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Summary of FSA discussion paper on the implementation of the AIFMD

This note summarises the FSA's Discussion Paper (DP12/1) on the implementation of the Alternative Investment Fund Managers Directive (AIFMD). The paper is an excellent summary of where we have got to with AIFMD, but it is very light on new content or clues about the FSA's approach, particularly on key topics such as scope.

The AIFMD was published in the Official Journal of the European Union in July 2011. Its aim is to create a comprehensive and effective regulatory and supervisory framework for alternative investment fund managers within the EU. In November 2011, European Securities and Markets Authority (ESMA) published its final advice to the European Commission on possible implementing measures for AIFMD. DP12/1 was published on 23 January 2012 and implementation of the AIFMD is due by 22 July 2013.

DP12/1 invites comment rather than committing the FSA to a position. Much remains uncertain because the majority of the measures under consideration will not be decided by the FSA, but at an EU level by ESMA's implementation guidelines (anticipated mid-2012). Comments on DP12/1 from firms, trade associations etc. can be made until 23 March 2012 and will contribute to the European debate.

Summary of Implementing measures in DP/12

How the AIFMD will be implemented in the UK

Alternative Investment Fund Managers (AIFMs) will be supervised by the new Financial Conduct Authority. The majority of AIFMD provisions will be implemented through updates to the FSA Handbook, and the remaining through HM Treasury regulations.

The FSA highlights several areas of the existing regulatory structure which will be affected by the implementation of the AIFMD, e.g. the definition and regulation of collective investment schemes. The FSA outlined provisional plans to replace COLL (the Collective Investment Scheme sourcebook) with a new FUND sourcebook - containing general fund management rules for both UCITS and AIFMs.

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The scope of the AIFMD

The Directive will impact Hedge Funds and Private Equity firms, though there is still an open question on scope, for example, there may be Real Estate funds who could also be caught. The FSA envisages over 1,000 UK firms and funds are likely to be in the scope of the AIFMD. The exclusions for "holding companies" and "joint ventures" mean these definitions are crucial, and the FSA is giving firms the opportunity to comment on how these could be interpreted.

Of note are the FSA's plans to require listed closed-ended investment funds (rather than the fund manager) to be authorised under the AIFM. There is expected to be a robust industry response to this proposal to make these funds "internally managed AIFs". Smaller funds may be subject to a registration regime, rather then authorisation - although some commentators doubt this light touch will be acceptable.

Operating requirements on AIFMs

Challenges anticipated by the FSA include:

> a limitation on the MiFID investment services that an external AIFM may provide;

> remuneration of AIFMs which may be brought under the FSA's existing code, or they may develop code specifically for AIFMs. The FSA comment on the need for a proportionate approach, which is positive, but we note that it will be subject to as-yet-unpublished ESMA guidance, so again there is little here in terms of comfort about the direction to be taken;

> what would be proportionate for smaller funds required to separate compliance and risk management functions, as in many funds these roles are virtually the same; and

> AIFMs will be required to disclose how they ensure the fair treatment of all investors. They must also identify investors who obtain preferential treatment.

The FSA is continuing to investigate the possibilities for professional indemnity insurance given the nature of the UK market.

Depositaries

The AIFMD requires the use of depositories and is prescriptive on the requirements for depositories. The FSA is considering making legislative changes to distinguish between the activity of being a depository from other AIFM activities. Rather disappointingly, the FSA seem to want to include new requirements where the strict directive requirements do not apply, in particular, for non-EU AIFs marketed in the UK and managed by a UK AIFM and depositary services offered by the AIFM's group (DP12/1 paras 7.19-21).

It is likely that depositories of authorised funds will face an increase in their own fund requirements, which could put them at a disadvantage to depositories who do not act for these types of funds. However, the FSA is considering allowing lawyers, accountants and fund administrators to act as depositories.

Marketing issues

The FSA consider that marketing needs to be done on behalf of the AIFM, meaning that situations such as capital introductions need to be analysed – when is there "marketing" and when is it "on behalf of" the AIFM. To some extent this also depends on identifying who is the AIFM in a given structure, as to which (as noted above) no further certainty is provided.

Private placement of AIFs managed by non-EU AIFMs in the UK will continue, though changes to the existing financial promotions regime are likely. The FSA has reserved its position on the requirements for marketing to UK retail investors. It is good to see that the private placement regime is to stay in the UK, although some of the suggestions about keeping a list of AIFs that are eligible for placement seem impractical.

Next Steps	
Early 2012	EC to conduct transposition workshops
Q1 2012	EC to propose implementing measures, including directly applicable EU regulations
23 March 2012	FSA deadline for comments on DP12/1
Q2 2012	FSA/HMT to publish UK consultation paper
Q2 2012	FCA (as successor to FSA) to receive AIFM applications for authorisation
22 July 2013	UK is required to implement the AIFMD

For more information please see the Linklaters AIFMD Client Site

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