

Financial Markets Law Committee (“FMLC”)

Asset Management Scoping Forum

Date: Thursday 22 February 2018

Time: 1.30pm to 3.00pm

Location: Travers Smith LLP, 10 Snow Hill, London, EC1A 2AL.



In Attendance:

Philip Bartram (Chair)	Travers Smith LLP
Iain Cullen	Simmons & Simmons LLP
Christopher Dearie	MJ Hudson
Martin Ferreiro Subi	BlackRock
David Gasperow	Orbis Investments
Jonathan Gilmour	Travers Smith LLP
Monica Gogna	Dechert LLP
Mark Kalderon	Freshfields Bruckhaus Deringer LLP
Kirsten Lapham	Ropes & Gray International LLP
Owen Lysak	Clifford Chance LLP
Michelle Moran	K&L Gates LLP
Neil Robson	Katten Muchin Rosenman UK LLP
Sarah Smith	Akin Gump LLP
Jennifer Enwezor	FMLC
Thomas Willett	FMLC

Guest Speakers:

Ida Levine	Capital International Limited
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Guest Observers:

Clarke Camper	Capital International Limited
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Registered Charity Number: 1164902.

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Regrets:

Matthew Baker	Berwin Leighton Paisner LLP
Gregg Beechey	Fried, Frank, Harris, Shriver & Jacobson (London) LLP
Antony Bryceson	AB Trading Advisors
Richard Chapman	AB Trading Advisors
Henrietta de Salis	Willkie Farr & Gallagher (UK) LLP
Julian Eustace	Schroders Investment Management Ltd
Jon May	Marshall Wace LLP
Shenell Page	CQS (UK) LLP
Martin Parkes	BlackRock
Bob Penn	Cleary Gottlieb Steen & Hamilton LLP
Selina Sagayam	Gibson, Dunn & Crutcher LLP
Martin Sandler	PricewaterhouseCoopers LLP
Palvi Shah	J P Morgan Asset Management

Minutes:

1. Introduction.

1.1. Philip Bartram opened the meeting and delivered a brief introduction.

2. Administration: a short presentation on the FMLC Radar Function – Revisited (Jennifer Enwezor)¹

2.1. Jennifer Enwezor outlined the remit of the FMLC and its radar function, defined as the manner in which the FMLC identifies appropriate issues to analyse. The function can be broken down into three initiatives: (i) scoping forums; (ii) the relationship management programme; and (iii) radar meetings. She explained that the radar programme guarantees that the FMLC addresses those issues that are of most concern to stakeholders in the financial markets, ensuring that the FMLC’s work is current and has impact.²

¹ Please see Appendix I below.

² If you would like to learn more about the FMLC radar programme, or become involved in one of the three initiatives, please contact Debbie Steen at secretarial@fmlc.org.

3. Remarks on the asset management industry (Michelle Moran)

- 3.1. Michelle Moran delivered a few introductory remarks on issues of legal uncertainty pertaining to the asset management industry.
- 3.2. Ms Moran identified Brexit as the foremost issue of uncertainty at present. The European Commission's notice to stakeholders in the asset management industry was cited.³ She explained that this notice highlights some of the primary legal and regulatory consequences arising from the U.K.'s transition to becoming a Third Country following Brexit. The notice also serves to remind stakeholders of the need to assess the potential impact Brexit may have on their businesses and to plan appropriately. Ms Moran stressed that asset managers have to look at real solutions to take their own actions in the midst of this uncertainty.
- 3.3. One participant mentioned the FMLC Brexit Advisory Group which meets quarterly and provides a space for discussion of current and future issues of legal uncertainty affecting the wholesale financial markets that relate to the British secession from the E.U. As a member of the Brexit Advisory Group, the participant offered to relay any issues of legal uncertainty concerning the asset management industry and Brexit to the group for their consideration.⁴

4. E.U. Regulation: Third Country perspective (Ida Levine)

- 4.1. Ida Levine's presentation focused on the application of E.U. regulation from a Third Country perspective.
- 4.2. Ms Levine began by highlighting how the issues of negotiating access to the global markets are not new. With the rise of technology and globalisation, the financial markets have become interconnected with regulators and scholars searching for solutions to provide access across the global markets without duplication of procedures or conditions or unnecessary complexity. Early attempts at solutions have been made, said Ms Levine, drawing attention to Ethiopia Tafara and Robert J. Peterson's 2007 work on cross-border access.⁵

³ European Commission, "Notice to Stakeholders, withdrawal of the United Kingdom and E.U. rules in the field of asset management", (8 February 2018), available at: https://ec.europa.eu/info/sites/info/files/180208-notice-withdrawal-uk-asset-management_en.pdf

⁴ For further information concerning the FMLC Brexit Advisory Group or to suggest agenda topics for future meetings, please contact Rachel Toon at executivesupport@fmlc.org.

⁵ Tafara and Peterson, "A Blueprint for Cross-Border Access to U.S. Investors: A New International Framework", (2007), 48(1), available at: <http://www.grahambishop.com/DocumentStore/Tafara-Peterson.pdf>.

- 4.3. Passporting access for U.K. Undertakings for Collective Investment in Transferable Securities (“UCITS”) management companies and Alternative Investment Fund (“AIF”) managers was discussed next. Ms Levine explained how passporting rights allow firms registered in one E.U. Member State (the “**home jurisdictions**”) authorisation to set up branches and provide cross-border services in other Member States. These permissions, however, will be withdrawn and U.K. UCITS and AIF managers will no longer benefit from authorisation should the U.K. become a Third Country following withdrawal from the E.U.
- 4.4. Alongside the European Commission’s notice, mentioned in 3.2. above, Ms Levine drew attention to Opinion published by the European Securities and Markets Authority (“ESMA”) on “General principles to support supervisory convergence in the context of the United Kingdom withdrawing from the European Union” published in May 2017.⁶ The Opinion sought to provide a practical tool to achieve supervisory convergence, and Ms Levine highlighted that it set out substance requirements which national competent authorities (“NCAs”) should meet. In this way, the ability of NCAs to efficiently and effectively authorise and supervise firms should not be hindered. One Forum member queried the use of Opinions which may itself give rise to legal uncertainty, emphasising the difference between an opinion and legislation.
- 4.5. The participants then discussed the issue of delegation post-Brexit. Delegation allows an asset manager to set up a fund in one E.U. Member State and outsource the portfolio management to investment staff in another Member State. Ultimately, members concluded that many uncertainties surrounding delegation were political, rather than legal, in nature. They did highlight, however, that it was unclear as to which aspects of the Directive 2014/65/EU on markets in financial instruments (“**MiFID II**”) could be performed by delegates.
- 4.6. Owing to time restrictions and as the next agenda item addressed MiFID II directly, it was deemed appropriate to move onto the next topic of discussion.

⁶ ESMA, “General principles to support supervisory convergence in the context of the United Kingdom withdrawing from the European Union”, (31 May 2017), available at: https://www.esma.europa.eu/sites/default/files/library/esma42-110-433_general_principles_to_support_supervisory_convergence_in_the_context_of_the_uk_withdrawing_from_the_eu.pdf.

5. Unresolved issues under MiFID II (Mark Kalderon)

- 5.1. Mr Kalderon, who had chaired an FMLC Working Group on legal uncertainties arising from MiFID II, presented some unresolved issues under the legislation.
- 5.2. Continuing from Ms Levine's talk, the issue of delegation under MiFID II was discussed. Following correspondence between the Financial Conduct Authority ("FCA") and the Alternative Investment Management Association ("AIMA"), as well as subsequent related correspondence between The City of London Law Society and the FCA, two approaches around the expectations on the application of certain MiFID II requirements became apparent, specifically on the application of Article 24(8) where management is delegated to a Third Country service provider. Mr Kalderon outlined these approaches wherein either:
 - i. the full suite of obligations under MiFID II continue to apply, with the firm required to impose obligations contractually on the service provider; or
 - ii. the firm ensures that outsourcing is in the clients' best interest.
- 5.3. Mr Kalderon articulated that the FCA's correspondence emphasised that where an investment firm outsources part of the portfolio management service provided to their clients under MiFID II, it would need to take steps to ensure an equivalent level of protection for its clients under a delegation agreement. Two possible justifications for the second approach then become evident: (i) MiFID II only applies to activities actually carried out by a firm; and (ii) MiFID II only applies to activities carried out from a U.K. establishment.
- 5.4. The participants agreed that delegation under MiFID II should be placed on the agenda for a future meeting of the Asset Management Scoping Forum.
- 5.5. Another key unresolved issue under MiFID II identified by Mr Kalderon was that of costs and charges; in particular, the need for *ex ante* disclosure of existing discretionary management arrangements. Members thought that it was not common practice to make such disclosure in respect of mandates in existence when MiFID II came into force. A lack of uniform methodology in calculating transaction costs and the inclusion of market movements was highlighted as particular concerns.

5.6. Lastly, Article 44 of MiFID II and FCA Conduct of Business Sourcebook (“COBS”) 4.5A.1R were discussed.⁷ Here, an issue occurred over the question of when a financial promotion relates to the firm’s MiFID business and when does it not. Mr Kalderon elaborated by describing a scenario in which a MiFID segregated investment manager provides services to a UCITS management company in respect to the management of a UCITS, and separately issues a financial promotion to prospective investors in the UCITS. Members identified the question whether this could as an area of legal uncertainty be classed as a financial promotion which “relates to” a firm’s MiFID business.

6. Any other business

6.1. Mr Bartram introduced a discussion on Regulation 28(10) of The Money Laundering, Terrorist Financing and Transfer of Funds Regulation 2017 with regards to customer due diligence.⁸ The legislation provides that

Where a person (“A”) purports to act on behalf of the customer, [a regulated firm] must: (a) verify that A is authorised to act on the customer’s behalf; (b) identify A; and (c) verify A’s identity.

Mr Bartram articulated that it is unclear whether this requires a firm to verify the identity of authorised signatories in every case. Referring to the draft guidance from The Law Society,⁹ the Joint Money Laundering Steering Group (“JMLSG”)¹⁰ and (E.U.) 2015/849 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing (“MLD 4”),¹¹ Mr Bartram suggested that it may be possible to conclude that when a firm is dealing directly with a corporate customer, no other person/entity is acting on behalf of that corporate customer. Its authorised representatives are internal to the customer rather than external. It, therefore, does not seem attractive to make a distinction between an individual signing “on behalf of” or “by” the company.

⁷ FCA, Conduct of Business Sourcebook, (2018), available at: <https://www.handbook.fca.org.uk/handbook/COBS.pdf>.

⁸ *The Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017*, available at: http://www.legislation.gov.uk/uksi/2017/692/pdfs/uksi_20170692_en.pdf.

⁹ Legal Sector Affinity Group, “Anti-Money Laundering Guidance for the Legal Sector, (2017), available at: <http://www.lawsociety.org.uk/policy-campaigns/articles/draft-anti-money-laundering-guidance/>.

¹⁰ JMLSG, “Prevention of money laundering/combating terrorist financing”, (2017), available at: <http://www.jmlsg.org.uk/industry-guidance/article/jmlsg-guidance-current>.

¹¹ *MLD 4 2015*, available at: http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=OJ:JOL_2015_141_R_0003&from=ES.

6.2. Attendees agreed to return to this topic at a future meeting for further consideration.

The FMLC Radar Function: *revisited*



Jennifer Enwezor, Project Manager

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FMLC Remit

“The role of the Financial Markets Law Committee (the "FMLC" or the "Committee") is to identify issues of legal uncertainty, or misunderstanding, present and future, in the framework of the wholesale financial markets which might give rise to material risks, and to consider how such issues should be addressed.”

FMLC Foundational Documents, September 2002



FMLC Mission



- According to the remit, the FMLC has a tripartite mission:
 - to identify relevant issues (the **radar** function);
 - to consider such issues (the **research** function); and
 - to address such issues (the **public education** function).
- The **radar function** relies on the FMLC’s **scoping forums** and other horizon-scanning, advisory bodies. It also relies on a **relationship management programme** which the FMLC Secretariat maintains with Patrons and Stakeholders.
- The **research function** is addressed by the FMLC Secretariat and by highly-focused working groups who work to draft papers and correspondence on behalf of the FMLC.
- The **public education function** is furthered when the FMLC publishes these letters and papers. It is also addressed by the regular programme of events organised by the FMLC Secretariat, including: roundtables, seminars and conferences. These feature high-profile guest speakers.

Breaking down the radar function

The FMLC's radar function is (broadly) broken down into three initiatives:

1. **Scoping forums**
2. **Relationship management programme; and**
3. **Radar meetings**



Scoping Forums

“Scoping forums serve as an avenue for the FMLC to engage with focus groups on legal issues affecting specific segments of the financial markets.

The forums serve as spaces for discussion of broader issues of legal uncertainty. Members formulate and propose to the FMLC issues considered by them to cause substantive legal uncertainty to their industry.”

FMLC Brochure, January 2017



Scoping forums in practice

- A scoping forum establishes a **pool of expertise** available to the FMLC. That pool can guide the FMLC by **recommending specific issue to the FMLC for analysis**.
- Scoping forum members can make non-binding suggestions as to the manner of the FMLC's engagement and nominate experts for working groups.
- Meetings include presentations from industry experts, individuals with first-hand experience of legal uncertainty and those at the cutting edge of their respective fields.
- Scoping forums discuss all manner of topics, issues and solutions within their sector.
- Not every issue discussed will go on to become an issue adopted by the FMLC. Scoping forums are horizon-scanning bodies and places to share and compare knowledge. They are about **learning and discovery** as much as they are about **identifying specific issues for further consideration**.
- Information about the FMLC's scoping forums—as well as the agenda and minutes of all 2017 meetings—can be found on our website at: <http://www.fmlc.org/scoping-forums.html>

Relationship management

- Another key aspect of the radar function, the FMLC's **relationship management programme**, ensures regular communication and information exchange between the FMLC Secretariat and Patrons, Members or other stakeholders.
- Relationship management calls provide a valuable opportunity for participants to highlight issues—both present and future—for the FMLC to investigate, providing the FMLC with up-to-date and market-relevant information. They also allow the FMLC Secretariat to update Patrons and stakeholders on the Committee's recent work.
- FMLC Patrons have calls monthly. We organise calls with a predetermined list of stakeholders according to their appetite for engagement.
- Monthly relationship management calls normally last around 15 minutes. If you're a Patron who'd like to participate in your firms' monthly call (as an alternate perhaps), or if you'd like to receive a stakeholder call, let us know!



Radar meetings

- FMLC Chief Executive Joanna Perkins regularly meets with financial markets participants to discuss issues of legal complexity.
- These meetings are an excellent opportunity for the exchange of information. Participants can:
 - raise issues of concern or interest in relation to legal complexity, and
 - learn about the FMLC’s recent work and insights, get updates on forthcoming publications or—in the case of new contacts—learn more generally about the work and remit of the FMLC.
- Please speak to a member of the Secretariat if you are interested in arranging a meeting with your firm or organisation.

Information exchange

- The Radar programme guarantees that the FMLC addresses those issues that are of most concern to stakeholders in the financial markets, across the public and private sector.
- It also helps to ensure that the FMLC only addresses in depth issues that are material and may have an appreciable impact on the international wholesale financial markets.
- Together, these three Radar initiatives ensure our work is current and has impact.



Summary and Conclusion



To sum up...

- The FMLC is tasked with identifying, considering and addressing **legal uncertainty**...
- ...which is sometimes better thought of as “legal risk”.
- The **radar function** is the manner in which the FMLC identifies appropriate issues to analyse.
- The radar function is fulfilled through **scoping forums, relationship management calls, and radar meetings**.
- At this time, the FMLC Secretariat would be grateful for help with **assessing legal risks, identifying priorities and selecting issues for further work**.