Hogan Lovells

Regulatory, Compliance & Investigation Solutions

For private equity, debt funds and other asset managers

2019

Introduction

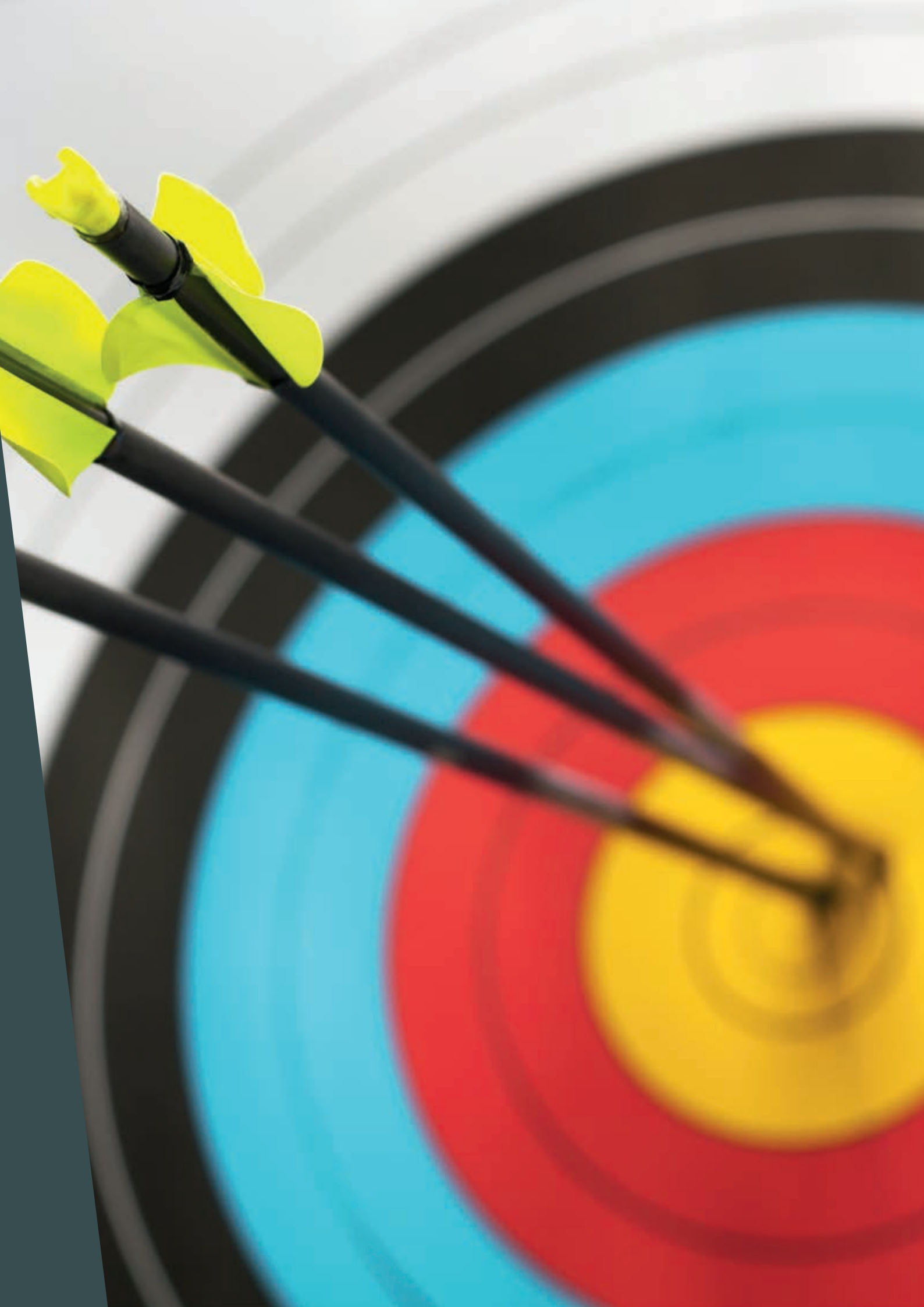
What is "RC&I Solutions"?

Private equity, debt funds and other asset managers face an ever increasing set of challenges from regulations and associated compliance risks. Failing to comply can lead to considerable reputational damage, financial penalties and in some cases, criminal action.

RC&I Solutions provides private equity, debt funds and other asset managers with a complete solution spanning sanctions and trade compliance, anti-bribery and corruption, anti-money laundering, cartels, environmental and health and safety, regulated activities, human rights, and data privacy and cybersecurity, delivered by our market-leading, multi-disciplinary team of lawyers.

Our team works with asset managers to understand their risk profile and business objectives, including those of their portfolio investments, to identify and deal with these risks, review or design compliance programmes and provide support if things go wrong.

For more information on how our team can help you with your compliance and Environmental, Social and Governance programmes, please get in touch with any of the contacts listed at the end of this brochure, or your usual Hogan Lovells contact.




Regulated
activities

AIFMD

Asset managers must be authorised when undertaking the regulated activity of 'managing an alternative investment fund' (AIF) in the EU under the provisions of the Alternative Investment Fund Managers Directive (AIFMD) as transposed into UK law by the Alternative Investment Fund Managers Regulations. We advise on the full range of issues arising under AIFMD including authorisation of fund managers and the marketing in the EU of funds by EU and non-EU fund managers under AIFMD and national private placement regimes.

General financial regulation

In addition to the authorised activity of managing an AIF, asset managers will typically also be authorised to undertake other regulated activities such as advising on and arranging investments. They will also be subject to other aspects of financial regulation.

Regulated activities of portfolio companies

Private equity fund managers will also need to ensure compliance by portfolio companies which themselves are authorised financial institutions with the applicable regulatory regime and understand the implications for the fund manager of holding those companies.

> "Hogan Lovells provides a 'top-notch' service to large global financial services entities on purely domestic, as well as multi-jurisdictional regulatory investigations and follow-on private litigation."
>
> *Legal 500 UK, 2019: Financial Services*

How we can help you

- We advise on the full range of issues arising under AIFMD.
- We advise on all aspects of general financial regulation applicable to private equity and other asset managers.
- We can provide advice on all regulatory aspects of the acquisition of companies operating in the regulated financial sector.

Anti-bribery and corruption

The UK Bribery Act along with other international bribery legislations such as the U.S. Foreign Corrupt Practices Act ("FPCA") has wide-ranging jurisdictional effect.

Companies who do business in the UK may be exposed to liability in relation to acts of bribery committed anywhere in the world including by their employees, agents, subsidiaries, portfolio companies and other third parties who perform a service for them.

Section 7 of the UK Bribery Act provides that a company carrying on a business in the UK will be liable if it fails to prevent bribery committed by "associated persons". Although the definition of "associated persons" is limited to entities "performing a service" to the UK company it is likely that the UK Courts will interpret the phrase widely to encompass wholly owned and/or controlled portfolio companies (no matter in which jurisdiction the portfolio companies are operating in). It is a defence under UK law to show that you had in place "adequate procedures" to prevent bribery and/or did not turn a blind eye to bribery at portfolio company level.

"Adequate procedures" includes having policies and procedures designed to ensure that proper diligence is done on third parties that are performing services for the portfolio companies as well as procedures to monitor ethical compliance by those companies. In the case of investment fund managers this will include clear procedures on ABC due diligence on target assets so as to minimise future exposure to risk. Court decisions and the actions of regulators have put the spotlight on fund managers and how they operate in more risky geographies and sectors.

Policies and procedures are one part of having in place "adequate procedures". However, another essential plank is conducting a documented ABC risk assessment and updating it regularly. A formal risk assessment is crucial to ensure that policies and procedures are in fact in place and that they properly reflect the risks associated with the relevant business.

For private equity fund managers and other investment holders there may not always be liability for the acts of portfolio companies but it is nevertheless important to ensure ethical compliance in order to maintain value and to minimise reputational damage.

Our award-winning team handles all issues relating to bribery and corruption, and we can work with you to limit the impact they have on your businesses. We pursue and defend claims against executive boards, and we craft internal programmes and policies that comply with global legislation, such as the Foreign Corrupt Practices Act and the UK Bribery Act.

> "Few firms can rival Hogan Lovells' size, reputation and experience in the investigations space.
>
> *Global Investigations Review, 2018*
> *Ranked second globally*
> *Most important case of the year*
>
> "

How we can help you

- We carry out stress-tests, design and implement anti-corruption policies and procedures, risk management strategies, training programmes and due diligence methodologies.
- We advise on complying with the UK Bribery Act, U.S. Foreign Corrupt Practices Act (FCPA) and local laws, including rules on police and investigatory agency powers, privacy, data protection, employee rights and privilege.
- We advise on self-reporting.
- We co-ordinate and manage other professionals involved in internal and official investigations, including forensic accountants, public relations advisers and enquiry agents.

Sanctions and trade compliance

Financial sanctions compliance

Financial sanctions are restrictions put in place by the UN, U.S., EU and UK to achieve a specific foreign policy or national security objective. They can limit the provision of certain financial services to specific designated entities, or persons, and restrict access to financial markets, funds and economic resources to these persons. U.S., EU and UK persons have an obligation to comply with financial sanctions.

The scope of application of U.S., EU and UK sanctions laws are wide, and breaches of financial sanctions are considered to be a serious criminal offence, and can lead to significant reputational damage. Portfolio companies are expected by their relevant sanctions regulators to have considered the likely exposure of their businesses to sanctions laws, and have in place appropriate and tailored specific procedures, processes and systems to mitigate any sanctions risks.

Trade compliance: Export controls and sanctions

Our full Trade Compliance package provides a solution that is tailored to a fund manager's risk profile and objectives that takes a holistic view of its business, including its portfolios of assets and acquisitions taking into consideration any sanctions, but also export controls or other applicable trade compliance issues.

Our International Trade and Investment group, rated as a leading international trade practice by Chambers and Legal 500, offers effective, informed advice on trade policy, legislation, compliance and enforcement, litigation, and administrative proceedings. We handle issues such as sanctions compliance, export and import controls, WTO law advice, anti-bribery rules, foreign direct investment, trade agreement negotiations, and anti-dumping and subsidy cases.

The geographic spread of our experience, combined with our substantive trade law expertise, is the feature that distinguishes Hogan Lovells from the other law firms in the market.

Many of our international trade lawyers previously occupied leadership positions within the relevant government agencies and we maintain regular contact with all the relevant U.S., EU, and other agencies.

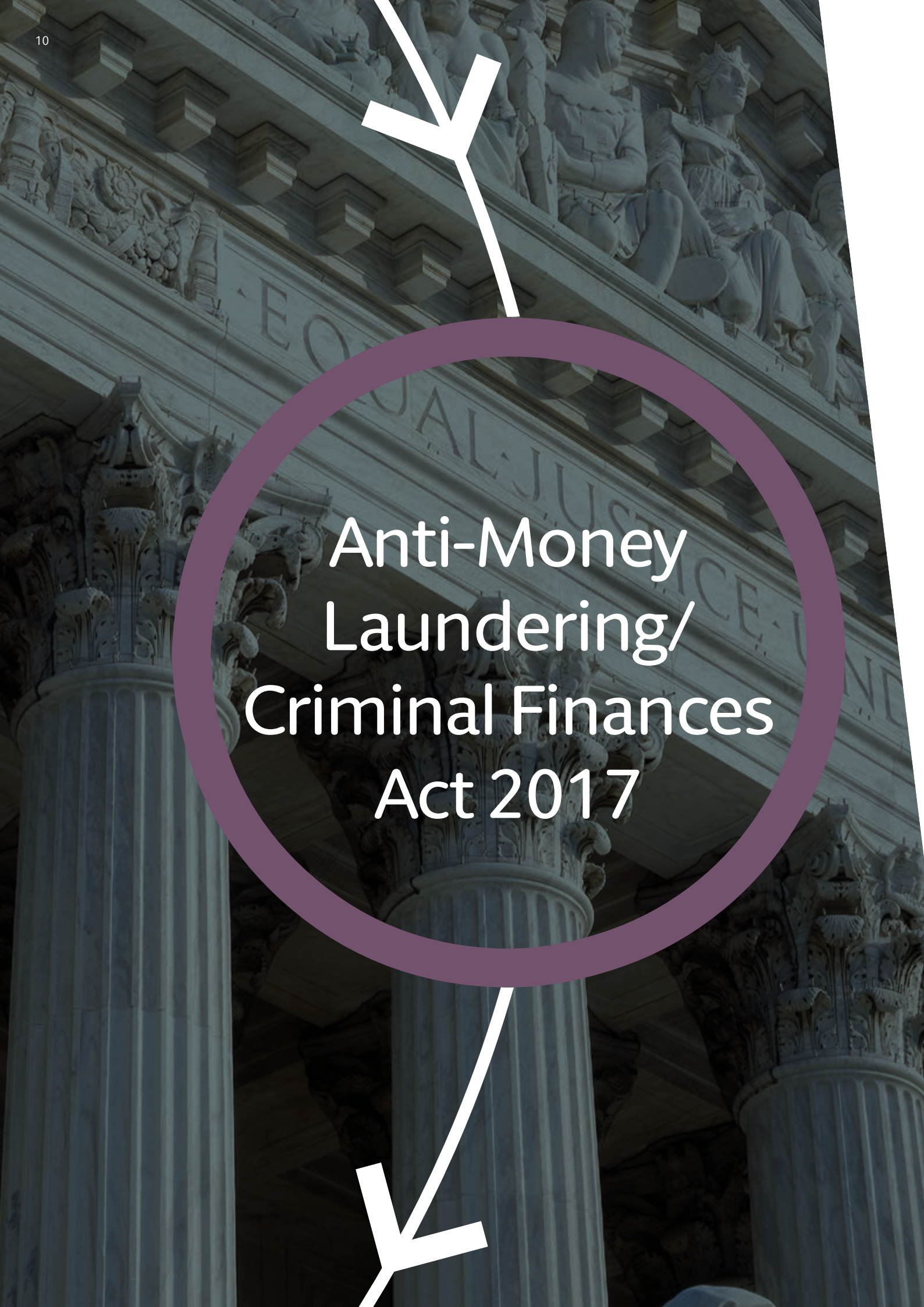
Our team can offer a tailored solution for financial sanctions compliance aimed specifically at private equity funds, debt funds and other asset manager clients.

> "Sources say that "the firm completely understands the minutiae of trade law. We enjoy working with them."
>
> *Chambers Global, 2018*

> "Named 'International Trade Law Firm of the Year – 2019'.
>
> *Chambers USA, 2019: Washington, D.C.*

How we can help you

- We carry out risk assessments and gap analysis reports on the compliance by fund managers and their portfolio companies with sanctions put in place by the UN, EU, U.S. and UK as well as export controls and customs duties where this is relevant.
- We design global sanctions compliance programmes and associated policies, and draft and deliver training on sanctions compliance.
- We undertake internal investigations and represent clients in external investigations conducted by U.S., EU and other agencies.
- We can call on advice from former UK regulators and prosecutors.
- We perform sanctions due diligence reviews in an M&A context, and implement sanctions uplift compliance programme post-closing.
- We work with compliance consultants.



Anti-Money Laundering/ Criminal Finances Act 2017

Anti-Money Laundering

Organisations which are authorised by the FCA are subject to the Money Laundering Regulations 2017 which contain obligations including: a requirement to conduct a risk assessment, establish and maintain policies, controls and procedures to mitigate identified risks, appoint a money laundering officer, report suspicions of money laundering, and provide anti-money laundering training.

UK agencies, including the FCA, are increasingly focused on investigating money laundering cases and breaches of the Regulations.

Tax evasion facilitation

Two new tax-related criminal offences were introduced by the Criminal Finances Act 2017.

It's no longer enough to get your own tax right. If your employees, agents or service providers facilitate tax evasion by someone else, that can create criminal liability for your company or fund. It's no defence to say you didn't know about it: the offences are strict liability.

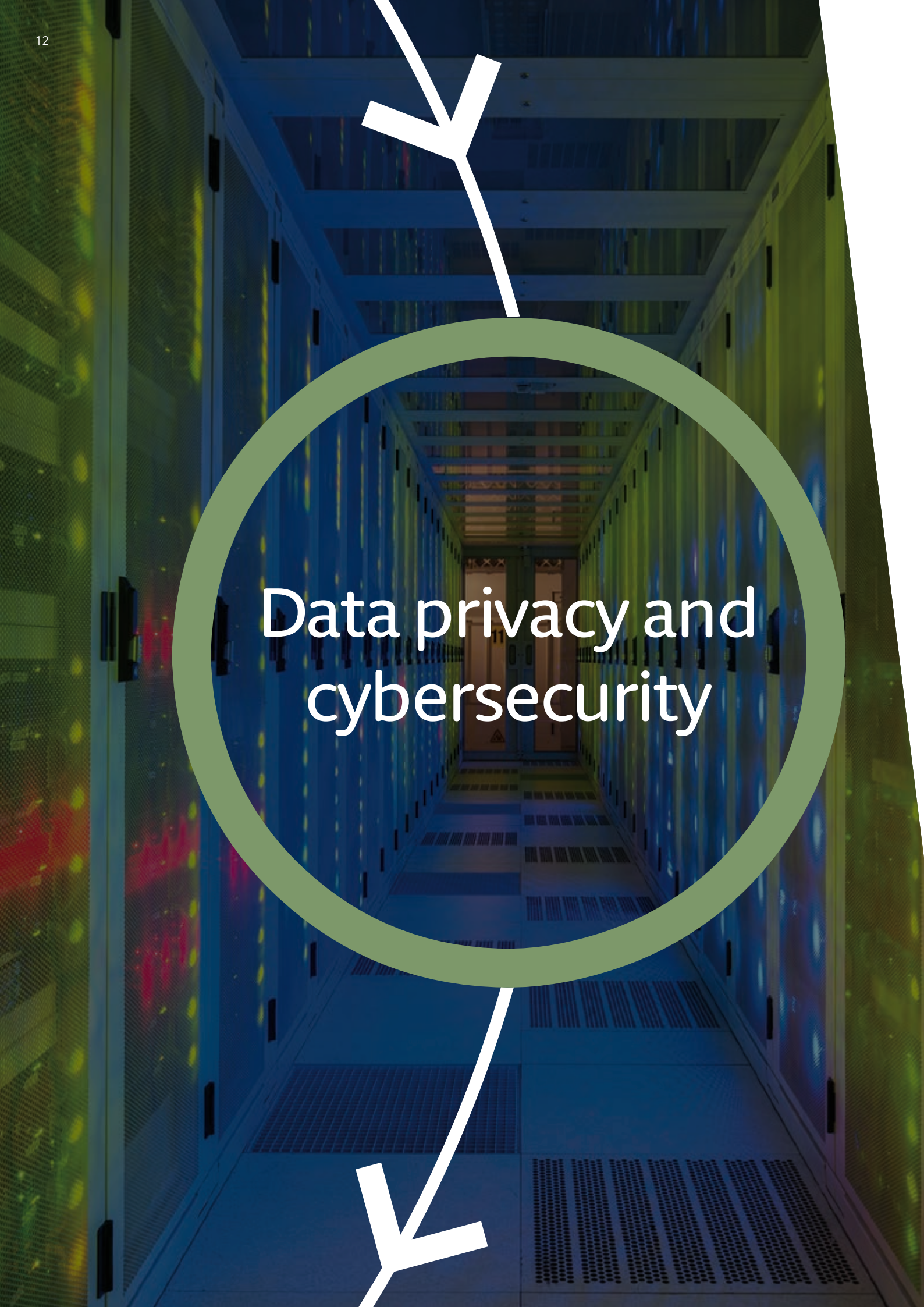
The offences can be committed in relation to tax evasion and facilitation in the UK or, in certain circumstances, abroad.

Ensuring you have the right prevention procedures in place creates a defence against liability. Our tax, disputes, and fraud specialists work together to advise companies and funds on implementing and maintaining robust procedures, tailored to their unique circumstances.

> "Flexible and effective service for clients faced with cross-border investigations into allegations of bribery and money laundering."
>
> *Chambers UK, 2019: Financial Crime*

How we can help you

- We carry out risk assessments and prepare code of conduct statements and policies and help to design procedures.
- We advise on complying with the UK Proceeds of Crime Act, Money Laundering Regulations and UK Criminal Finances Act and on police and investigatory agency powers, data protection, whistleblowing issues and legal privilege.
- We advise on money laundering risk and on obtaining 'consent' to transact.
- We undertake internal investigations and represent clients in external investigations conducted by UK agencies. We can call on advice from former UK regulators and prosecutors.
- We assess domestic and international tax evasion and facilitation risk, calling on the expertise of our specialist tax investigations team.
- We work with and manage compliance consultants.



Data privacy and cybersecurity

Our leading Privacy and Cybersecurity team members know the GDPR inside out. Our input has been actively sought by the European Commission both as part of the policy formulation process and the drafting of the GDPR, and we have worked closely with EU institutions which are part of the legislative process. We offer practical, hands-on experience of advising international businesses on compliance with GDPR, the Data Protection Act and e-Privacy, the implementation of appropriate policies and procedures and dealing with any breach incidents.

For many organisations, data has become a business asset of strategic importance. Personal data can help develop new technologies or personalise marketing campaigns, but subject to strict privacy laws.

Understanding whether a business has the rights to continue or increase commercial benefits derived from data, or that it has appropriate compliance in place to mitigate regulatory risk, may be a core priority for a buyer or investor.

Cybersecurity is the focus of a number of global regulatory bodies including the SEC and European data protection, financial and other regulators. As such, private equity and debt fund managers should be alert to the implications of a breach. Given the online and global nature of data in the modern world, the ramifications of a cybersecurity breach can be huge. Such ramifications can be both financial (as a result of litigation and/or remediation as well as significant regulatory fines) or perhaps more importantly, reputational, affecting the fund manager, investors and any portfolio company subject to a cybersecurity breach.

A cyber-attack or security breach can be hugely damaging. As such a fund manager must take a holistic approach to cybersecurity risk across its entire portfolio, and not just the risks for the fund or its manager. The lack of strong cybersecurity policies and best practice can, of itself, present an indication of higher risk exposure for a company to data security breaches and cybersecurity attacks. It is therefore essential when assessing the opportunities presented by a potential investee company, to ascertain the level of understanding and preparedness to comply with privacy law and keep personal data secure. This is particularly true for any company which depends on the exploitation of personal data.

> “Excellent team of data protection and privacy specialists in the full range of issues facing clients around the world. Comprehensive understanding of the GDPR and its corporate implications, as well as extensive cross-border regulatory connections.”
>
> *Chambers UK, 2019: Data Protection & Information Law*

How we can help you

- We conduct data protection compliance audits and produce reports outlining any identified remediation actions.
- We review and update necessary data privacy accountability documentation including policies and privacy notices.
- We assist with training and awareness.
- We review and devise specific approaches to due diligence and data protection law warranties and indemnities in transaction documents.
- We draft and negotiate data protection terms in IT and commercial agreements.
- We assist in the event of a data breach incident including dealing with regulators and advise on incident preparedness.

Cartels

It is now well established that private equity fund managers can be liable for breaches of competition law (and potentially exposed to follow-on damages claims in national courts) in circumstances where they are deemed to have control or "decisive influence" over their portfolio companies (including those indirectly held or where control is shared with others). This is regardless of whether the fund manager was aware of the infringing entity's involvement in the cartel or that it has disposed of the fund's interest in the meantime.

The most serious breaches under Article 101 of the Treaty on the Functioning of the European Union and the UK domestic equivalent under Chapter I Competition Act 1998 concern horizontal arrangements between competitors such as price fixing, market sharing and other cartel behaviour. The European Commission and Member State competition authorities have also imposed significant fines on suppliers and distributors for vertical price fixing cases (i.e. resale price maintenance). Although the level of fines imposed will have as a cap 10% of the total worldwide turnover in the preceding year of business, for a private equity fund manager, the relevant turnover will include all the companies over which it has "decisive influence". In addition to administrative fines, there are also significant risks of joint and several liability alongside the infringing portfolio entity in follow-on damages actions before national courts (where a European Commission infringement decision is binding proof that the behaviour took place and was illegal).

"Decisive influence" is a complex concept. Where a shareholder has a shareholding of over 90% in an infringing subsidiary, there will be a rebuttable presumption that it has "decisive influence". Where the shareholder holds either a majority shareholding amounting to less than 90% of the shares or a minority shareholding in an infringing entity, the particular economic, organisational and legal links between the companies need to be scrutinised. Indicators of "decisive influence" are where the minority shareholder holds important veto rights over strategic decisions of the company such as the budget, the business plan, major investments or the appointment of senior management.

> "Clients highlight that the "quality of advice is excellent and it is delivered in a way that is effective - succinct, to the point, commercial and tailored to the audience."
>
> *Chambers UK 2020: Competition Law*

How we can help you

- We advise on all aspects of compliance with antitrust and competition laws.
- We carry out risk assessments (including due diligence reviews in an M&A context), and prepare compliance policies and procedures to ensure compliance with antitrust and competition laws.
- We advise on whistleblowing issues and self-reporting.
- We advise on major antitrust investigations, including investigations conducted by the U.S. Department of Justice (DOJ), the Federal Trade Commission (FTC), individual U.S. states, the European Commission, and national competition law authorities across the globe.
- We advise clients regarding investigations by sector specific regulatory authorities.
- We assist clients in responding to litigation arising from alleged anticompetitive conduct.
- We draw on the experience of former antitrust officials.

Environmental and health and safety

Not only do fund managers need to remain conscious of the penalties for failure to comply with environmental and health and safety (EHS) legislation, but also the reputational impact and the impact on value creation. Furthermore, LPs are increasingly looking to their GPs to manage and report on the EHS performance of their portfolio companies.

The extent to which EHS regulation and compliance risk impacts a portfolio company will depend considerably on the sector and geography concerned, but almost all portfolio companies will be affected to some degree, whether in terms of financial, operational and/or reputational impacts.

In broad terms, these regulatory risks comprise:

- requirements for material capex/opex to comply with environmental regulation either on-going or when a site is decommissioned or closed (e.g. to comply with conditions of an environmental permit);
- sanctions and penalties for non-compliance with environmental regulation (e.g. criminal fines for breach of UK environmental regulation, or the service of enforcement notices requiring action to be taken or operations suspended);
- legal obligations to remediate environmental damage and restore the environment (e.g. liability to clean up land contamination); and
- civil liabilities arising from legal liability for damage to the environment, human health or property.

How we can help you

- We provide specialist EHS due diligence and liability allocation support on transaction matters. We can also assist with the integration of EHS factors into investments, including the use of EHS provisions in fund terms.
- We draft and review EHS policies and standards and management procedures. We have assisted a number of clients, particularly in high-risk sectors, with the creation of organisation-wide systems to manage EHS risks.
- We have a large regulatory practice providing advice to clients on all aspects of EHS compliance, from corporate reporting to tracking and influencing legislative developments. We have experience in a number of very niche areas (such as chemicals regulation, emissions trading and F-gas quota trading).
- We support internal compliance, audit and reporting exercises. We have supported a number of funds on the application of EU and UK environmental and energy regulatory requirements across their portfolio companies.
- We can call upon a well-established network of expert contacts within environmental and safety agencies, consultancies, and other relevant industry and trade institutions.

Business and human rights

> “Sources praise the firm for its “instrumental advice in the discussion around business human rights responsibility,” further endorsing its “innovative understanding of a variety of complex issues.”
>
> *Chambers Global 2019: Business & Human Rights Law*

Would you know if a business was involved in child labour, a privacy violation, or another human rights impact? How do you identify and manage human rights risk associated with artificial intelligence? What about a business partner or supplier? If a business doesn't respect human rights, you could be open to devastating adverse publicity as well as hard legal liability.

We understand the risk associated with adverse human rights impacts and our integrated practice group builds on this foundation to provide the full spectrum of business and human rights advice for the private equity industry.

Human rights due diligence

The UN Guiding Principles on Business and Human Rights (UNGPs) set out the expectation that all businesses respect human rights. To meet this expectation, businesses should have in place appropriate policies and procedures, including a policy commitment to respect human rights; a human rights due diligence process to identify, prevent and mitigate and account for how they address human rights impacts, across their corporate structure, including in their supply chain; and processes to enable remediation of any adverse human rights impacts which they cause or to which they contribute.

Traditionally, the UNGPs have been seen as "soft" law. However, increasingly elements are reflected in "hard" law and there is the prospect of legal liability for companies which do not respect human rights. Courts around the world are extending their jurisdiction to human rights impacts which occur extra-territorially and throughout a business's value chain. Businesses which don't respect human rights are open to criminal and civil liability, not to mention devastating adverse publicity.

The impact of national legislation such as the UK Modern Slavery Act 2015

Under Section 54 of the UK Modern Slavery Act ("MSA"), any organisation carrying on business in the UK with an annual turnover of £36 million or more is required to report publically on the steps which it has taken to prevent slavery and trafficking in its operations and supply chain (including where these are overseas).

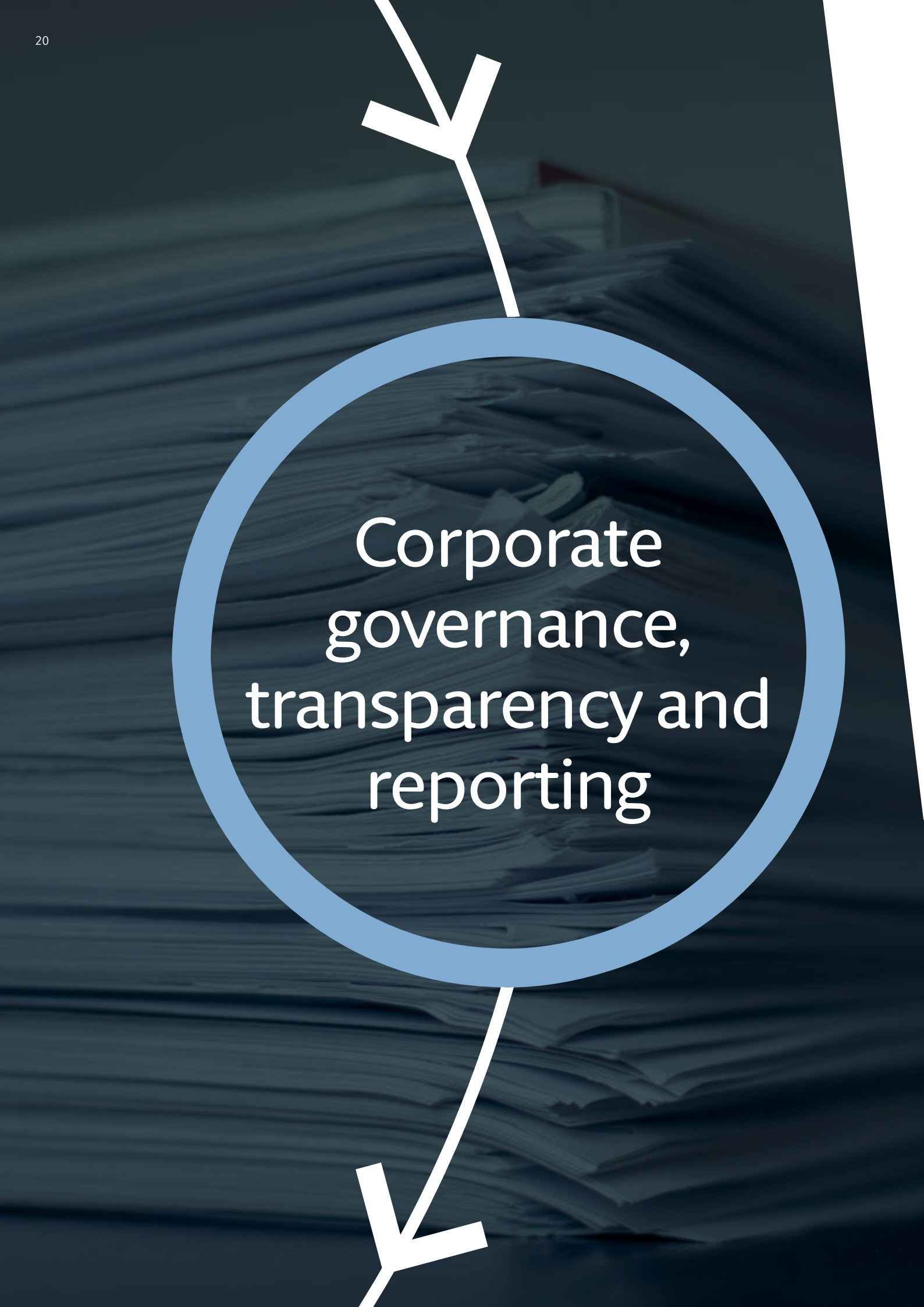
There is an expectation that a reporting entity is able to show improvements from year to year against certain criteria. Although reporting against these criteria is currently not mandatory, a Parliamentary inquiry published in January 2019 recommended making these steps mandatory and introducing sanctions for non-compliance. The steps which an organisation takes pursuant to the MSA can be used to report under various other, similar pieces of legislation elsewhere (e.g. the California Transparency in Supply Chains Act, the Australian MSA etc.).

Investigations and Dispute Resolution

We have acted in some of the leading disputes in the human rights field, wherever and however they were brought: in the U.S. under the Alien Tort Claims Act, in English parent company liability cases, and in other courts exercising universal jurisdiction over alleged complicity in war crimes.

How we can help you

- We provide the full spectrum of business and human rights advice, including:
  - preventing and reporting on modern slavery
  - supply chain transparency
  - human rights due diligence
  - risk assessment and deal approvals
  - human rights investigations and crisis management
  - managing the remediation of harm, including operational-level grievance mechanisms
  - defending human rights-related claims, wherever, and however, they are brought



Corporate governance, transparency and reporting

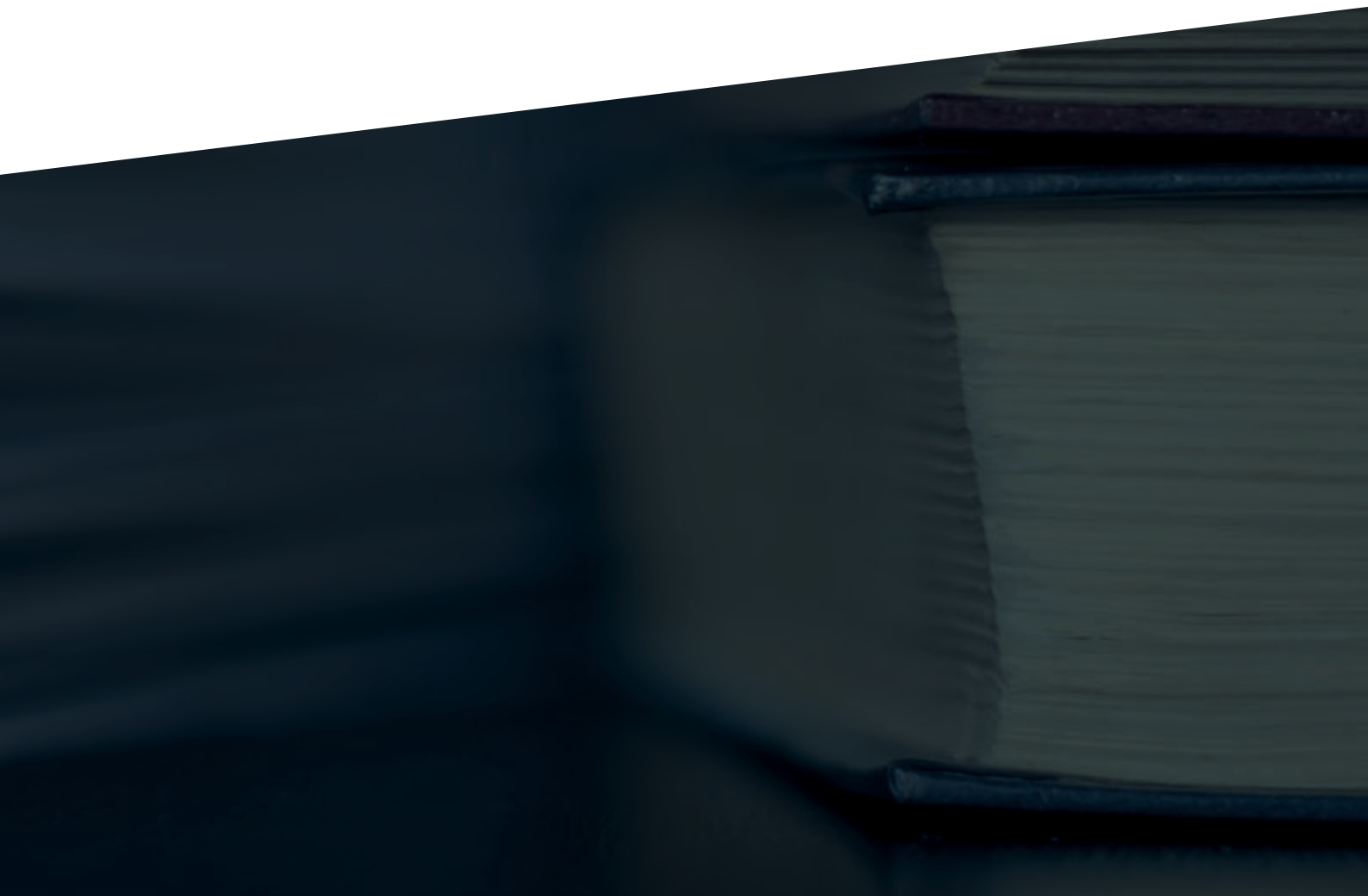
Private equity funds, debt funds and other asset managers are increasingly subject to calls for more transparency and reporting as well as calls for improved corporate governance. The calls for more transparency and reporting and improved corporate governance come from both regulators and investors, resulting in the application of statutory and non-statutory regimes to private equity and debt fund managers.

In addition to the transparency, reporting and corporate governance requirements aimed specifically at the private equity industry, portfolio companies are also subject to transparency, reporting and corporate governance provisions applying to companies generally.

> Top ranked for Corporate Governance
>
> *Legal 500 UK, 2019: Risk Advisory – Corporate Governance*

How we can help you

- We advise on all aspects of the disclosure and corporate governance regimes applicable to private equity and other asset managers.



Your contacts

Nicholas Holman
Funds and Fund Regulation
Partner, London
T +44 20 7296 5180
nicholas.holman@hoganlovells.com

Michael Thomas
Financial Regulation
Partner, London
T +44 20 7296 5081
michael.thomas@hoganlovells.com

Crispin Rapinet
Anti-Bribery and Corruption
Partner, London
T +44 20 7296 5167
crispin.rapinet@hoganlovells.com

Rupert Shiers
Criminal Finances Act 2017
Partner, London
T +44 20 7296 2966
rupert.shiers@hoganlovells.com

Aline Doussin
Sanctions
Partner, London
T +44 20 7296 2961
aline.doussin@hoganlovells.com

Claire Lipworth
Anti-Money Laundering
Partner, London
T +44 20 7296 2982
claire.lipworth@hoganlovells.com

Nicola Fulford
Data Privacy and Cybersecurity
Partner, London
T +44 20 7296 2988
nicola.fulford@hoganlovells.com

Suyong Kim
Cartels
Partner, London
T +44 20 7296 2301
suyong.kim@hoganlovells.com

Kevin O'Connor
Environmental and Health and Safety
Senior Associate, London
T +44 20 7296 5376
kevin.oconnor@hoganlovells.com

Alicante
Amsterdam
Baltimore
Beijing
Birmingham
Boston
Brussels
Budapest*
Colorado Springs
Denver
Dubai
Dusseldorf
Frankfurt
Hamburg
Hanoi
Ho Chi Minh City
Hong Kong
Houston
Jakarta*
Johannesburg
London
Los Angeles
Louisville
Luxembourg
Madrid
Mexico City
Miami
Milan
Minneapolis
Monterrey
Moscow
Munich
New York
Northern Virginia
Paris
Perth
Philadelphia
Riyadh*
Rome
San Francisco
Sao Paulo
Shanghai
Shanghai FTZ*
Silicon Valley
Singapore
Sydney
Tokyo
Ulaanbaatar*
Warsaw
Washington, D.C.
Zagreb*

*Our associated offices
Legal Services Centre: Berlin

www.hoganlovells.com