

Legal 500

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United Kingdom

Alternative Investment Funds

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This country-specific Q&A provides an overview of alternative investment funds laws and regulations applicable in United Kingdom.

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United Kingdom: Alternative Investment Funds

1. What are the principal legal structures used for Alternative Investment Funds?

A UK sponsor would most typically establish a private fund overseas, using a tax neutral structure domiciled either in a low tax jurisdiction, such as the Cayman Islands (or another Caribbean jurisdiction), Jersey, Guernsey or potentially a member state of the EU, such as Luxembourg or Ireland. U.S. structures (often in Delaware) may also be utilised where the assets or the investors are located in the United States.

There are four regulatory categories of FCA authorised funds which fall within the scope of the AIFMD; the non-UCITS retail scheme (NURS), the qualified investor scheme (QIS), Long-Term Asset Fund (LTAF) and the Long-Term Investment Fund (LTIF). A NURS, QIS or LTAF may be formed as an investment company with variable capital (ICVC) (which is also referred to as an open-ended investment company (OEIC)), authorised unit trust (AUT), authorised unit trust (AUT) or authorised contractual scheme (ACS), formed as either a limited partnership scheme a contractual scheme. The legal form of an LTIF is not prescribed in the LTIF Regulation.

However, these FCA authorised funds tend to be utilised by managers only for UK investors and where there is a specific tax benefit in doing so. All of them tend not to be familiar to non-UK investors and, as such, cannot generally be widely used for asset raising outside of the UK. In addition, all of these vehicles are subject to prescriptive rules on their investment and borrowing powers and the NURS, in particular, is generally not viewed as an appropriate vehicle in which to raise capital for alternative investment strategies.

Unauthorised AIFs – i.e. UK AIF vehicles that are not themselves authorised by the FCA but which have an FCA authorised AIFM – are also possible. These include an English limited partnership structured either as a traditional limited partnership or as private fund limited partnership ("PFLP") (which is a voluntary election available to English limited partnerships which qualify as collective investment schemes) and are generally used in private equity structures. The PFLP structure (which has been available since 2017 and is now the default option for new structures) addresses some of the disadvantages of the traditional English limited partnership structure (including, for example, by removing the requirement for

limited partners to make and hold a capital contribution to the partnership).

The legal form of the fund will be driven by investors' regulatory, tax and reporting requirements as well as the strategy of the Fund. Non-U.S. investors and U.S. tax-exempt investors will generally prefer a corporate structure or a partnership structure which has elected to be treated as a corporation for US tax purposes which provides an opaque entry point, which manages the US tax exposure on the investments and reduces the investor's filing requirements. U.S. taxpayers generally prefer a U.S. partnership which provides tax transparency. For sponsors intending to market the strategy on a global basis, a master-feeder structure, which provides for multiple entry points and pooling of assets can be used.

2. Does a structure provide limited liability to the investors? If so, how is this achieved?

In the case of funds structured as limited partnerships, provided that limited partners do not involve themselves in the management and operations of the partnership (other than as might be permitted by applicable safe harbours or "white lists"), an investor's liability will be limited to the amount of capital contributed by them as a limited partner.

In the case of funds structured as corporates, investors will typically hold shares in the fund and, as such, by operation of law, their liability will be limited to the amount paid up or agreed to be paid up on their shares.

Beyond the operation of law, fund managers and investors typically negotiate and agree to limits on investor liability through contractual terms in the constitutional documents of the fund or side letters. For example, an investor's liability under indemnity provisions might be limited to an amount not exceeding that investor's capital commitment to the fund.

3. Is there a market preference and/or most preferred structure? Does it depend on asset class or investment strategy?

For UK managers raising capital on a global basis, generally a master-feeder structure is preferred to

provide maximum flexibility. The master-feeder structure is often complimented by one or more parallel funds to meet specific legal, tax or regulatory requirements of certain types of investors (e.g. U.S. ERISA investors). The vast majority of hedge funds continue to be established either in the Cayman Islands or the State of Delaware and private equity funds in these two jurisdictions plus Luxembourg, Jersey and Guernsey. Typically, other jurisdictions are selected to enable marketing, accommodate investor preferences or facilitate bespoke tax structuring for a specific asset class or strategy.

4. Does the regulatory regime distinguish between open-ended and closed-ended Alternative Investment Funds (or otherwise differentiate between different types of funds or strategies (e.g. private equity vs. hedge)) and, if so, how?

A UK NURS, LTAF or a QIS can only be established as an open-ended fund. The LTIF, on the other hand, is a closed-ended AIF.

For non-UK AIFs, the UK NPPR operates in the same way for open- and closed-ended funds.

5. Are there any limits on the manager's ability to restrict redemptions? What factors determine the degree of liquidity that a manager offers investors of an Alternative Investment Fund?

Generally, the AIFM of a NURS must undertake redemptions on any dealing day on request. Certain categories of NURS can limit redemptions to once every six months.

The authorised fund manager of a QIS or a NURS may impose restrictions on redemptions or temporarily suspend dealings in a QIS or a NURS, with the agreement of the depositary. For a QIS, the terms of such restriction or suspension must be specified in the prospectus. And any suspension may only be applied where the authorised fund manager has determined that there is sufficient reason, taking into account the interests of all unitholders. For a NURS, the suspension must be due to exceptional circumstances and be in the interests of all unitholders. Additional suspension rules apply to NURS that are property investment funds or money market funds. Any suspension must be immediately notified to the FCA.

The AIFM is subject to terms the FCA's handbook of rules

and guidance as they apply to the AIFM's liquidity management in respect of both UK and non-UK AIFs. In particular:

- the AIFM must ensure that the investment strategy, liquidity profile and redemption policy of each AIF it manages are consistent;
- the AIFM must, for each AIF it manages that is not an unleveraged closed-ended AIF:

(a) employ an appropriate liquidity management system; and

(b) regularly conduct stress tests, under normal and exceptional liquidity conditions, which enable it to assess the liquidity risk of the AIF and monitor that risk.

In the case of LTIFs, the ability to offer redemption rights is very limited and the parameters are set out in the UK LTIF Regulation. With respect to LTAFs, again, they may offer limited or restricted redemption rights, and the scope of that ability is set out in chapter 15 of COLL of the UK FCA Handbook of Rules and Guidance (FCA Handbook), together with certain provisions of the FUND, COBS and SYSC modules of the FCA Handbook.

6. What are potential tools that a manager may use to manage illiquidity risks regarding the portfolio of its Alternative Investment Fund?

Subject to the rules and offering documents of the AIF and the applicable legal and regulatory regime:

- Setting redemption notice periods;
- Setting the frequency of dealing days;
- Imposing fund-level gates and/or investor-level gates (however, only very limited gating would be permitted for certain NURS and for QIS);
- Creating side pockets/ liquidating classes (not applicable for a QIS or a NURS);
- Applying hard or soft lock-ups (not applicable for a QIS or a NURS);
- (As a last resort) imposing a suspension.

7. Are there any restrictions on transfers of investors' interests?

Generally, the shares or units in a NURS formed as an OEIC or AUT are freely transferrable, although the AIFM would typically have a right to refuse the transfer if it would cause legal, regulatory, pecuniary or fiscal disadvantages or otherwise be unlawful. The AIFM would need to restrict transfers for a NURS that is an ACS or for a QIS or LTAF, to the categories of investor that are

permitted to invest in it under the UK Financial Services and Markets Act 2000 (as amended) ("FSMA") and/or the FCA rules.

LTIFs are designed to be eligible for retail investors and as such, transferability is less restrictive than in the case of NURS formed as ACS, LTAFs or QIS'. The QIS and the LTAF are restricted to certain qualified investors (as specified in COLL) and thus, transferability of QIS and LTAF units is limited to investors who satisfy the applicable status.

For an unauthorised English limited partnership, the transfer restrictions will be determined by its partnership agreement. However, sponsors should also have regard to the wider regulatory framework when considering permitted transfers in the context of closed ended funds, in particular the US "publicly traded partnership" rules.

For a non-UK AIF with an FCA authorised AIFM, the FCA does not have direct oversight and the AIF would be subject to its rules and offering document as well as applicable law and regulation in its home jurisdiction.

8. Are there any other limitations on a manager's ability to manage its funds (e.g., diversification requirements)?

A QIS is subject to a general risk spreading obligation. Subject to its fund rules, a QIS may invest in specified investments, real property, precious metals and / or certain listed commodity contracts. A QIS is subject to rules on the taking of collateral in respect of stock lending and derivative transactions. The borrowing of a QIS cannot exceed 100% of the net value of the scheme property. There are restrictions on the ability of a QIS to invest in other funds.

NURS are subject to substantive restrictions on their investment and borrowing powers, similar to a UCITS, although a NURS is not restricted to borrowing on a temporary basis. Subject to limited exceptions, the assets of a NURS may only be invested in transferable securities, money market instruments, units in CIS, derivatives, deposits, property (immovables) and gold (up to 10% of the value of the scheme property). The NURS is subject to strict limits on the concentration of assets and counterparty exposure.

The LTIF and the LTAF are also subject to general risk and portfolio diversification rules as well as eligible asset rules, as more specifically set out in the LTIF Regulation and COLL, respectively.

For an English private equity fund established as a traditional limited partnership or a PFLP which is not authorised by the FCA, the fund's investment and borrowing powers will be determined by its partnership agreement.

For a non-UK AIF with an FCA authorised AIFM, the FCA does not have direct oversight and the AIF would be subject to its rules and offering documents as well as applicable law and regulation in its jurisdiction.

9. What is the local tax treatment of (a) resident, (b) non-resident, (c) pension fund and (d) sovereign wealth fund investors (or any other common investor type) in Alternative Investment Funds? Does the tax status or preference of investors or the tax treatment of the target investments primarily dictate the structure of the Alternative Investment Fund?

A UK resident and domiciled taxpayer will typically seek to invest in a hedge fund via a corporate vehicle. Generally, each class of a corporate hedge fund will be classified as an "offshore fund" for the purposes of the UK offshore fund legislation. As such, UK taxpayers will generally be taxed upon any distributions received from the fund and any gain realised on a redemption of their shares, save that there are limited circumstances in which a UK corporate shareholder may pay tax on their unrealised gains in the fund (where, broadly, the fund's investments are more than 60% in interest bearing assets) and "close companies" (which are narrowly held) will be treated differently.

If the class in which an individual UK investor holds shares does not have UK "reporting fund" status, the UK investor will pay tax at UK income tax rates on any realised gain (resulting in tax at up to 45% rather than the 24% generally attributable to capital gains for top rate taxpayers)

If the class in which an individual UK investor holds shares has UK reporting fund status, the UK investor will pay tax at UK income tax rates each year on their share of the accrued income in respect of that class (whether or not it is distributed to them) but will receive capital gains treatment on any realised gain. Reporting fund status may also be important to certain classes of investor which are taxable on income but exempt from tax on gains (for example, certain authorised UK funds).

Non-UK resident investors and non-UK sovereign wealth funds are typically not subject to UK tax in respect of

interests in offshore funds.

As referred to in Question 1, the structure of an AIF for a private equity or other alternatives strategy will be driven by the tax status of the investors, the nature of its investments and where the AIF will invest. The starting point will generally be to try to achieve tax neutrality such that there will be no tax at the level of the fund by using a tax transparent vehicle such as a limited partnership and UK investors would be taxed on any distributions received from the Fund.

The tax treatment of target investments may influence the structure of the AIF. In particular, if withholding tax will be due in respect of the target investments (for example in the case of debt funds), consideration should be given to a fund jurisdiction and vehicle which may enable treaty relief to be claimed (for example, Ireland or Luxembourg may be preferred to the Cayman Islands and other offshore jurisdictions). Alternatively, consideration may be given to establishing intermediate holding companies to mitigate withholding tax. While such vehicles are subject to increasing substance requirements and scrutiny, they remain relatively common and the UK has recently introduced its own tax advantaged intermediate asset holding vehicle regime, the Qualifying Asset Holding Company regime, for this purpose. Sponsors may also make use of corporate "blocker" vehicles to protect non-US investors from US tax filing obligations. Please refer to Question 1 above for further information.

10. What rights do investors typically have and what restrictions are investors typically subject to with respect to the management or operations of the Alternative Investment Fund?

Typically, the AIF would be established as a passive investment vehicle, with investors having no rights as to management or operations.

Generally, UK investors in a unitised hedge fund would receive voting shares, giving them limited rights on changes made to the articles. Investors would also be given the opportunity to vote on a proposed variation in their class (fundamental) rights.

Generally, investors in an English private equity fund established as a traditional limited partnership or as a PFLP which is not authorised and regulated by the FCA would receive non/limited-voting interests. However strategic investors may receive a seat on the LPAC, which would provide them with a vote or consultation right on certain matters. For funds structured as a PFLP, the

regulations contain a so-called "white list" of activities which may be accorded to limited partners but which do not cause them to lose their limited liability status on the basis of them taking part in the management or operations of the partnership.

11. Where customization of Alternative Investment Funds is required by investors, what types of legal structures are most commonly used?

In recent years, the range of customized investment solutions has become very comprehensive, with the following types most commonly used:

- Investment management agreement overlays to an investor's bank or custody account;
- Use of special purpose vehicles such as companies and trusts with investment management agreement overlays;
- Funds-of-one;
- Club funds;
- Separate Managed Account platforms utilisation umbrella fund structures; and
- Hybrid entities combining features of a private equity or hedge fund with features of a joint venture company.

English Limited Partnerships are very easy to customise as they are not subject to any prescriptive rules relating to the contents of the governing documents. The governing documents of English limited partnerships are commonly highly negotiated to fit the bespoke needs of a particular strategy and investor base.

12. Are managers or advisers to Alternative Investment Funds required to be licensed, authorised or regulated by a regulatory body?

A UK undertaking which provides risk management and/or portfolio management services to an AIF and is appointed by the governing body of the AIF as that AIF's designated AIFM must be authorised by the FCA to conduct the regulated activity of managing an AIF.

13. Are Alternative Investment Funds themselves required to be licensed, authorised or regulated by a regulatory body?

The QIS, NURS, LTIF and LTAF are authorised by the FCA.

A private equity fund can be established as a traditional

English limited partnership or a PFLP which is not authorised by the FCA.

Non-UK AIFs managed or sponsored by UK managers are not subject to the direct oversight of the FCA (although these vehicles may be indirectly subject to UK regulation via the manager under the terms of the AIFMD and its implementing legislation).

14. Does the Alternative Investment Fund require a manager or advisor to be domiciled in the same jurisdiction as the Alternative Investment Fund itself?

FCA authorisation is required to serve as AIFM to an FCA authorised UK AIF – i.e. a NURS, QIS, LTAF or LTIF.

AIFMs established in a third country (i.e. any country other than the UK or Gibraltar) may market in the UK AIFs they manage (including non-FCA authorised UK AIFs) subject to compliance with the UK implementation of AIFMD Article 42.

FCA authorised UK AIFMs may serve as the AIFM of a third country AIF, subject to compliance with AIFMD Article 36 (if the AIF is marketed in the UK) or Article 34 (if the AIF is not marketed in the UK).

It is common for AIFMs to delegate investment management to a professional fund manager, and it is usual to see delegation to either an FCA-regulated investment management firm or an investment manager domiciled outside of the UK.

15. Are there local residence or other local qualification or substance requirements for the Alternative Investment Fund and/or the manager and/or the advisor to the fund?

Substance requirements should be considered in the jurisdiction(s) in which the fund vehicle and any subsidiary asset holding vehicles are established.

16. What service providers are required by applicable law and regulation?

This will depend upon the legal form selected for the fund.

An open-ended investment company (OEIC), authorised unit trust (AUT) or authorised contractual scheme (ACS) must appoint an authorised fund manager and

depository/custodian domiciled in England and authorised by the FCA.

An OEIC's authorised fund manager is called an authorised corporate director and is typically the OEIC's sole director.

An AUT's authorised fund manager is called a manager and its depository is called a trustee.

There are no local service provider requirements for an English private equity fund established as a traditional limited partnership or a PFLP which is not authorised and regulated by the FCA.

A non-UK AIF managed by a UK manager must appoint a single AIFM or, if it is a self-managed corporate fund, designate its governing body as its AIFM.

A non-UK AIF with a UK AIFM which is registered for marketing in the UK under AIFMD Article 36 must appoint a depository to perform a limited oversight role.

The AIF's annual report must be audited.

17. Are local resident directors / trustees required?

Please refer to Question 15 in relation to FCA authorised funds.

In respect of non-UK funds, central management and control should be discharged outside of the UK for tax reasons. Accordingly, the number and role of any UK directors should be limited.

18. What rules apply to foreign managers or advisers wishing to manage, advise, or otherwise operate funds domiciled in your jurisdiction?

The activities of managing an AIF, managing investments, advising on investments and establishing, operating or winding-up a collective investment scheme are all regulated by the FCA when undertaken in the UK.

An undertaking which is providing these services in the UK must either (1) be regulated by the FCA or (2) comply with a relevant exemption – e.g. for providing non-discretionary investment advice to a UK recipient, the exemption for overseas persons (which, amongst other things, requires the adviser not to provide the advice from a permanent place of business available to it in the UK).

Conducting a business in the UK can also result in the

establishment of a branch which will create filing obligations with Companies House and may impact on the UK tax position of the undertaking.

19. What are the common enforcement risks that managers face with respect to the management of their Alternative Investment Funds?

Key areas of risk include:

- breaches of reporting or notification obligations applicable to the AIFM or the AIF
- misrepresentations in investor disclosures
- breaches of marketing rules
- failure to ensure accurate valuations
- failure to manage conflicts of interests properly
- failure to conduct proper client due diligence and anti-money laundering checks
- liquidity failures.

20. What is the typical level of management fee paid? Does it vary by asset type?

Management fees charged by UK managers typically range 1.25 – 2%. For venture capital funds, it is not uncommon to see management fees of 2.5%.

21. Is a performance fee or carried interest typical? If so, does it commonly include a "high water mark", "hurdle", "water-fall", "preferred return" or other condition? If so, please explain.

Performance fees are a standard feature of absolute return funds and would typically include a "high water mark" (being the higher of an investor's (x) initial subscription amount and (y) the highest value of such subscription amount as at the most recent date on which a performance fee was charged). The "high water mark" is designed to ensure an investor is not charged performance fees on its investment in the fund until any losses incurred are recovered.

Hurdles are often included in equities strategies. The hurdle is added to the "high water mark" (e.g. no performance fee is charge unless the "high water mark" plus the hurdle is exceeded). The hurdle is typically an absolute number (e.g. 3% – 5%).

Long-only funds may incorporate an out-performance fee, which works in the same way as a typical performance fee save that it is calculated on performance in excess of a benchmark (which may result in fees being

payable even if the fund has lost value).

Private equity and private real assets funds typically only feature an IRR hurdle but not a high water mark. In the UK, the European style "whole of fund" waterfall is the most common structure used to determine the carried interest payable to a manager.

22. Are fee discounts / fee rebates or other economic benefits for initial investors typical in raising assets for new fund launches?

Yes. Typically for hedge strategies, founder shares would be offered for a limited period of time (e.g. 12 months) and/or until a certain capacity has been reached (e.g. \$100million). For private equity and private equity-style strategies, "early bird" management fee discounts/rebates are offered to investors who commit as at the first closing of the fund.

23. Are management fee "break-points" offered based on investment size?

For hedge funds, UK managers often offer a lower fee paying class in return for a higher initial investment, albeit the discount is typically focused on the management fee rather than the performance fee.

In the case of private equity funds, there tends to be one stated management fee rate, but that can be reduced through a discount or fee rebate based on investment size either through a side letter agreement or the volume discount thresholds may be set out in the partnership agreement.

24. Are first loss programs used as a source of capital (i.e., a managed account into which the manager contributes approximately 10-20% of the account balance and the remainder is furnished by the investor)?

When capital raising is particularly challenging, some UK managers turn to first-loss capital providers as a way of boosting assets under management (which can help in marketing the strategy to prospective investors). That said, such first-loss programs are still relatively rarely used by UK managers.

25. What are the typical terms of a seeding / acceleration program?

Seeding/acceleration deals can vary widely, from seed investors who seek preferential investment terms, to seed investors who also seek control over the constitution of the fund and its offering terms together with a share of future revenues and/or an equity stake in the investment management business. In return for such terms, the fund manager should secure committed seed/acceleration capital which will remain in the fund for an extended period allowing the manager time to build its track record and attract new capital.

Preferential investment terms would include lower fees, increased transparency, capacity rights, a 'most-favoured-nations' right (namely a right to receive investment terms at least as good as other investors), certain approval rights and controls (including in respect of the investment policy being pursued and the activities of the UK manager) and redemption rights.

26. What industry trends have recently developed regarding management fees and incentive/performance fees or carried interest? In particular, are there industry norms between primary funds and secondary funds?

Management fees and performance fees charged by UK managers came under significant pressure in the aftermath of the 2008 financial crisis. There is less pressure on management fees and performance fees since 2018 for those managers who can demonstrate a strong track record.

In recent years, the industry has looked at alternative fee structures designed to reward 'alpha' rather than 'beta' returns. This is sought to be achieved by incorporating a benchmark return into the performance fee structure. However, these structures did not become widespread, primarily due to a difficulty in selecting an appropriate benchmark against which to measure performance given the absolute return and uncorrelated nature of most alternative fund strategies. Some managers have included clawbacks against performance fees and/or longer performance periods but again this has not become widespread. Management fees for secondary funds usually range between 0.5 – 1.25%, with carried interest ranging between 12.5 – 15%, subject to a typical hurdle of 8% and extending to a "super carry" rate of 25%, subject to both an IRR and MOIC hurdle.

27. What restrictions are there on marketing Alternative Investment Funds?

AIFMs wishing to market AIFs in the UK will be required to

comply with AIFMD (as implemented in the UK). An AIFM established in a third country – i.e. any country other than the UK or Gibraltar – may access the UK market by registering the AIF for marketing under the UK's national private placement regime (NPPR) implementing AIFMD Article 42, which is a relatively simple and quick process.

The promotion of an investment product or service in the UK by a person that is not authorised by the FCA is governed by Section 21 of the FSMA which provides that an unauthorised person must not, in the course of business, communicate an invitation or inducement to engage in investment activity unless either (i) the content of the communication has been approved by an authorised person or (ii) the communication is covered by an exemption (the "section 21 prohibition").

Financial promotions to various categories of person by unauthorised firms are excluded from the section 21 prohibition under the UK Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 ("FPO"), including financial promotions to investment professionals and certain high net worth businesses. The FPO also exempts promotions of PE-style funds that invest predominantly in unlisted securities which are made to "certified high net worth investors".

An FCA authorised firm promoting an investment product or service must comply with the rules set out in Chapter 4 of the Conduct of Business Sourcebook which forms part of the FCA Handbook ("COBS"), including certain high level contents requirements.

An FCA authorised firm is prohibited from promoting an unauthorised CIS unless the promotion falls within one of the exclusions contained in the UK Financial Services & Markets Act 2000 (Promotion of Collective Investment Schemes) (Exemptions) Order 2001 (the "PCIS Order") is subject to additional promotion rules which apply specifically to the promotion of unregulated collective investment schemes. These exclusions broadly follow exclusions created by the FPO. The PCIS Order includes an exemption for promotions to overseas recipients. In addition, Section 4.12B of COBS extends these exclusions by allowing an FCA authorised firm to promote an unauthorised CIS to additional categories of recipients, including persons who are members of a similar scheme and to clients of the firm for whom the unauthorised CIS is "suitable".

An FCA authorised firm may promote a QIS to a person falling within one or more of the exempt categories in COBS 4.12B and a LTAF to one or more of the exempt categories in COBS 4.12A.

Separate rules apply to AIFs which publish a prospectus under the Prospectus Regulation as implemented in the UK, however, this is outside of the scope of this chapter.

28. Is the concept of "pre-marketing" (or equivalent) recognised in your jurisdiction? If so, how has it been defined (by law and/or practice)?

In general, the FCA guidance takes a reasonably narrow view of "marketing", meaning that a wide range of "pre-marketing" activity is permissible without triggering the need for a marketing notification / registration pursuant to AIFMD. Communications relating to a draft offering document would not fall within the meaning of an 'offer' or 'placement' for the purposes of AIFMD, as the AIFM cannot apply for permission to market the AIF at this point. For example, a promotional presentation or a pathfinder version of the private placement memorandum would not constitute an offer or placement, provided such documents cannot be used by a potential investor to make an investment in the AIF. However, a unit or share of the AIF should not be made available for purchase as part of the capital raising of the AIF on the basis of draft documentation in order to circumvent the marketing restriction.

29. Can Alternative Investment Funds be marketed to retail investors?

Yes, in principle an AIF may be marketed to retail investors provided certain requirements are followed. The AIFM (full scope) would need to obtain FCA approval and prepare a Key Information Document to be provided to retail investors prior to their investment. It would also be necessary to comply with the UK's financial promotion regime. There are very few exemptions available for promotion to retail investors.

30. Does your jurisdiction have a particular form of Alternative Investment Fund be that can be marketed to retail investors (e.g. a Long-Term Investment Fund or Non-UCITS Retail Scheme)?

Yes, the UK has the Non-UCITS Retail Scheme (NURS) as well as the Long-Term Investment Fund (LTIF, based very closely on the European Long-Term Investment Fund) which can be marketed to retail investors. The UK Long-Term Asset Fund (LTAF) can be marketed only to "qualified investors" which in practice means semi-retail investors through to professional investors.

31. What are the minimum investor qualification requirements for an Alternative Investment Fund? Does this vary by asset class (e.g. hedge vs. private equity)?

Please refer to Question 27 above.

32. Are there additional restrictions on marketing to government entities or similar investors (e.g. sovereign wealth funds) or pension funds or insurance company investors?

No.

33. Are there any restrictions on the use of intermediaries to assist in the fundraising process?

The AIFMD marketing restrictions apply to marketing by the AIFM and marketing "at the initiative of, or on behalf of" the AIFM, including intermediaries. Where a UK intermediary has been appointed by the AIFM, any marketing of the AIF by the intermediary "at the initiative of, or on behalf of" the AIFM would require an AIFMD marketing passport / notification to the FCA (and the AIFM would be accountable for the activities of the intermediary).

Please refer to Question 27 above in relation to the communication of financial promotions by an intermediary.

34. Is the use of "side letters" restricted?

No. However, side letter terms are not permitted where they would result in an overall material disadvantage to other investors. This has broadly been interpreted as restricting a manager's ability to offer preferential liquidity terms (albeit it may also extend to preferential transparency where such transparency may be important in influencing an investor's decision to remain invested in the fund).

35. Are there any disclosure requirements with respect to side letters?

UK managers of alternative investment funds are required to "make available" details of any preferential treatment granted to investors together with details of the type of investor who obtain such preferential treatment and, where relevant, the investor's legal or economic links to

the UK manager or the fund. Whilst the requirement is to "make available" such details rather than disclose per se, disclosure is commonly made. Typically, UK hedge fund managers would make such disclosure in their standard due diligence questionnaire to avoid needing to update the fund's offering documentation each time a side letter is entered into. Private equity and other alternative asset class funds will generally carry out a "most favoured nation" process disclosing side letter terms agreed with investors following the final closing of the fund.

**36. What are the most common side letter terms?
What industry trends have recently developed
regarding side letter terms?**

Common side letter terms include lower fees, a 'most-favoured-nations' right (namely a right to receive investment terms at least as good as other investors) and transparency rights.

Due to the regulatory requirements detailed above, UK managers have increasingly sought to restrict the number of side letters entered into in favour of offering negotiated terms to all investors. This is particularly the case with regard to transparency and rights requested in respect of redemption terms. Accordingly, side letter terms increasingly tend to cover bespoke tax and regulatory representations, additional information or reporting rights required by investors with specific tax and regulatory requirements.

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