

# Keeping up with Alternative Investment Funds

June 2020

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# Introduction

Welcome to our June edition of Keeping up with Alternative Investment Funds. Whilst we continue to see the lifting of certain lockdown measures by Government, and the economy and wider environment begins to head towards some form of normality, we continue to live in unpredictable and challenging times. We hope you and your families continue to remain safe and well.

As various new measures are being announced by government in response to the pandemic, our [COVID-19 website](#) will be updated regularly with the latest guidance, updates, and details of how we can offer help and support to businesses, from crisis scenario planning, to cashflow management and cyber security.

Areas where we are seeing a lot of client interest at present are around the “return to the office” protocols which employers will need to put in place to ensure employee safety and managing a workforce in the event of a second COVID-19 spike.

We hosted our latest virtual client roundtable on 3 June, where we covered the following areas:

1. HMRC enquiry activity during COVID-19 and in the past 12 months;
2. HMRC consultation on tax scheme notification;
3. Corporate Criminal Offence, Senior Accounting Officer and Tax Strategy - what did Alternative Fund Managers do originally and what level of challenge has there been?

Our next roundtable event for clients will be held on 1 July; this will focus on the role of technology within AIF managers and we very much hope you are able to join us then.

Looking ahead, we are still keen to hear feedback from clients on the virtual client roundtables held to date regarding frequency (bi-monthly vs monthly), content, format and any suggested topics to be covered at future events. Please contact [richard.madden@pwc.com](mailto:richard.madden@pwc.com) or [Robert.mellor@pwc.com](mailto:Robert.mellor@pwc.com) if you have any feedback or suggestions.

Our June newsletter covers a wide variety of topics including corporate governance and broader workforce issues in light of COVID-19, as well as a refresher on where things stand on Brexit.

See the full list of articles in this newsletter below:

- COVID-19 – The people perspective
- UK – Update on non-resident capital gains tax
- COVID-19 – Is it time for a tax strategy reset?
- UK – Corporate governance response to COVID-19 and its future
- UK & EU – Whatever happened to Brexit?...
- AIFMD Review – Assessing the application and the scope of the Alternative Investment Fund Manager Directive

Please do continue to reach out to your usual PwC contacts if you would like to discuss any of the above, and please do share your feedback with us if there is a particular topic or issue you would like us to cover.

Kind regards,

PwC Alternative Investment Funds team



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# News Bulletin

## DAC 6 Delays

Following recent announcements made by certain territories, it is likely that the revised proposal will provide for a deferral in implementation of the rules, as set out below.

With regards to the reporting of arrangements devised during the transitional period, it is proposed that Member States may, on an optional basis, allow intermediaries and relevant taxpayers to file, by 28 February 2021, information on reportable cross-border arrangements (the first step of which was implemented between 25 June 2018 and 30 June 2020). This is an extension on the previous deadline of 31 August 2020.

Should this option be exercised by a Member State, the following additional rules would apply:

- the deadline of 30 days for filing information by intermediaries and relevant taxpayers shall begin on 1 January 2021 where the triggering event took place between 1 July 2020 and 31 December 2020;
- the first automatic exchange of information shall take place by 30 April 2021;
- in the case of marketable arrangements, the first periodic report shall be made by the intermediary by 30 April 2021.

## Next steps

The deferral needs to be unanimously approved by the Economic and Financial Affairs Council (ECOFIN). It should be noted that a European Parliament (EP) opinion is required (the EP cannot amend the proposal) and is expected by 30 June 2020. Furthermore, the opinion of the European Economic and Social Committee is expected by 14 June 2020.

## UK – Senior Accounting Officer Deadlines

The relevant SAO notification and certification deadlines have not been impacted by COVID-19, unless an official deferral of the accounts filing has otherwise been obtained on a standalone basis from Companies House.

Where a company, either alone, or as part of a group satisfies the relevant turnover, and/or balance sheet tests, the deadlines for filing are:

- 6 months following the end of the accounting period for public companies; and
- 9 months for private companies.

A large number of alternative investment fund managers are approaching their usual SAO deadlines on either 30 June 2020 or 30 September 2020, and a failure to meet these deadlines is likely to lead to penalties being levied. Alternative investment fund managers and their SAOs should therefore be mindful of these deadlines and ensure that they have appropriate procedures in place to meet them.

One particular point to highlight regarding the rules is that qualifying companies need to be able to demonstrate that they had appropriate tax accounting arrangements in place for the relevant period. There is no relaxation of this requirement during the COVID-19 outbreak. However many businesses are finding that demonstrating that existing controls are robust and appropriately evidenced is more difficult in the current climate.



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## COVID-19 – The people perspective

The coronavirus (COVID-19) pandemic of 2020 has completely changed the way that many of us view the world and the part that we play in it. The threat of the virus reaches each of the four corners and it has fundamentally changed how we conduct our lives today and also how we expect our lives and businesses to be conducted in the future. Over the past few months we have all had to think about how we can adapt our working practices and support our people in order to keep businesses going as best as they can through these unprecedented challenges. But what does it all mean for the people in your business and what are the questions that you need to work through?

During the pandemic so far there have been three key areas of focus that we have seen from the alternatives industry.

- Employees' **well-being** has rocketed to the top of the employee value proposition with employers offering numerous initiatives from mindfulness sessions, hosting events with external speakers, virtual team quizzes, additional time off to care for dependents and much more (the taxation of benefits implications of some of this well being support should not be overlooked).
- **Crisis management** and deployment of business continuity contingency programmes, making sure that your people can safely carry on their work, continue to maintain strong data and cyber security protocols, and ongoing communication with employees at a time when the alternatives industry seems to be more active than ever
- Grappling with the immigration, regulatory, legal and tax consequences for both individuals and organisations in the case of **individuals who are displaced** from their normal living and working arrangements as a result of COVID-19.

Some of the key questions that should be considered in light of the current situation are:

**Immigration** - does the individual have the right to work in the country in which they are currently located? In the vast majority of cases this has been an easy box to tick because the nature of the health crisis has meant that individuals are more likely to have returned to their country of citizenship rather than another location in which their permission to work may be restricted.

**Regulatory concerns** - does the individual perform regulated activities, for which entity and are they still permitted to carry out the activities you need them to if they are displaced outside their normal place of work? In the event that regulatory permissions do not extend to that individual, then how can you manage the chain of work in order to remain compliant?

**Permanent establishment** - does an individual's increased presence and activity in a particular location give you cause

for PE concern? The OECD have indicated that they do not expect COVID-19 on its own to lead to PE risks and that a 'temporary' presence in a location is unlikely to change the overall position. However, it is still necessary to look at the position in aggregate of all individuals in a particular location, in order to make a proper PE assessment. In the UK, by way of example, business visitors to the UK will often be relieved from having to file a UK tax return by means of the Short Term Business Visitor arrangements with HMRC. However, during the pandemic, one should be aware of the potentially heightened PE risks, especially where people are carrying out their normal day-to-day functions in the UK and also thinking about volumes of people involved.

**Residence analysis** - Will an individual's tax residence status change because of their physical presence during the COVID-19 pandemic? Many countries, including the UK, have announced that additional days spent in a territory as a result of COVID-19 will be treated as 'exceptional' days and not within the normal day counting rules to assess whether someone is tax resident in that location or not. However, this does not necessarily mean their tax bill will not increase as a result of the individual's increased presence. More often than not, the difference between a resident and a non-resident is whether the taxpayer is taxed on worldwide income in that location, or just income which is sourced to that location.

**Withholding** - whenever we consider that a tax liability might exist on employment income, it is important to consider whether tax withholding is required. In many countries, tax withholding will only be required if the individual has a particular residence status, or if the organisation already has an entity or presence in that location (this is the case in the UK for example).

However, other locations, such as Canada and Portugal, can require foreign employers to register and operate local payroll withholding. The practical challenges of doing so for one individual could potentially be quite onerous, especially if it is not known how long that individual will be in that location for. We expect most tax authorities to take a relatively pragmatic approach in cases where withholding applies as a result of COVID-19. However, as borders reopen and a new 'business as usual' state emerges, organisations need to stay close to where their individuals are based to ensure that they do not fall foul of compliance obligations in the medium term.

## COVID-19 – The people perspective cont.

**Employment law and social security** - does the individual's unusually increased presence in a country give rise to employment law obligations for you as an employer? We have seen instances of new hires not being able to take up their new positions as a result of the pandemic and so where does that leave organisations in terms of paying the individuals or helping them get set up to work from home despite being new to the firm? And what about how the social security rules apply in each country? From a UK perspective, adding on top of this the ongoing complexity that Brexit brings us on our access to the European social security regulations, compounded by the rather emotive concern about access to healthcare means that social security is more of a concern for employees as well as employers.

**Benefits** – If say as an organisation you wanted to make sure that your people were able to perform their duties from home, wherever home may be, so you let them buy a comfortable new office chair and a screen for use at home and then reimbursed the expense. Do we now need to report the benefit in kind on the 2019/20 P11Ds which are coming up for filing, and equivalents in other locations? In most countries there will be specific exemptions for qualifying business expenses but this may require consideration as to the arrangements over, for example, who owns the products and what the individual could be required to do with them in the event they leave your organisation.

For many of us, as part of our Brexit planning, we saw increases in the number of people working across borders and more and more people undertaking commuter arrangements. For example, having a family home in one country and spending weekends there, but commuting to another country for the working week. Many of these arrangements will be challenged, not just in the short term in respect of all the areas mentioned above, but also in the future as we look past the current pandemic.

**Looking ahead** - Will those individuals who have historically travelled a lot still want to travel?

Will people still expect to commute on public transport to go to the office every day? How will you give people cycles of experience without physically moving them to a new country or role? How will costs of employing people be impacted by cultural changes in the way we work? What will the new "business as usual" look like?

Many organisations have found themselves surprised by just how successful the enforced virtual working arrangements have been. Employees have felt empowered to find a way of working that better suits their lifestyle for example adopting much more flexible working hours to fit around dependent care. Employees seem to thrive on the sense of autonomy and have found enriching ways to use time freed up that was previously spent commuting.

Whilst there are inevitable challenges - how to help integrate into new teams, help new joiners successfully onboard, build a sense of community, manage and monitor underperformance and so on - we are presented with an opportunity to rethink the future of work. Perhaps we can reduce fixed costs of running businesses by reducing the reliance on real estate, potentially providing access to a much larger talent pool if we can be largely location agnostic, increase employee engagement if we can find the right framework, perhaps even achieve fixed pay savings by using home location rates rather than big city pay rates

There is a fine balancing act between the various risks, challenges and benefits, which will no doubt evolve over time, as Alternative Investment Funds think about the extent to which virtual working will form a greater part of the way they work in the future.

### Next steps for Alternative Investment Funds

Some of the above analyses, such as personal income tax residence and associated withholding obligations, will be possible to undertake on an individual by individual basis.

However, other aspects, such as permanent establishment risks, can only be assessed accurately when armed with information on an aggregate basis. As such, all firms should

ensure they have adequate information about members of their workforce who are 'displaced individuals' in the context of the tax and other implications mentioned above. PwC would be happy to work with you to help analyse that information and understand your requirements on a location by location basis.

Many Alternative Investment Funds will also want to think about a more strategic approach to HR, as the culture of work continues to evolve over the coming months and years.



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# UK – Update on non-resident capital gains tax

On the 10th April 2020, the non-residents capital gains tax ('NRCGT') rules were amended in a very fundamental way, impacting Real Estate Investment Trust ('REIT') disposals made by non-resident funds (collective investment vehicles, 'CIVs') between 6 April 2019 and 9 April 2020. The headline is that such disposals were previously taxable; now they are most likely not.

The UK Property Rich Collective Investment Vehicles (Amendment of the Taxation of Chargeable Gains Act 1992) Regulations 2020 came into force from 10 April 2020. These regulations, which were also supplemented by draft guidance (Appendix 16) have brought about some changes which may impact whether they have a UK Corporate tax obligation for the period 6 April 2019 to 9 April 2020.

We have summarised some of the salient changes below.

## Definition of group UK REIT

In practice most, if not all, UK REITs are likely to be group UK REITs, but the position should be confirmed on a case-by-case basis.

HMRC have acknowledged that disposals of shares in the principal company of a group UK REIT, assuming it is 'UK property rich', should not fall within the definition of 'collective investment vehicle'. The definition has been corrected by Regulation 3 of SI 2020 No. 315. However this change does not take effect for disposals prior to 10 April 2020.

Disposals of interests of less than 25% in such REITs by non-UK tax residents (other than those who held the shares in connection with a UK PE through which a trade is carried on) are not within the charge to UK tax on capital gains between 6 April 2019 and 9 April 2020 (inclusive).

Many non-UK residents are not within the charge to UK tax on the disposal of shares in listed/regularly traded shares under the terms of the relevant Double Tax Treaty. Notable exceptions are Australian tax resident investors and investors who are not able to benefit from a treaty (e.g. Luxembourg entities within the RAIF regime and potentially exempt Irish Funds).

Following a recent update from the IA, to the extent that you have disposed of UK group REITs prior to the 10th April 2020, even if you are registered for UK tax, HMRC have confirmed these are not in scope and that no nil returns are expected to be filed. However, if you have received a Unique Tax Reference number, you are expected to inform HMRC why you will not be filing a return.

## Transparency Election

Non-resident CIVs that are set up as trusts or contractual co-ownership arrangements are typically deemed to be opaque for UK capital gains purposes. These include Irish CCFs and Jersey Property Unit trusts.

Where, however, such CIVs are UK property rich and also transparent for the purposes of UK tax on income, they will have the ability to make the Transparency Election. The effect of this election is that the CIV will be treated as transparent for the purposes of UK tax on capital gains (i.e. the CIV will not be subject to tax on capital gains, but rather the Investors in the CIV will be subject to tax on the capital gains, subject to them being taxable).

All participants need to consent to the irrevocable election, which has retrospective effect.

Further clarifications were also issued in relation to the information that is required to be provided to HMRC.

**Effect:** the Transparency Election was previously required to be made within 12 months of 6 April 2019 or the date the first UK property is acquired (if later). This means that the deadline to make the election was 5 April 2020. HMRC has extended the deadline for making the Transparency Election for existing qualifying CIVs from 6 April 2020 to 1 October 2020.

CIVs that have made the transparency election now need to file an annual partnership return regardless of whether any property has been disposed of. Moreover, upon the election, the CIV needs to provide investor's details to HMRC.

## Exemption Elections

An election may be made for a UK property rich qualifying CIV, or a qualifying company which is not itself a qualifying CIV (but is wholly or almost wholly owned by a collective investment scheme partnership or CoACS). The effect of the election is to exempt that entity, and any other entities in which it has at least a 40% stake, on direct and indirect disposals of UK property. The exemption regime is only available to UK property rich CIVs in order to be able to tax gains at the investor level.

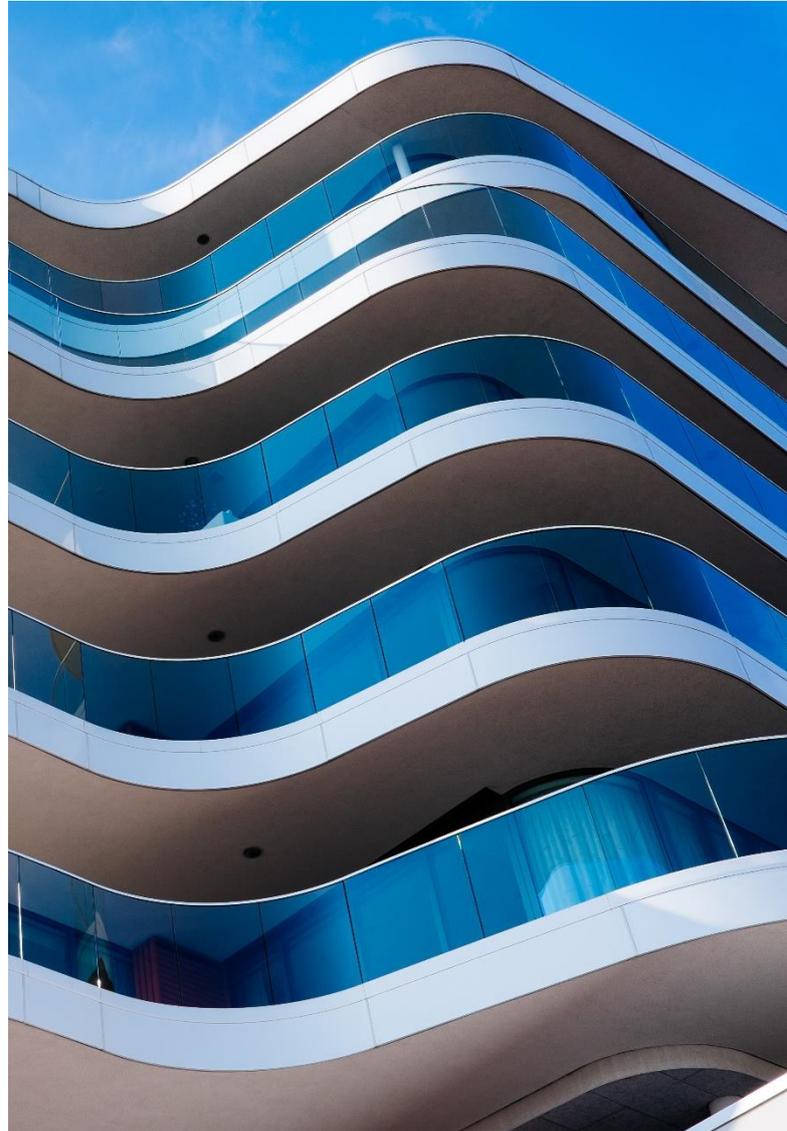
An election was required to be made by the fund manager with retrospective effect of up to 12 months, and it did not require the consent of all the investors. Therefore, to exempt disposals on or after 6 April 2019, the Exemption election had to be made by 5 April 2020.

## UK – Update on non-resident capital gains tax cont.

Effect: as a consequence of the Statutory Instrument, HMRC have now confirmed that Exemption Elections may be treated as having retrospective effect for a period greater than the 12 months, where the Exemption Election is submitted after 10 April 2020 but before 1 October 2020. In practice, this means that for existing CIVs, the Exemption Election can now be made up until 30 September 2020 and it will still exempt any disposals on or after 6 April 2019.

### Exemptions from UK property rich test for CIVs

Certain collective investment vehicles were previously not considered to be UK property rich as they relied on the exemptions available under Schedule 1A TCGA 1992, i.e. the trading exemption and the linked disposals election. These exemptions have been eliminated from the new regulations and therefore CIVs which were previously out of the scope of these rules are now in scope. These CIVs should now consider whether they are able to make any elections (transparency/exemption) elections. This is only applicable to CIVs, and therefore investors can still avail of these exemptions if they do not hold these interests through a CIV.



### Next steps for Alternative Investment Funds

Alternative Investment Funds should consider these fundamental changes to the rules in light of their UK real estate holdings. An overall assessment should be made as to whether the rules will now require you to file a UK tax return, or

alternatively if they enable an exemption from the regime on relevant disposals. Further clarifications from the local industry bodies should also be monitored.



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# COVID-19: is it time for a tax strategy reset?

*In PwC's latest online roundtable discussion on the impacts of COVID-19 on the alternatives sector, our experts discussed the growing operational challenges facing the tax function – and how it should respond.*

Should alternative investment funds' tax functions take time to review their "operational fitness"? Amid the disruption of COVID-19, now might not be an obvious time to address such questions. But as HMRC and other tax authorities continue to press ahead with new initiatives and reforms – and begin to scrutinise how alternatives have responded to previous change – there is good reason for tax functions to think of the interruption to "business as usual" at the present time as a fitting prompt to reconsider some fundamental issues.

The Senior Accounting Officer (SAO) and Corporate Criminal Offence (CCO) regimes represent important straws in the wind. It is becoming increasingly clear that HMRC is concerned that firms maintain the standards they have set and adapt to new developments.

On the SAO regime, for example, have alternative investment funds followed up on their strong initial readiness assessment work – how do they demonstrate the link between their annual certification exercises and what's actually going on in the business? HMRC has flagged issues such as rolling forward assessments and the level of the challenge in the business.

On CCO, high-level impact assessments satisfied HMRC at the time the regime was introduced, but it will now be more important to be able to demonstrate to HMRC that firms have followed through with additional testing and review programmes.

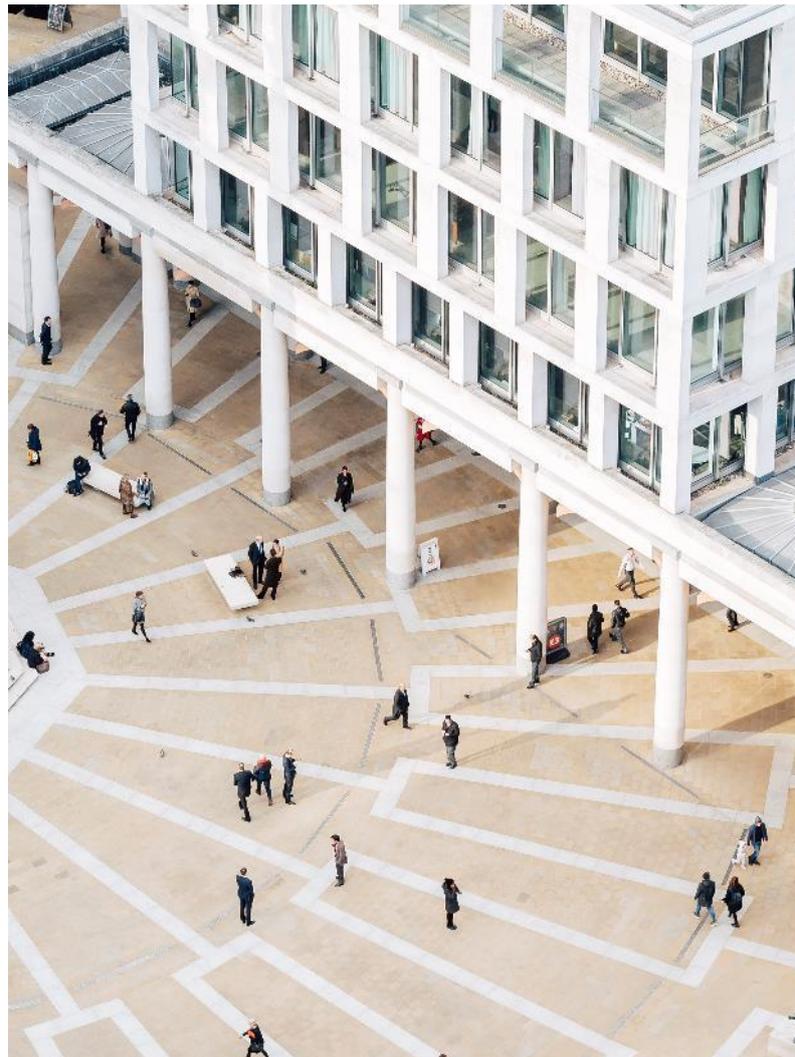
The broader picture here is that the UK's landscape of tax governance and reporting requirements is evolving at pace, including in areas such as the uncertain tax treatment disclosure consultation and HMRC's business risk review. The operational challenges for alternative investment funds in managing tax continue to increase – and staying on top of the day job while confronting additional imperatives is more challenging than ever.

## *Technology provides (part of) the answer*

In this regard, a recent PwC survey of alternative fund's tax functions had some revealing findings. Respondents said their top four issues were tax regulation, disputes, digital filings and technology. Budgets are increasing somewhat, but many tax functions think further headcount increases will be required. Other solutions may come into play – many respondents pointed to strategic or tactical outsourcing, or managed services, for example, but there is no one-size-fits-all approach to these issues.

Certainly, technology will be part of the picture. In PwC's survey, 77% of firms said they were increasing their focus on exploiting technology – and 75% said they were open to using technologies operated by external advisers. More advanced tools are now becoming available at pace, in areas such as workflow automation and data management, for example. But most firms are still heavily dependent on Excel spreadsheets.

COVID-19 may provide an accelerant here. In workplaces where face-to-face contact is no more – at least for now – increased automation and more seamless integration of systems and technologies will be vital. Data visualisation tools in particular provide really valuable opportunities for tax to stay on top of its workload. Improved data collection and analytics can help tax add significant value.



# COVID-19: is it time for a tax strategy reset? cont.

## Bringing it all together

In the end, however, technology is only part of the picture. Now may be the time for alternatives investment fund's tax functions to take a step back – to reconsider their purpose and to ask some fundamental questions. For firms that have not renewed their tax strategy and vision in recent times, are the tax function's objectives for the short and long term still relevant, how will they be achieved, and has this been documented?

With that vision in place, the tax function will bring a much sharper focus to the lens of governance and risk management. And considering how tax risk is managed across the organisation – from statutory obligations to operational risk, processes and skills – will take firms to the operational model. Is that model aligned to the business's priorities and structures? If not, how should the structures, processes and the approach to data be updated?

Debating those issues will eventually bring the tax function back to the practical challenges of its operational imperatives – and hopefully in a better position to deal with them effectively and efficiently. And for organisations just getting started with those debates, the questions below might help.

## 10 organisational questions for the tax function to answer...

- What is the overall purpose of the tax function and what role is it expected to assume?
- How should tax be organised, given this role?
- How does the tax strategy support and become an extension of the broader corporate strategy?
- How do you ensure that all post-transaction implementation actions have been addressed?
- How far should the tax function support underlying investments and portfolio companies?
- What processes do you need to support the business effectively and efficiently?
- What is the internal and external best practice that you can apply to tax processes?

- What technology can you deploy to enable the capabilities you desire?
- What skills and experiences should tax function staff possess?
- What are the high-priority issues to solve, and what timeline and resources are required?

## ...and 10 functional areas to cover

- Transaction support
- Budgeting, forecasting and management reporting
- Management of international structure and post-deal structural issues
- International tax policy impact monitoring
- Tax compliance across all taxes
- Tax authority relationship management
- Emerging reporting requirements - CBCR, transfer pricing documentation, BEPS and so on
- Tax governance and risk management reporting
- Board oversight, ESG reporting, public reputation management



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# UK – Corporate governance response to COVID-19 and its future

COVID-19 has forced alternative investment fund managers to act quickly and responsibly in relation to their corporate governance processes. In this article we have summarised some of the adaptations we have witnessed over the past few months in terms of how governance is being carried out in practice, as well as how they might influence the future of corporate governance.

## Virtual boards: focused and effective decision making

Virtual board meetings have quickly become the new norm and, on the whole, most AIFMs we have spoken to agreed that meetings had gone smoothly, and that non-executive directors had embraced the technology. A theme which has emerged in the industry is the strength and value of governance frameworks and the way in which they have enabled swift, but effective, decision making.

Also noteworthy in our discussions has been that ‘business as usual’ board meetings are returning, but the length of meetings has been reduced to accommodate video or teleconferencing. As a result, agendas have been sharper, prioritised and more strategic in focus. For example, ‘for information’ agenda items are being taken offline and circulated to directors (often using Board Portal technology) instead of appearing on board agendas.

A final element of note is the shift in both investor and boardroom dialogue towards environmental, social and corporate governance issues. Under s172 of the Companies Act 2006, company boards must focus on stakeholder engagement around principal decisions and, as a result board decisions and discussions have become broader, encompassing all stakeholders on an equal footing. At the company level, it has been important to document these discussions and demonstrate that directors have met their s172 obligations. Equally, COVID-19 has highlighted a number of important ESG issues that AIFMs

need to be alert to, not least in the context of the Disclosure Regulation and integrating ESG risks and opportunities into their investment decision-making and wider organisational processes. This has been particularly relevant in light of the virtual, and often “behind closed doors” format of shareholder meetings in recent weeks, which has made engagement on ESG issues more challenging.

## Decision-making and the SM&CR

Regulated entities have received additional input from the regulator due to COVID-19, and the continued need for SMFs to take reasonable steps in order to meet their prescribed responsibilities and evidence that fact, particularly given that decisions are being taken more quickly, often with imperfect information. Some AIFMs have found it useful to agree management information protocols which give the board, and SMFs, the information they need without distracting management from the task in hand. In some cases board papers have improved for the better as the relevant information has to be far more easily identified, as does the ask from the board.

The reach of some governance frameworks has also extended beyond the support provided to legal entity boards to management level governance forums that were looking for guidance to ensure that decision making was effectively taking place and being sufficiently documented throughout the business.

## Document execution

In the same way that Directors have quickly adapted to virtual board meetings, the use of digital or electronic signatures has become the norm. This approach has been accepted by management, third parties and most authorities. In many cases digital signatures have replaced previously time consuming manual processes. The use of powers of attorney has also been adapted during this period.

## Next steps for Alternative Investment Funds

The value of strong corporate governance has been highlighted in recent months and alternative investment funds have needed to embrace the changes highlighted above to an increasing extent.

Looking forward, it is expected that the new ways of working, the elevation of wider stakeholder considerations within the boardroom and in investment decisions, and the role that the company secretary/chief governance officer has played in enabling those changes, will continue into the future, changing

corporate governance for the better.

As alternative investment funds begin to navigate the release from lockdown, boards of directors should continue to keep their legal duty to consider the impact of a broad range of stakeholders at the forefront of decision making. Company secretaries/chief governance officers should also ensure that they are capturing these decision making processes and the impact on stakeholders to enable them to be reported on in their financial statements and their website at the end of the current financial year.



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## UK & EU – Whatever happened to Brexit?...

It is now June, the month when there are a number of key dates in the Brexit calendar, for example, the deadline for equivalence assessments to have been completed, the deadline for an extension to the transition period, and a high level summit to determine whether or not sufficient progress has been made for the talks to continue.

The UK's approach to the negotiations, published at the end of February, indicated that it would take stock of progress in June and determine whether or not to continue with the negotiations or whether to focus on planning for a no trade deal Brexit. However, indications are that the UK will not walk away from the talks at this stage, but will negotiate over the summer, with the aim of having made sufficient progress by September.

The UK is holding firm to its position not to extend the transition period, which allows it to temporarily preserve the cross-border passporting rights it had as a member state, from the current deadline of 31 December 2020. We understand that work on financial services regulatory equivalence assessments is being progressed by both sides. However, with limited time remaining until the UK must move away from the transitional arrangements the alternative funds industry is once again preparing for a number of potential outcomes.

Some form of 'equivalence' may well be agreed, but this currently remains uncertain. Many firms have been well advanced in their planning and preparations on previous occasions, such as March and October 2019 and even January this year.

For some firms this has involved the establishment of a regulated business presence in a new territory, with relocations of people and activities, design and implementation of cross-border operating models and transfer pricing, and development of relationships with new regulatory bodies.

A significant period of time has passed since the original Brexit date of 29 March 2019. The world has not stood still, and with that passage of time firms are likely to have seen material changes in investor appetite, fee pressures, management and business changes, local regulator expectations and of course the significant disruption

caused by COVID-19.

It may therefore be time for firms to revisit, rework or revise their original plans to ensure they are still fit for purpose in the new business environment.

Andrew Gray, chair of PwC's Brexit Steering Committee, recently shared what he has learned from conversations with clients on Brexit preparations and his eight 'no regret' decisions in [this article](#) on PwC's Beyond Brexit website.

Whilst not repeated here, he picks out a 'plan to be agile' as being more important than ever and this is likely to resonate, not just with firms thinking about their Brexit preparations, but also with the response of the industry to the COVID-19 pandemic.



## UK & EU – Whatever happened to Brexit?... cont.

So are firms' Brexit preparations still optimal to service the needs of the business in the post Brexit, post COVID-19 world? How would you respond if delegation of portfolio management activity from the EU to the UK was restricted?

Some of our clients are experiencing a changing business environment which has led them to diverge from operating models, transfer pricing policies and commitments to regulators that they made at prior stages in the Brexit process.

Some of these shifts are linked to common themes in to the alternative fund industry as a whole, so we urge all alternative fund managers reviewing their Brexit preparations to ask themselves:

- How has the pandemic and the increase in home-working affected the nature, location and frequency of decision making, at board meetings in particular?
- Temporary displacement and the increase in home-working, which may or may not become permanent, may put pressure on permanent establishment thresholds and transfer pricing policies. Are your people still working for the appropriate entity in the appropriate jurisdiction, in line with the operating model and regulatory commitments?
- Have your new hires and/or relocated employees ended up doing what you expected them to be doing? Where people are working part-time in different jurisdictions, is any time split agreed with regulators for substance purposes aligned to the actual business?
- Will fly-in support for EU Brexit structures be possible if travel bans and, or self isolation rules disrupt travel flexibility?



### Next steps for Alternative Investment Funds

Alternative investment funds should revisit, rework or revise their original Brexit plans to ensure they are still fit for purpose in the new business environment.

They should also ensure alignment with commitments made in regulatory licence applications and/or transfer pricing policies, or consider updating policies and renegotiating with regulators.



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# AIFMD Review – Assessing the application and the scope of the Alternative Investment Fund Manager Directive

In this article, we consider the recently published [report](#) by the European Commission (the ‘**EC**’) assessing the application and the scope of the Alternative Investment Fund Managers Directive (**AIFMD**).

By way of background, the AIFMD is a regulatory framework for alternative investment fund managers (**AIFMs**), including managers of private equity firms, hedge funds and investment trusts, which entered into application on 22 July 2013. The AIFMD required the European Commission to commence a review of the Directive by July 2017 to establish whether its objectives were being met and, if necessary, to propose appropriate amendments. The first stage of that review was completed last year with the publication on 10 January 2019 by the European Commission of the [report](#) it had commissioned into the operation of the AIFMD, intended to ‘provide and assess evidence’ for the European Commission’s review (the “**Report on the operation of the AIFMD**”).

The European Commission has now released its own [report](#), in which findings included in the Report on the operation of the AIFMD are complemented by other sources of information, including from European Securities and Markets Authority (ESMA) and the European Systemic Risk Board (ESRB). Although the report does not at this stage provide a clear way forward, the issues it has flagged can be expected to be the subject of further scrutiny in the months and years ahead as the review process continues.

## Key Message - Growth of EU AIF Market

The key message from the report is a positive one: the EU alternative investment fund (“**AIF**”) market has been on a continuous growth with notable cross-border activity of AIFMs. Since the adoption of the AIFMD in 2011, total net assets of AIFs have more than doubled in size from € 2.3 trillion to € 5.9 trillion. There has also been an increased retail investor participation in several Member States.

The depositary regime, rules on conflicts of interest, disclosure and transparency requirements are seen to have built investor confidence in financial markets and to have largely achieved their objectives.

## Key Findings

There are, however, aspects of the AIFMD that have not contributed, or may run counter to, the achievement of creating an internal market for AIFs and a harmonised and stringent regulatory environment for AIFMs. We have highlighted below the key points highlighted by the EC in the report:

### Access to markets

Although access to national markets has increased due to the AIFMD, in some cases, the time to market has increased. The AIFM passport is declared to have been an “important factor” in the growth of the EU AIF market but its impact has been impaired by some countries choosing to impose additional requirements, divergences in the national marketing rules, varying interpretations of the AIFMD by national supervisors and its limited scope. Moreover, the AIFM passport allows marketing only to professional investors, again restricting the cross-border activities of AIFMs as semi-professional and retail investors can only be approached under varying (and often restrictive) national rules. Small AIFMs looking to raise capital in other member states would also have to look to the national rules imposed in such member states.

### National Private Placement Regimes

National Private Placement Regimes (**NPPRs**) allow AIFMs to market AIFs that are not allowed to be marketed under the AIFM passporting regime (such as third country non-EU AIFMs). The role of NPPRs is acknowledged to have been an important factor in market development given the absence of the AIFM passport for third-country managers. However, as NPPRs differ among member states, it has created an unequal playing field between EU and non-EU AIFMs. A potential solution would be the activation of the third country passport and the report notes that this has been suggested by some member states with some other member states favouring harmonisation of the NPPR requirements.

# AIFMD Review – Assessing the application and the scope of the Alternative Investment Fund Manager Directive cont.

## Other issues identified in the report, include:

**Depositaries:** The lack of a depositary passport is at odds with the EU’s single market approach. Given the limited choice of service providers in smaller markets, there are fears of concentration risk where a single depositary could hold the assets of all AIFs established in a member state.

**Valuation:** The AIFMD brought some structure to the AIF asset valuation process, but there are some issues with the binary choice in the valuation rules between internal or external valuation, as well as uncertainty about the liability of external valuers.

**Supervisory reporting requirements:** Some of the AIFMD reporting requirements may not be essential, and some may be insufficient or duplicative. Therefore, further streamlining might be needed with regards to supervisory reporting requirements.

**Lending:** The trend of expanding non-bank lending raises financial stability concerns, thus there might be a need to reassess the case for setting common standards for loan-originating AIFs.



## Next steps for Alternative Investment Funds

The European Commission is still assessing the need for further proposals to amend the AIFMD.

It should be noted that some of the areas highlighted in the report have been tackled in other legislative reforms, such as the package on cross-border distribution of funds. However, other areas outlined in the report could possibly require further action at European Union level to deepen the European market for AIFs and to ensure that the AIFMD legal framework is fit for

purpose.

It is believed that any consultation to make potential amendments to the AIFMD will be issued by the EC this summer (although COVID-19 may impact this timetable). For now, we would recommend AIFs and AIFMs to continue to monitor this review process closely including any consultation that may be issued by the EC.



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200206-154355-ML-OS