

Brexit – 5 days to go for applying for the Luxembourg transitional period

09 September 2019

Three questions relevant for UK managers still considering whether to apply or not

1. We are a UK manager acting as portfolio manager based on a delegation from a Luxembourg AIFM or UCITS management company. Should we file the CSSF Brexit notification form for MiFID firms?

No. The CSSF has confirmed that UK managers that are exclusively providing portfolio management services based on a delegation from a Luxembourg authorised AIFM or UCITS management company (and without establishment in Luxembourg) do not have to fill in the CSSF questionnaire for MiFID firms.

Those UK managers will be in a position to continue providing the relevant portfolio management services post-hard Brexit, subject to the AIFMD/UCITSD delegation rules. This assumes – and we understand from the CSSF press release 19/05 that it is safe to make this assumption – that a cooperation agreement will be in place in time between the FCA and the CSSF.

Although MiFID II remains silent on this point, there seems to be a general consensus that the provision of portfolio management services to an AIFM or UCITS management company is only subject to the AIFMD/UCITSD rules on delegation of portfolio management and is not caught by the rules regarding the provision of cross-border MiFID services.

For the avoidance of doubt, the above only holds true where the AIFMD/UCITSD rules on delegation of portfolio management apply, which is not the case for instance if the UK manager is providing:

- other MiFID services to the Luxembourg AIFM or management company (eg, investment advice or reception and transmission of orders);
- portfolio management (or any other MiFID services) to any other Luxembourg client (eg, SPVs of the funds under management or investors in the funds under management); or
- portfolio management (or any other MiFID services) to a Luxembourg fund (or the GP of a fund) that is exempted from the AIFMD.

In those circumstances, the UK manager is performing a MiFID activity that (under the current regime) must be passported into Luxembourg and the UK manager should therefore complete the CSSF Brexit notification form for MiFID firms by 15 September 2019 if it wants to benefit from the 12 month transitional period.

2. We are acting as UK AIFM of a Luxembourg AIFMD-compliant AIF. If we were not to apply with the CSSF to benefit from the 12 month transitional period, would the Luxembourg AIF be automatically converted into an AIFMD-exempt AIF on the date of hard Brexit?

Luxembourg AIFs managed by a non-EU AIFM currently benefit from an exemption and may choose not to comply with the requirements of the AIFMD (in which case they do of course not benefit from the AIFMD marketing passport).

If a Luxembourg AIFMD-compliant AIF is managed by a UK duly authorised AIFM which does not apply with the CSSF for the 12 month transitional period (a “non-grandfathered AIFM”), would that AIF not be automatically converted into an AIFMD-exempt AIF on the date of hard Brexit? This might appear to be an attractive solution, in particular if the relevant AIF is no longer marketed within the EU (and the loss of the AIFMD marketing passport is therefore not an issue).

To the best of our knowledge, there is no regulatory guidance available, whether at EU or Luxembourg level, on conversions of AIFMD-compliant vehicles into AIFMD-exempt vehicles. For AIFs that have been marketed outside of Luxembourg on the basis of the AIFMD marketing passport, the consequences of such a conversion should not only be analysed from a Luxembourg regulatory standpoint but also under the rules applicable in the countries where the relevant funds have been marketed. How would local regulators look at a Luxembourg AIF that has been marketed in their country as an AIFMD-compliant vehicle and converted afterwards into an AIFMD-exempt vehicle, which does no longer offer the same level of investors’ protection?

For Luxembourg regulated funds (SIFs, SICARs or Part II funds), the conversion into an AIFMD-exempt vehicle would be subject to CSSF approval. Those applications would be subject to a case-by-case review but the CSSF is unlikely to give its approval without obtaining confirmation that all investors agree with the conversion and that local regulators in the countries where the fund has been marketed do not oppose the change. And AIFMs/AIFs which do not act proactively (eg, by applying for the transitional period) will probably have a hard time explaining (to regulators and investors) that the occurrence of hard Brexit is a sudden or unforeseen event.

For Luxembourg AIFs which are not subject to CSSF supervision (eg, unregulated SCSs/SCSps) and have not been passported by the UK AIFM into Luxembourg for marketing, the CSSF would have no say over the conversion into an AIFMD-exempt vehicle. Ultimately, it would be up to the Luxembourg courts to determine if such a conversion is compatible with Luxembourg laws. But, even if such conversion were in line with Luxembourg law, the conversion would also have to be effected in compliance with the relevant fund documents. Does the conversion constitute a change which is subject to investor consent? This requires a careful analysis of the relevant fund documents.

Even if one were to consider that an AIF managed by a UK non-grandfathered AIFM would “automatically” be converted into an AIFMD-exempt AIF on the date of hard Brexit, this would create a disconnect between the fund documents (which will still be referring to an AIFMD-compliant vehicle) and the new regulatory status of the AIF and its AIFM (non-AIFMD compliant). Until the situation is clarified (through an amendment of the fund documents and, if applicable, regulatory approval), there may be uncertainties around the rules governing the fund and its agents. Will the depositary of the relevant AIF still be subject to the AIFMD depositary regime? Will its AIFM still be subject to the detailed obligations and stringent liability regime (eg, vis-à-vis delegates) under the AIFMD?

The Luxembourg 12 month transitional period is useful as it allows AIFMs/AIFs to eliminate the above risks and legal uncertainties. Luxembourg AIFs managed by a “grandfathered” UK AIFM will, from a Luxembourg perspective, benefit from a status quo until the end of the transitional period. From a Luxembourg regulatory standpoint, it will be as if no Brexit had occurred. They will have until the end of the transitional period to restructure themselves (through the appointment of an EU AIFM, a liquidation or, if at all permitted, a conversion into an AIFMD-exempt vehicle) and amend their fund documents accordingly. Until then, the AIF and its agents (including the AIFM and its depositary) will remain fully subject to the AIFMD regime. This is of course limited to Luxembourg and marketing in other EU member states will be subject to local laws.

3. We are a UK AIFM and we are intending to apply with the CSSF to benefit from the 12 month transitional period. We are asked in the CSSF questionnaire to indicate what the post-Brexit status of the relevant Luxembourg AIFs will be (after the end of the transitional period). However, there are only two options available in the questionnaire (appointment of a duly authorised EU AIFM or liquidation). How should we answer this question if we want to keep options open or would like to retain another option (eg, conversion into an AIFMD-exempt vehicle)?

It is no surprise that, in light of the above uncertainties, the CSSF questionnaire does not list the conversion of a Luxembourg AIF into an AIFMD-exempt vehicle as a post-Brexit option. This option requires a complex case-by-case analysis and has ramifications which exceed the remit of the CSSF.

In our view, the CSSF seeks to ensure that UK AIFMs that apply for the transitional period realise that this regime is temporary and that actions will have to be taken before the end of the transitional period. Again, it is no surprise that the appointment of an EU AIFM in replacement of the UK grandfathered AIFM seems the more natural option for the CSSF (alongside the more extreme option of liquidating the fund). AIFMs/AIFs that want to pursue another avenue (eg, conversion into an AIFMD-exempt vehicle) must carry out their own analysis and, if relevant, seek appropriate regulatory approvals.

In any case, the CSSF form is a mere questionnaire and certainly not an unconditional and irrevocable undertaking from the relevant AIFM to either liquidate the relevant AIF(s) or appoint another EU AIFM by the end of the transitional period. AIFMs are asked to indicate what they expect – at the time of filling in the questionnaire – the relevant AIF will do by the end of the transitional period (and, by the way, AIFMs may not have control over that in all circumstances). In cases where, before the end of the transitional period, there would be a change of plan, the CSSF would simply have to be informed accordingly.

Also, Brexit being quite unpredictable, other options which are not covered in the CSSF questionnaire may be available by then, depending on legal and political developments.

For regulated AIFs (SIFs, SICARs or Part II funds) for which it is intended that an EU AIFM be appointed before the end of the transitional period, the UK AIFM is required under the CSSF questionnaire to ensure that an application (for the approval of the new EU AIFM) be submitted to the CSSF by 31 October 2019 at the latest. This aims at making sure the CSSF will have the time to properly review applications. It is expressly provided that all dates in the questionnaire are “based on the assumption of a no-deal Brexit date on 31 October 2019”. We therefore expect that, if Brexit is further delayed, the 31 October deadline will also be postponed.

Finally, it should be noted that the CSSF will assess each notification received and inform firms and/or the relevant regulated Luxembourg AIFs individually as to whether they can benefit or not from the transitional regime. For the purpose of the assessment, the CSSF will check that applicable conditions for benefitting from the transitional period are met and, in particular, that the relevant firm has duly passported its services to Luxembourg in the past and that the information provided in the notification on its activities is consistent and sufficiently detailed.

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If you would like to discuss the issues raised in this paper in more detail, please contact any of the experts above or your usual Allen & Overy contact.

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