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UK Authorised
Investment
Funds



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Introduction

There are currently four types of fund structure that may be formed in the UK and which may be authorised by the FCA for sale to retail clients, namely:

1. Authorised open-ended investment company (OEIC), also known as an investment company with variable capital (ICVC);
2. Authorised unit trust (AUT);
3. European long-term investment fund (ELTIF); and
4. Authorised contractual scheme (ACS).

This note will focus solely on the first two fund structures i.e. OEICs and AUTs.

It is possible to establish either an OEIC or an AUT as:

1. a UCITS scheme;
2. a non-UCITS scheme (NURS); and/or
3. a qualified investor scheme (QIS).

Both OEICs and AUTs are collective investment schemes for the purpose of the Financial Services and Markets Act 2000 (FSMA). OEICs and AUTs which are not UCITS will also be deemed to be alternative investment funds (AIFs) for the purpose of the Alternative Investment Fund Managers Directive (AIFMD) and therefore subject to the provisions of the AIFMD Directive, while OEICs and AUTs which are UCITS will be subject to the provisions of the UCITS Directive.

The regulations governing each scheme are very similar, other than in relation to a small number of technical areas where company law or trust law so dictates. The ACD of an OEIC and the Manager of an AUT (each as further described below) are subject to identical requirements, as are the Depositary and the Trustee (again, as further described below). In practice, it is very common for fund managers to manage both

OEICs and AUTs and for firms to act as both depositaries and trustees.

The following discussion does not discuss the varying types of schemes noted above, but will cover the following points in relation to both OEICs and AUTs:

1. the governing regulations of each scheme;
2. the key entities involved in the scheme;
3. principal documentation required; and
4. the FCA application process.

Authorised open-ended investment companies (OEICs)

Authorised OEICs are established in the UK under a corporate structure, similar to that for a company, but under a code which is almost entirely separate from the Companies Act 2006. OEICs are governed by the *Open-Ended Investment Companies Regulations 2001 (SI 2001/1228)*, as amended (OEIC Regulations) and OEICs are subject to the FCA's rules set out in the Collective Investment Schemes sourcebook (COLL). As mentioned above, an OEIC will also be subject to the AIFMD, and thus the FCA's rules in the Investment Funds sourcebook (FUND), or the UCITS Directive, as applicable.

Please note that it is still not possible to establish an unauthorised OEIC in the UK.

Unlike an AUT, OEICs are bodies corporate and have a separate legal personality. The OEIC owns its portfolio of investments and shareholders in an OEIC simply own shares in a company and will have no beneficial interest in the underlying portfolio.

OEICs may be structured as single funds or umbrella funds with one or more sub-funds. The OEIC Regulations were amended in 2011 to provide for a protected cell regime which ring-fences the assets of each sub-fund. Under the amended provisions, sub-funds are segregated portfolios of assets and, as such, the assets of a



sub-fund belong exclusively to that sub-fund and shall not be used to discharge the liabilities of any other of the OEIC's sub-funds or the general liabilities of the umbrella OEIC itself.

Authorised Corporate Director (ACD)/Manager

Under the OEIC Regulations, an OEIC must have at least one director, although additional directors are allowed. If the OEIC has only one director, it must be an authorised corporate director (ACD). The ACD must be an authorised person under FSMA. In essence, the ACD runs the day-to-day operations of the OEIC and where the ACD is the sole director, this means that it will also be the manager. In practice, almost all OEICs have only one director, which is the ACD. References in this note to the ACD shall therefore include reference to the ACD as the manager of the OEIC.

Depositary

The Depositary has oversight responsibilities for the ACD's activities in a number of key areas, such as unit pricing, dealing, portfolio valuation and in the adherence to investment and borrowing power restrictions. Under the OEIC Regulations, OEICs are obliged to entrust their assets to the Depositary for safe keeping. This separation of the management of the fund's assets from their ownership is the most fundamental element of investor protection provided by UK authorised funds. The legal ownership of an OEIC's portfolio will be vested in the Depositary, or its nominee. Unlike an AUT, however, the beneficial interest in the portfolio will be vested in the OEIC itself and not the OEIC's shareholders.

The Depositary also has a responsibility for protecting the interests of incoming, outgoing and continuing investors. Whilst not having a direct responsibility for the ACD's activities, the Depositary must take reasonable care to ensure that the ACD is properly discharging its own responsibilities.

The Depositary must be independent of the OEIC and of the ACD. The Depositary must also be an authorised person under FSMA.

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Auditor and independent valuer

An OEIC will generally appoint independent auditors, as well as independent valuers in the event that any real property is held by the OEIC.

Other service providers

An ACD may have comprehensive operational capability to manage all aspects of its functions but quite often ACDs choose to outsource certain functions to specialist service providers, for example, shareholder administration and servicing, the registrar functions, fund accounting and valuation. It is quite common for investment management or advisory functions to be delegated, often to another group company. The Depositary may also delegate its safekeeping functions.

As a highly regulated vehicle, there are detailed regulatory requirements in COLL governing the outsourcing envisaged above. ACDs and Depositaries must also take into account provisions relating to outsourcing in the FCA's Senior Management Arrangements, Systems and Controls sourcebook (SYSC), in particular SYSC 8, and FUND 3.10R in relation to OEICs which are AIFs. Details of any proposed delegation and outsourcing arrangements, either by the ACD or the Depositary, have to be provided in the authorisation application (see further below) and the FCA will often request sight of the outsourcing contracts.

Principal documentation required

The following documentation is required by the FCA to establish an authorised OEIC:

1. an instrument of incorporation, which is similar to the trust deed for the AUT, which is the key founding document of the OEIC (similar to the memorandum and articles of association of a company) and which must comply with the content requirements set out in the OEIC Regulations;
2. a prospectus, which must comply with the content requirements set out in COLL;
3. a solicitor's certificate stating that the instrument of incorporation complies with the OEIC Regulations as to its contents;



4. material contracts between the OEIC and each of the ACD and the Depositary. Where the ACD is delegating investment management or using an investment adviser, these arrangements will also need to be documented;
5. a KIID, if the OEIC is also authorised as a UCITS scheme, or a KFD, if the OEIC is a NURS. Both of these are mandatory disclosure documents which must be given to retail clients prior to investment, subject to certain exceptions; and
6. if the OEIC is a NURS or QIS, prior disclosure to investors must also be made in accordance with Article 23 of the AIFMD, as set out in FUND 3.2.2R.

FCA application for authorisation

As mentioned above, both the ACD and the Depositary must be authorised persons under FSMA. For OEICs which are UCITS, the ACD must be appropriately authorised to act a manager of a UCITS. For OEICs which are NURS or QIS, the ACD must be appropriately authorised to act as an AIFM.

The OEIC itself must also be separately authorised by the FCA. Application for authorisation is made to the FCA by submitting an application form (Form 12), together with a fee, and drafts of the various documents listed above, including a model portfolio. The FCA may wish to review the depositary agreement and the contracts covering any significant delegations by the ACD as part of the approval process, so while these agreements do not have to be finalised prior to the application for authorisation being submitted to the FCA, they do need to be in an advanced draft state.

The amount of the application fee will depend on whether the OEIC is a UCITS, NURS or QIS and on whether it is a single company or an umbrella fund. Details of the relevant fees can be found in the FCA's Fees Manual at FEES 3, Annex 2.

The FCA has two months to consider the application for authorisation if the fund is a

UCITS and up to six months if it is a NURS or a QIS. The FCA currently aims to authorise NURS funds within two months and QIS funds within one month.

If the FCA is satisfied with the application, the FCA will issue a certificate of incorporation and the OEIC comes into existence at this point.

Consequences of authorisation

These are that:

1. an OEIC is subject to the OEIC Regulations and COLL on an ongoing basis;
2. an OEIC may be promoted and sold to the general public in the UK subject to compliance with COLL and the FCA's Conduct of Business sourcebook (COBS) (to which the ACD will usually be subject); and
3. an OEIC, like an AUT, is exempt from UK tax on its capital gains, but does pay tax on its income.

Authorised Unit Trust

An AUT is defined under s.237(1) of FSMA and is a collective investment scheme for the purposes of FSMA under which the scheme property is held in trust for the investors by the Trustee (see further below), who has legal ownership of the property. The investors have a direct beneficial economic interest in the scheme property and are the legal owners of the units.

A unit trust is constituted by a trust deed made between the Trustee and the Manager (see further below) and is governed by the terms of that trust deed, general trust law, COLL and for AUTs which are NURS and QIS, subject to FUND.

An AUT is different from an OEIC in that it does not have its own legal personality.

An AUT can be established as a single fund or it can be an umbrella unit trust with several sub-funds where the property of each sub-fund is held on a separate trust in accordance with that sub-fund's investment objectives and policies. An AUT can also be established as a feeder fund dedicated to investing in a single fund.



Please note that the only type of authorised fund that cannot be established using an AUT is a property authorised investment fund (PAIF), which must be an OEIC.

In the case of a unit trust, three parties are involved:

1. the Trustee;
2. the Manager, which operates as a distinct entity from the Trustee; and
3. the unitholders, who occupy the position of beneficiaries under the trust deed.

Manager

The Manager operates the trust scheme, such role being substantially similar to that of an ACD of an OEIC, and must be an authorised person under FSMA. For AUTs which are UCITS, the Manager must be appropriately authorised to act a manager of a UCITS. For AUTs which are NURS or QIS, the Manager must be appropriately authorised to act as an AIFM.

Trustee

The Trustee's role is substantially similar to that of the Depositary of an OEIC. As mentioned above, the Trustee is responsible for the safekeeping of the AUT assets and has a duty of oversight over the Manager. The Trustee must be an authorised person under FSMA and must be completely independent of the Manager.

Other service providers

The AUT is required to appoint an independent auditor and, if the AUT is a property fund, an independent valuer. As regards other service providers and delegation by the Manager, the information set out in 'Other Service Providers' under the OEIC section above is equally applicable.

Principal documentation required

The following documentation is required by the FCA to authorise an AUT:

1. a trust deed between the Manager and the Trustee, which must satisfy the detailed requirements of COLL;
2. a prospectus, which must comply with the detailed content requirements set out in COLL;
3. a solicitor's certificate stating that the trust deed complies with FSMA and the FCA rules on the contents of the trust deed;
4. material contracts between the AUT and each of the Manager and the Trustee. Where the Manager is delegating investment management or using an investment adviser, these arrangements will also need to be documented;
5. a KIID, if the AUT is a UCITS scheme, or a KFD, if the AUT is a NURS. Both of these are mandatory disclosure documents which must be given to retail clients prior to investment, subject to certain exceptions; and
6. if the AUT is a NURS or QIS, prior disclosure to investors must also be made in accordance with Article 23 of the AIFMD, as set out in FUND 3.2.2R.

FCA application for authorisation

As mentioned above, the Manager and the Trustee must be appropriately authorised.

The Manager and the Trustee must apply to the FCA for approval of the AUT in accordance with s.243 FSMA. Application for authorisation is made to the FCA by submitting an application form (Form 242), together with a fee, and drafts of the various documents listed above, including a model portfolio.

The amount of the application fee will depend on whether the AUT is a UCITS, NURS or QIS and on whether it is a single fund or an umbrella unit trust. Details of the relevant fees can be found in the FCA's Fees Manual at FEES 3, Annex 2.



The FCA has two months to consider the application for authorisation if the fund is a UCITS and up to six months if it is a NURS or a QIS. The FCA currently aims to authorise NURS funds within two months and QIS funds within one month.

Authorisation may be granted by the FCA if:

1. a satisfactory application has been made (in accordance with s.242 of FSMA); and
2. the scheme complies with the trust scheme rules and scheme particulars rules made under ss. 247 and 248 of FSMA (i.e. the rules in COLL); and
3. a copy of the scheme particulars and the trust deed has been sent to the FCA accompanied by a solicitor's certificate stating that the trust deed complies with regulations as to its contents under s.243(1) of FSMA.

The scheme must also meet certain other requirements which are set out in s. 243 of FSMA.

If authorisation is granted, the FCA may issue a certificate stating that the scheme complies with relevant conditions.

Consequences of authorisation

These are that:

1. an AUT scheme is subject to COLL on an ongoing basis and to sections 242 to 261 of FSMA;
2. an AUT scheme may be promoted and sold to the public in the UK subject to compliance with COLL and COBS (to which the Manager will usually be subject); and
3. AUTs are exempt from UK capital gains tax but do pay UK tax on their income.

If you require more detailed information on any of the above, please contact us at claire.cummings@cummingslaw.com.

**This document is for general guidance only. It does not constitute advice
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