



Time is of the essence

A compression of legal negotiations around AIFMD to the last months and weeks is not in anybody's interest, says Rolf Bachner

The transition period for the Alternative Investment Fund Managers Directive (AIFMD) is drawing to a close. The 12 months from 22 July 2013 to 22 July 2014 seemed like a reasonable transition period for managers falling into the scope of the directive. However, a study BNY Mellon conducted in December 2013 assessed how far the fund management industry still has to go in preparing itself for compliance. The study measured preparedness by asking managers if they had already submitted their application for authorisation to their regulator.

Only 12 percent answered that they had. This means that a full 88 percent of managers were planning to submit their authorisation, and demonstrate their compliance, in the second half of the transition period. There are number of reasons behind these statistics, such as complexity, resource challenges, work on other regulations, volume of work. If we were to run the survey again today we would not be surprised to see a substantial number of respondents still planning to submit their application in the remaining months. If this is the case, this would mean that the industry is pushing an ever growing pile of pending authorisation requests ahead of itself and is thereby condensing the effort required to a shorter and shorter time-frame.

Regulators are aware of this scenario. Some regulators have actively encouraged earlier submissions, probably with the intent to reduce the concentration of their own efforts to the very last weeks, as well as in recognition of the risk of non-compliance for the industry as a whole. Some regulators are also issuing, and continuously updating, Q&A documents. These papers and other

guidance documents constantly provide further detail as to how a manager should comply. And, it is also through these papers that divergences between the regulatory regimes become apparent—sometimes through what is said and sometimes through what is not said. Some regulators appear more willing to give further guidance on the way the directive should be applied in practical terms. Other regulators are less forthcoming. They may be waiting to see how other regulators and the industry address the practical issues that the directive is creating. Questions relating to the optional fields in the AIFMD regulatory report, the depository cash monitoring as well as asset segregation are but a few examples of issues where, at this point in time, there is a perceived regulatory divergence.

Managers are therefore also faced with the task of weighing up the benefits of early compliance versus the advantages of a late submission. A few managers submitted their application for authorisation almost a year ago. A few were already authorised and compliant with AIFMD on 23 July 2013. These managers have been able to lay down the basis for increased distribution and asset gathering, through the passport, at an early stage. Managers who have complied early have also reduced their compliance risk. This means that these managers have a head start and can now focus on, and divert effort to, other regulatory, performance and cost reduction initiatives.

The managers who choose to submit their application for authorisation late may have several reasons to do so. One reason may be a 'let's wait and see' approach. Best practice takes some time to form

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and managers who choose to apply later in the transition period have better access to best practice. Additionally, regulators, consultants, lawyers, service providers and industry associations are still developing best practice. A late application and use of industry best practice can therefore reduce both compliance cost and compliance risk. This should, however, be put in contrast with the challenges to comply as the time available is getting shorter and there is more and more demand on the same consultants, lawyers and service providers from an increasing number of managers. A legal contract takes a certain time to negotiate. An IT project often takes longer than planned. A compliance effort conducted in emergency mode does not allow for strategic considerations, such as a review of the number and function of group management companies, fund platform consolidations, re-domiciliations, or conversions from or to UCITS.

And the list of compliance tasks is long. There may be a tendency to focus on operating conditions and organisational requirements. Compliance with remuneration provisions has, for example, gathered many headlines. But even this is only one of the internal compliance tasks that managers typically have to consider. Complying with the risk management, valuation and liquidity management provisions will be potentially challenging—especially when compliance is done in the spirit of the directive rather than merely to the letter of the law.

An internal focus may reduce the resources available on the delegated tasks. The depository needs significantly more information under AIFMD to discharge its duties. The scale of this information

requirement should not be underestimated. It is the manager's obligation to ensure the depository receives the required information in a timely manner from the manager itself as well as its delegates. The contract with the depository is possibly also the largest 'AIFMD legal building site'. A compression, at an industry level, of legal negotiations to the last months and weeks is not in anybody's interest.

The regulatory report is another external building site that many managers may focus less on now as assumptions are made, such as 'our administrator does our reporting now, this is just more of the same'. The AIFMD regulatory reporting scope is, however, beyond any fund regulatory reporting in Europe today. Many commentators ask the legitimate question: "what are the regulators going to do with all that information?" The US Form PF reporting experience is a practical reference for the scope and scale of the AIFMD reporting requirement. The fund administrator simply does not have all the available information and the manager must deliver a large part of it, especially as it relates to portfolio and risk data.

On balance, we should recognise the diversity of funds and managers that need to comply with AIFMD. This means the learning curve for some is much steeper and the work required to comply more challenging. For some, AIFMD has led to a review and re-shaping of some of their funds, creating more work, if not directly AIFMD related. This also helps to explain the seeming delay in compliance. The work on AIFMD will not end on 23 July 2014, and the impact of this new directive will continue to play out for some time yet. **AST**

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