

Marie-Noëlle Loewe
Financial Conduct Authority
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By email: Marie-Noelle.Loewe@fca.org.uk

16 May 2017

Dear Ms Loewe

Concerns regarding the ESMA Q&A related to AIFMD Annex I and Delegation

The City of London Law Society ("**CLLS**") represents approximately 17,000 City lawyers through individual and corporate membership including some of the largest international law firms in the world. These law firms advise a variety of clients from multinational companies and financial institutions to Government departments, often in relation to complex, multi-jurisdictional legal issues. The CLLS responds to a variety of consultations on issues of importance to its members through its 19 specialist committees.

This letter has been prepared by the CLLS Regulatory Law Committee (the "**Committee**"). The Regulatory Committee not only responds to consultations but also proactively raises concerns where it becomes aware of issues which it considers to be of importance in a regulatory context.

We write in connection with the recently published updated version of the European Securities and Markets Authority ("**ESMA**") Questions and Answers on the application of the AIFMD (issued 16 November 2016 with reference ESMA/2016/1576). In particular, we write with reference to the response to new question 2 in Section VIII on Delegation.

We have had the opportunity to consider the letter sent to you by the Alternative Investment Management Association Limited ("**AIMA**") and the Alternative Credit Council ("**ACC**") dated 25 November 2016, a copy of which is attached for ease of reference.

We agree with the contents of that letter, and we are concerned that ESMA's response to question 2 on Delegation is based on an incorrect interpretation of the relevant provisions of AIFMD. We also believe that the response cuts directly across the approach taken by fund managers and practitioners in the UK funds industry and is not supported by the approach taken by the FCA in FUND and PERG. If the FCA were to adopt a similar approach, this

would require significant reorganisation and re-documentation of AIFs and their organisational arrangements.

We therefore support and reiterate the request made by AIMA and the ACC that the FCA should seek to update its rules or guidance or otherwise take steps to give effect to ESMA's response to Question 2 on Delegation.

We do not propose to reiterate the arguments set out in the AIMA and ACC letter but broadly, our concerns can be summarised as follows:

Functions the AIFM must perform

Annex 1 of AIFMD contemplated that there was a fundamental difference between services that an AIFM must carry out in order to be considered an AIFM (namely portfolio management and/or risk management) and those which it may carry out.

The functions which an AIFM may carry out are not additional services which an AIF would never require. It cannot have been the legislator's intention in enacting Annex 1, point 2 that AIFs would never require legal services or accounting services. We believe the better view, and the view currently taken by most AIFs and AIFMS, is that third parties must be permitted to provide those services in Annex 1 point 2 without impacting the management function of the AIFM.

Ability to delegate functions

If it is correct that an AIFM is not required to automatically be responsible for the functions in Annex 1 point 2, it must be **appointed** in order to carry out those tasks. Where the AIF and AIFM are legally separate entities (which is the case with many AIFs), only the AIF itself may direct its business and authorise third parties to carry out those services it requires.

If an AIFM has not been appointed to provide a particular service, then legally or contractually, it has no basis for delegating to a third party. It would also have no power to terminate the delegation arrangement if compliance was at risk. Further, Articles 5(2) and (3) AIFMD specifically provide for steps that need to be taken in instances where an external AIFM cannot ensure compliance. This would not be necessary if the AIFM was responsible for the provision of all services to the AIF.

Impact on legal services

We are additionally concerned that the interpretation of the AIFM's responsibilities on Delegation could negatively impact the provision of legal services to AIFs. In particular, the protection of client privilege may be affected if legal counsel are to be considered delegates of the AIFM rather than directly appointed by the AIF itself. There is also a possibility that a conflict of interest could arise in a case where the AIF might wish to pursue a course of action which might adversely affect the AIFM.

Compliance with Article 20 of AIFMD also creates some significant practical issues for law firms, most notably the need to grant the AIFM right of access to the premises of the law firm as envisaged by Article 75(h) of the delegated Regulation.

Current FCA rules and guidance

The FCA rules and guidance on this topic already make clear that an AIFM can only delegate services for which it is responsible (for example, FUND 3.10 and the response to question 3.5 in PERG 16.3). We see no reason for the FCA to make any fundamental alteration to

existing rules that are based on a plainly correct reading of the underlying European legislation.

We would be happy to set out our views in more detail or to attend a meeting to discuss it further with you on request.

If you would find it helpful to discuss any of these comments then we would be happy to do so. Please contact Karen Anderson by telephone on +44 (0) 20 7466 2404 or by email at Karen.Anderson@hsf.com in the first instance.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Karen Anderson', followed by a comma.

Karen Anderson
Chair, CLLS Regulatory Law Committee
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