemptions, among others.
FATCA	**Foreign Account Tax Compliance Act** FATCA is a 2010 United States federal law to enforce the requirement for United States persons including those living outside the U.S. to file yearly reports on their non-U.S. financial accounts to the Financial Crimes Enforcement Network ("FINCEN").
SEC	**Securities and Exchange Commission** The SEC is an independent government body in the US, and its aim is to protect investors; maintain fair, orderly, and efficient markets; and facilitate capital formation.

British Private Equity &
Venture Capital Association (BVCA)

5th Floor East, Chancery House
53-64 Chancery Lane
London WC2A 1QS

T. +44 (0)20 7492 0400
E. bvca@bvca.co.uk

www.bvca.co.uk