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By E-Mail: markt-g4@ec.europa.eu

Dear Sirs

Re: CLLS Regulatory Law Committee response to the European Commission Consultation on New European Regime for Venture Capital Funds

The City of London Law Society ("**CLLS**") represents approximately 14,000 City lawyers through individual and corporate membership including some of the largest international law firms in the world.

The CLLS is registered on the European Commission's Transparency Register, and its registration number is **24418535037-82**.

This response to the European Commission Consultation on New European Regime for Venture Capital Funds has been prepared by the CLLS Regulatory Law Committee (the "**Committee**"). Members of the Committee advise a wide range of firms in the financial markets including banks, brokers, investment advisers, investment managers, custodians, private equity and other specialist fund managers as well as market infrastructure providers such as the operators of trading, clearing and settlement systems.

We have restricted our comments to matters which are within our scope as lawyers who advise on the promotion of these kinds of fund. We are not commenting on wider policy issues.

We understand that the proposal has been developed to facilitate the cross-border operations of venture capital funds to add to the overall supply of capital for growth oriented firms. It will of course be the case that there are funds which invest in venture and enterprise situations which will fall within the scope of the Alternative Investment Fund Managers Directive ("**AIFMD**"). This proposal is therefore, we understand, directed at the smaller funds who will not automatically be in the scope of the AIFMD but who will have the ability to opt in to it, but this is not clear and we can see that there could be value in using the new Directive to take larger funds out of scope of the AIFMD if they have the relevant investment policy profile.

We have the following comments:

1. The consultation document states that the Commission committed itself to considering the adoption of new rules, ensuring that by 2012 venture capital funds established in any Member State can operate and invest freely throughout the EU. There are a number of references which refer to the proposed procedure as entitling a venture capital manager to provide its services, raise and invest capital on the basis of an EU passport. We are not aware of any laws that would require a venture capital fund, no matter whether it is established and/or managed within or outside the EU, or indeed that would require any other investor of any kind, to have a licence or permission in order to invest in European companies. Any such requirement would have extremely wide implications, going far beyond venture capital funds. We assume that the reference is not intended to imply this, but we would encourage the Commission to ensure that its future references to this proposal make it clear that the passport concept applies to the ability to raise funds, not invest them.
2. We see the proposal as capable of adding value to those firms who wish to take advantage of the passport, provided that the cost of doing so does not become excessive. However we regard it as critical that those firms who are out of scope of the AIFMD remain able to make use of national private placement regimes, even if they are eligible to apply for the passport under the new proposal. The proposed regime needs to operate as an additional option, rather than as an exclusive possibility, where fund raising is concerned, in order to provide firms with real value and flexibility.
3. The proposal refers in a number of areas to "professional investors". We have expressed concerns on a number of occasions to the effect that the MiFID definition of professional investor is not appropriate to private equity or venture capital investment. The quantitative tests simply make no sense in the context of these types of investment, even the largest funds do not invest in ten transactions a quarter, every four quarters. In the UK venture capital sector "business angel" investors have proved extremely important sources of SME funding. The UK has a regime which has been specifically designed to permit marketing promotion of investment opportunities to sophisticated and high net worth individuals. It has been a successful means by which such individuals have been able to invest in funds (and also directly in SMEs). We attach as an Annex to this letter the statutory provisions to which we refer. If the Commission is really serious about encouraging the flow of money into funds designed for investment in SMEs, it will not ignore the fact that there are many individuals (often themselves successful entrepreneurs) who wish to be able to participate in such investments.
4. We also think that the Commission should review the definition of an SME. There is a general concern that the definition can be interpreted as if all SMEs owned by fund(s) managed by the same manager should be aggregated, with the result that none of them qualifies as an SME. The term is of course already used in the AIFMD but it is clear from the overall context of the AIFMD that the definition cannot be applied with this 'full' meaning, when that term is used in the AIFMD, as it would deprive the provisions of the AIFMD which refer to SMEs of any real effect. We think that would also be so in this case. However we believe that there is a more general issue and it would be appropriate to clarify the definition, as in other contexts this gives rise to potential disadvantages for SMEs which are owned by venture capital funds. This of itself can be a disincentive to investment or accepting investment from such funds.

We would be delighted to discuss any of the above observations and suggestions with you. You may contact me on +44 (0)20 7295 3233 or by email at margaret.chamberlain@traverssmith.com.

Yours faithfully

A handwritten signature in black ink, appearing to read 'M. Chamberlain', with a stylized flourish at the end.

Margaret Chamberlain
Chair, CLLS Regulatory Law Committee

**THE CITY OF LONDON LAW SOCIETY
REGULATORY LAW COMMITTEE**

Individuals and firms represented on this Committee are as follows:

Margaret Chamberlain (Travers Smith LLP) (Chair)
Chris Bates (Clifford Chance LLP)
David Berman (Macfarlanes LLP)
Peter Bevan (Linklaters LLP)
Patrick Buckingham (Herbert Smith LLP)
John Crosthwait (Independent)
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Annex

- UK Financial Promotions Regime Exemptions Relating to Sophisticated and High Net Worth Individuals -

NB. Please note that the statutory exemptions set out below relate to the promotion of interests in unregulated collective investment schemes by FSA authorised persons. A different regime, comprising substantially similar exemptions, will apply if the relevant fund interests are promoted to UK investors by a person who is not FSA authorised.

Certified high net worth individuals

(1) If the requirements of paragraphs (4) and (7) are met, the scheme promotion restriction does not apply to any communication which—

- (a) is a non-real time communication or a solicited real time communication;
- (b) is made to an individual whom the person making the communication believes on reasonable grounds to be a certified high net worth individual;
- (c) relates only to units falling within paragraph (8); and
- (d) does not invite or induce the recipient to enter into an agreement under the terms of which he can incur a liability or obligation to pay or contribute more than he commits by way of investment.

(2) “Certified high net worth individual” means an individual who has signed, within the period of twelve months ending with the day on which the communication is made, a statement complying with Part I of the Schedule (see below).

(3) The validity of a statement signed for the purposes of paragraph (2) is not affected by a defect in the form or wording of the statement, provided that the defect does not alter the statement's meaning and that the words shown in bold type in Part I of the Schedule are so shown in the statement.

(4) The requirements of this paragraph are that either the communication is accompanied by the giving of a warning in accordance with paragraphs (5) and (6) or, where because of the nature of the communication this is not reasonably practicable,—

- (a) a warning in accordance with paragraph (5) is given to the recipient orally at the beginning of the communication together with an indication that he will receive the warning in legible form and that, before receipt of that warning, he should consider carefully any decision to participate in a collective investment scheme to which the communication relates; and
- (b) a warning in accordance with paragraphs (5) and (6) (d) to (h) is sent to the recipient of the communication within two business days of the day on which the communication is made.

(5) The warning must be in the following terms—

“Reliance on this promotion for the purpose of buying the units to which the promotion relates may expose an individual to a significant risk of losing all of the property or other assets invested.”.

But, where a warning is sent pursuant to paragraph (4)(b), for the words “this promotion” in both places where they occur there must be substituted wording which clearly identifies the promotion which is the subject of the warning.

(6) The warning must—

- (a) be given at the beginning of the communication;
- (b) precede any other written or pictorial matter;
- (c) be in a font size consistent with the text forming the remainder of the communication;
- (d) be indelible;
- (e) be legible;
- (f) be printed in black, bold type;
- (g) be surrounded by a black border which does not interfere with the text of the warning; and
- (h) not be hidden, obscured or interrupted by any other written or pictorial matter.

(7) The requirements of this paragraph are that the communication is accompanied by an indication—

- (a) that it is exempt from the restriction on the promotion of unregulated schemes (in section 238 of the Act) on the grounds that the communication is made to a certified high net worth individual;
- (b) of the requirements that must be met for an individual to qualify as a certified high net worth individual;
- (c) that any individual who is in any doubt about the units to which the communication relates should consult an authorised person specialising in advising in participation in unregulated schemes.

(8) A unit falls within this paragraph if it is in an unregulated scheme which invests wholly or predominantly in the shares in or debentures of one or more unlisted companies.

(9) “Business day” means any day except a Saturday, a Sunday, Christmas Day, Good Friday or a day which is a bank holiday under the Banking and Financial Dealings Act 1971 in any part of the United Kingdom.

(10) “Unlisted company” has the meaning given in the Financial Services and Markets Act 2000 (Financial Promotion) Order 2001.]

The statement to be signed for the purposes of article 21(2) (definition of high net worth individual) must be in the following form and contain the following content—

[“Statement for Certified High Net Worth Individual

I declare that I am a certified high net worth individual for the purposes of the Financial Services and Markets Act 2000 (Promotion of Collective Investment Schemes) (Exemptions) Order 2001.

I understand that this means—

- (a) I can receive promotions, made by a person who is authorised by the Financial Services Authority, which relate to units in unregulated collective investment schemes that invest wholly or predominantly in unlisted companies;
- (b) the schemes to which the promotions will relate are not authorised or recognised for the purposes of the Financial Services and Markets Act 2000.

I am a certified high net worth individual because **at least one of the following applies—**

- (a) I had, during the financial year immediately preceding the date below, an annual income to the value of £100,000 or more;
- (b) I held, throughout the financial year immediately preceding the date below, net assets to the value of £250,000 or more. Net assets for these purposes do not include—
 - (i) the property which is my primary residence or any loan secured on that residence;
 - (ii) any rights of mine under a qualifying contract of insurance within the meaning of the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001; or
 - (iii) any benefits (in the form of pensions or otherwise) which are payable on the termination of my service or on my death or retirement and to which I am (or my dependants are), or may be, entitled.

I accept that I can lose my property and other assets from making investment decisions based on financial promotions.

I am aware that it is open to me to seek advice from someone who specialises in advising on unregulated collective investment schemes.

Signature

Date”.]

Self-Certified Sophisticated Investors

(1) “Self-certified sophisticated investor” means an individual who has signed, within the period of twelve months ending with the day on which the communication is made, a statement complying with Part II of the Schedule (see below).

(2) The validity of a statement signed for the purposes of paragraph (1) is not affected by a defect in the form or wording of the statement, provided that the defect does not alter the statement's meaning and that the words shown in bold type in Part II of the Schedule are so shown in the statement.

(3) If the requirements of paragraphs (4) and (7) are met, the scheme promotion restriction does not apply to any communication which—

- (a) is made to an individual whom the person making the communication believes on reasonable grounds to be a self-certified sophisticated investor;
- (b) relates only to units falling within paragraph (8); and
- (c) does not invite or induce the recipient to enter into an agreement under the terms of which he can incur a liability or obligation to pay or contribute more than he commits by way of investment.

(4) The requirements of this paragraph are—

- (a) . . .
- (b) . . . that either the communication is accompanied by the giving of a warning in accordance with paragraphs (5) and (6) or, where because of the nature of the communication this is not reasonably practicable,—
 - (i) a warning in accordance with paragraph (5) is given to the recipient orally at the beginning of the communication together with an indication that he will receive the warning in legible form and that, before receipt of that warning, he should consider carefully any decision to participate in a collective investment scheme to which the communication relates; and
 - (ii) a warning in accordance with paragraphs (5) and (6) (d) to (h) is sent to the recipient of the communication within two business days of the day on which the communication is made.

(5) The warning must be in the following terms—

“Reliance on this promotion for the purpose of buying [the] units to which the promotion relates may expose an individual to a significant risk of losing all of the property or other assets invested.”.

But, where a warning is sent pursuant to paragraph (4)(b), for the words “this promotion” in both places where they occur there must be substituted wording which clearly identifies the promotion which is the subject of the warning.

(6) The warning must—

- (a) be given at the beginning of the communication;
- (b) precede any other written or pictorial matter;
- (c) be in a font size consistent with the text forming the remainder of the communication;
- (d) be indelible;
- (e) be legible;
- (f) be printed in black, bold type;
- (g) be surrounded by a black border which does not interfere with the text of the warning; and
- (h) not be hidden, obscured or interrupted by any other written or pictorial matter.

(7) The requirements of this paragraph are that the communication is accompanied by an indication—

- (a) that it is exempt from the scheme promotion restriction (in section 238 of the Act) on the communication of invitations or inducements to participate in unregulated schemes on the ground that it is made to a self-certified sophisticated investor;
- (b) of the requirements that must be met for an individual to qualify as a self-certified sophisticated investor;
- (c) that any individual who is in any doubt about the investment to which the invitation or inducement relates should consult an authorised person specialising in advising on investments of the kind in question.

(8) A unit falls within this paragraph if it is in an unregulated scheme which invests wholly or predominantly in the shares in or debentures of one or more an unlisted companies.

(9) "Business day" means any day except a Saturday, a Sunday, Christmas Day, Good Friday or a day which is a bank holiday under the Banking and Financial Dealings Act 1971 in any part of the United Kingdom.

(10) "Unlisted company" has the meaning given in the Financial Services and Markets Act 2000 (Financial Promotion) Order 2001.

The statement to be signed for the purposes of article 23A(1) (definition of self-certified sophisticated investor) must be in the following form and contain the following content—

[“Statement for Self-certified Sophisticated Investor

I declare that I am a self-certified sophisticated investor for the purposes of the Financial Services and Markets Act 2000 (Promotion of Collective Investment Schemes) (Exemptions) Order 2001.

I understand that this means—

- (a) I can receive promotions, made by a person who is authorised by the Financial Services Authority, which relate to units in unregulated collective investment schemes that invest wholly or predominantly in unlisted companies;
- (b) the schemes to which the promotions will relate are not authorised or recognised for the purposes of the Financial Services and Markets Act 2000.

I am a self-certified sophisticated investor because at least one of the following applies—

- (a) I am a member of a network or syndicate of business angels and have been so for at least the last six months prior to the date below;
- (b) I have made more than one investment in an unlisted company in the two years prior to the date below;
- (c) I am working, or have worked in the two years prior to the date below, in a professional capacity in the private equity sector, or in the provision of finance for small and medium enterprises;
- (d) I am currently, or have been in the two years prior to the date below, a director of a company with an annual turnover of at least £1 million.

I accept that I can lose my property and other assets from making investment decisions based on financial promotions.

I am aware that it is open to me to seek advice from someone who specialises in advising on unregulated collective investment schemes.

Signature

Date”.]