



K&L GATES

**2016 INVESTMENT MANAGEMENT CONFERENCE**

# European Investment Management Issues

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# Brexit

## HOW DOES THE UK EXIT?

- Article 50 of the Lisbon Treaty
- New Brexit task force created
- Oliver Robbins appointed as the Permanent Secretary to the new team
- EU split roles for exit (EC) and continued access (EU Council)
  - Didier Seeuws, former chief of staff to former European council president Herman Van Rompuy
  - Michel Barnier (and Martin Selmayr, current EC president Juncker's chief of staff)
- European Parliament also has a role
  - Guy Verhofstadt, former Belgian prime minister
















## ARTICLE 50 PROCESS

- Art 50 of the Treaty on European Union.
- Notification in the hands of the UK.
  - Does it require an Act of Parliament?
  - Can it be deemed?
- Up to two-year period for withdrawal to be negotiated and take effect.
- Negotiations between the UK and the European Commission, as EU negotiator, based on guidelines issued by the European Council and in accordance with article 218(3) of the Treaty on the Functioning of the European Union (TFEU).
- Can be extended by agreement of all EU member states.
- If no extension, UK automatically ceases to be a member of the EU at the end of two years.



## How Could the UK's Relationship With the EU Change?

The UK already opts out from parts of the EU. If it leaves, its future could look like Norway, Switzerland, or Turkey, nonmembers with partial participation in the EU.

	 FULL PARTICIPATION  PARTIAL PARTICIPATION <small>Indicates a negotiated special arrangement.</small>	 SINGLE MARKET	 FREE MOVEMENT OF PEOPLE	 CONTRIBUTE TO EU BUDGET	 VOTE ON EU LAW	 EUROZONE	 "EVER CLOSER UNION"
 STANDARD EU*		●	●	●	●	●	●
 CURRENT UK MEMBERSHIP		●	●	○	●		
<b>POTENTIAL POST-BREXIT SCENARIOS</b>							
 EUROPEAN ECONOMIC AREA (NORWAY)		○	●	○			
 BILATERAL DEAL (SWITZERLAND)		○	●				
 CUSTOMS UNION (TURKEY)		○					

COUNCIL OF FOREIGN RELATIONS

\*Except for the UK Sources: UK Government, *The Economist* Credits: James McBride, David Foster



# IMPACT OF BREXIT ON FUNDS AND MANAGERS

- UCITS and AIFMs
- Cross-border advisory/management services (MiFid services)
- Solvency II, CRD, myriad of other EU laws and directives incorporated into UK laws (competition, immigration, etc.)
- Potential outcomes
  - EEA (Norway) – Single-market access for goods and services
  - EFTA (Switzerland) – Single-market access – goods only
  - Something else?



## BREXIT PRACTICAL CONSIDERATIONS

- NO CHANGE FOR THE TIME BEING, but now is time for detailed contingency planning
- Consider exposure to EU markets
- What is your current licensing strategy and does it rely on passporting?
- Where are your operations and staff based?
- It's not just about passporting! *UK laws are based on EU laws*



## HOW SHOULD THE INDUSTRY RESPOND?

- Raise awareness with EU/Eurozone of the importance of the UK as a partner outside of the EU.
- Build coalitions of stakeholders throughout the EU to communicate the importance of a balanced deal with the UK and to reinforce the above.
- Promote a set of policies to improve the UK's competitive position (for example, tax, skilled migration, targeted removal of regulations etc).
- Propose solutions and options that remove uncertainty – what is realistically achievable?
- UK debate should recognize the very real concerns of Eurozone leaders of the risk of contagion from the Brexit result.
- The negotiations will be a multi-party process with no one party able to leverage its position.
- Work with industry trade groups.
- Get involved with the UK's Brexit task force.





## EXAMPLES

- US or EU manager has Irish ManCo with Ireland-domiciled UCITS passported into UK
- US or EU manager with UK-based UCITS for local market and passported throughout EU
- US or EU manager with UK-based UCITS for local UK market
  - *UK Non-UCITS Retail Scheme (NURS)?*



# NURS 101

- **UK (FCA) authorized fund**
  - *must be organized in the UK as either an open-ended investment company or unit trust.*
- **May be marketed to retail investors in UK**
  - *Non-UCITS, so no UCITS passport*
- **Subject to the AIFMD; not UCITS**
  - *Although they have more in common with UCITS, NURS are subject to the AIFMD.*
  - *NURS could benefit from the AIFMD passport to market to professional clients in the EEA outside the UK, subject to NPPRs*
- **Investment powers / restrictions similar to UCITS but with additional flexibility, e.g.:**
  - *Up to 100% NAV in real estate*
  - *Up to 10% NAV in transferable securities of single issuer (cf 5/10/40 rule for UCITS)*
  - *Up to 20% NAV in unlisted securities (cf 10% limit for UCITS)*
  - *Up to 35% NAV in CIS (cf 20% for UCITS)*
  - *For “feeder NURS”, up to 100% in a UCITS or other NURS*
  - *For NURS authorized as “fund of alternative investment funds” (“FAIFs”, up to 100% NAV in unregulated funds meeting certain criteria)*
- **KIID / PRIIPs**
  - *A NURS will need to produce a short disclosure document accompanying the prospectus.*
  - *FCA permits NURS to produce a “NURS KIID”, which is effectively the same as the KIID for UCITS.*
  - *Both UCITS and NURS are within the scope of the PRIIPs Regulation, but it remains unclear whether NURS will benefit from the same exemption as UCITS which last until 31 December 2019.*





UCITS/AIFMD

# UCITS V - REMUNERATION

## ■ Remuneration

- Alignment of UCITS manager remuneration with AIFMD
- Applies to all compensation paid to all staff whose activities have a material impact on the risk profile of the UCITS
  - Assessment of potential “material influence” of the staff member on the UCITS’s risk profile
  - Executives, directors, senior management, portfolio managers, traders, CIOs
  - What about compliance officers, internal counsel, sales persons, chief risk officer?
- Application to “delegates” – if not subject to an equivalent regulatory regime (AIFMD/CRD), “appropriate contractual arrangements” should be put in place with the delegate
- Proportionality applies and may allow for disapplication of some of the restrictions
  - Compliance only required in a way and to an extent that is appropriate to the manager’s size, internal organization, and the nature, scope and complexity of activities
- ESMA to issue additional details in Level 2 guidelines regarding applicability to staff, proportionality



## UCITS V - REMUNERATION

- Remuneration (continued)
  - Variable Remuneration - Shares
    - 50% paid in UCITS shares (or certain other), with vesting periods
    - Does not apply if management of UCITS is less than 50% of the total assets managed by the management company
  - Variable Remuneration – Bonuses
    - 40% deferral over minimum of 3 years (or recommended holding period of UCITS concerned)
    - Deferral higher where variable compensation is a large component of total compensation



## UCITS V - PROPORTIONALITY

- General principle requiring managers to comply with remuneration rules “*in a way and to the extent that is appropriate to their size, internal organization and the nature, scope, and complexity of their activities.*”
- ESMA consultation proposed to interpret proportionality to allow dis-application of certain requirements in some circumstances (consistent with AIFMD)
  - Inconsistent with EBA application of similar rules under CRD



## UCITS V – ESMA FINAL GUIDELINES REPORT

- Issued 31 March
- Most significant change to initial draft was lack of guidance regarding application of proportionality principles
- ESMA sent a letter to EC and EP –
  - Proportionality should apply, but....
  - Legislative changes may be necessary

